Bird & Bird

# Defence & Security Procurement 2021 Edition

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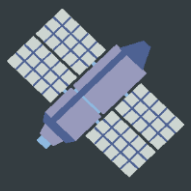

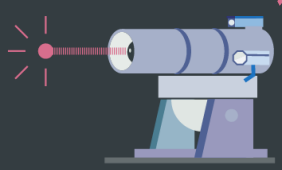

*Bird & Bird's International Defence & Security team are delighted to have contributed to the global 2021 edition of 'Getting the Deal Through: Defence & Security Procurement'.* Our *team has written the chapters for France, Germany, Italy, Poland and the UK and Elizabeth Reid is contributing editor for the publication.*

*This annual publication provides excellent expert analysis of how government procurement works in this highly regulated sector and is an ideal tool for in-house counsel and commercial practitioners.*

*Technology continues to disrupt this sector: as the assets and services being procured become more complex, a fit for purpose procurement process is vital for both the procuring entities and suppliers. Our experts analyse all the hot topics, including single source regulations, competitive processes, intellectual property, standard form contracts, anti-bribery & corruption, export controls and sanctions. They also explore some of the wider macroeconomic factors driving change: Covid-19, Brexit and a free trade agreement, and the election of a new US president.*

*Please get in touch if you would like to hear more about how our international team can help you.*

# Defence & Security Procurement 2021

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LEXOLOGY
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# Defence & Security Procurement

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Contributing editor
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Lexology Getting The Deal Through is delighted to publish the fifth edition of *Defence & Security Procurement*, which is available in print and online at www.lexology.com/gtdt.

Lexology Getting The Deal Through provides international expert analysis in key areas of law, practice and regulation for corporate counsel, cross-border legal practitioners, and company directors and officers.

Throughout this edition, and following the unique Lexology Getting The Deal Through format, the same key questions are answered by leading practitioners in each of the jurisdictions featured. Our coverage this year includes a new chapter on Sweden.

Lexology Getting The Deal Through titles are published annually in print. Please ensure you are referring to the latest edition or to the online version at www.lexology.com/gtdt.

Every effort has been made to cover all matters of concern to readers. However, specific legal advice should always be sought from experienced local advisers.

Lexology Getting The Deal Through gratefully acknowledges the efforts of all the contributors to this volume, who were chosen for their recognised expertise. We also extend special thanks to the contributing editor, Elizabeth Reid of Bird & Bird.

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# Global Overview

**Elizabeth Reid**

Bird & Bird

Upon reaching the end of a tumultuous 2020, we look ahead to what promises to be another year of global upheaval. As the world struggles to emerge from the covid-19 crisis – a hugely economically destructive and impactful event – international threats to security, privacy and freedom of both expression and information are rising. With social media becoming increasingly weaponised, the hurling of digital insults can only continue for so long before fights spill over into cyber attacks, data thefts or physical military conflicts. As a result, there is a huge pressure on countries to reinforce innovative efforts and research and development to stay ahead of the defence game.

Whilst defence manufacturing held up reasonably well during the covid-19 crisis, the pandemic has caused nations' economies to drastically slow and many countries' gross domestic products to crash. The World Bank has projected the global economy will shrink by 5.2% in 2020. While countries regroup following the repercussions of the pandemic, priorities will likely move towards other public services and defence budgets will likely suffer. While the severe economic damage will probably lead to reduced government spending in 2021, the global geopolitical situation means some countries are still prioritising defence. For example, in November, the UK's prime minister Boris Johnson revealed a £16.5bn increase in defence spending over the next four years – the largest practical increase in the country's defence budget since Margaret Thatcher's tenure.

With the Brexit transition period ending on 31 December 2020, and by reaching a free trade agreement (the EU–UK Trade and Cooperation Agreement), which does not cover cooperation on foreign policy, external security and defence, the questions remain as to what the UK's future defence and security relationship with the EU will look like, and in which areas of defence and security policies industry partners will still be able to coordinate their efforts. Even though the free trade agreement has been concluded, Brexit is likely to cause delay and disruption for any cross-border trade with the UK, both with and outside the EU.

Meanwhile, across the Atlantic, the 2020 United States presidential election was one of the most significant for decades in terms of foreign policy. President-elect Joe Biden's administration is likely to be less boisterous than Trump's, and will certainly promote globalisation. It is expected that Biden will strengthen US relations with Nato countries, Japan and South Korea, and that he will work towards reducing the tension with China and Russia that mounted under Trump's leadership.

With international conflict progressing beyond the confines of land and air, the defence and security sector inevitably continues to involve the procurement of high-value, technologically complex, mission-critical assets. Major military powers are showing a hugely increased interest in space – with a particular regard to the need to ensure the security of satellites, given Russian and Chinese efforts to develop anti-satellite capabilities. Satellites govern bank transactions, traffic systems, national power grids and even elements of governments' coronavirus responses (eg, logistics of rolling out vaccines). In the UK, a new National Cyber Force – which recruits personnel from GCHQ, the Ministry of Defence, the Secret Intelligence Service (MI6) and the Defence Science and Technology Laboratory – is working alongside GCHQ's National Cyber Security Centre, and a new 'Space Command' is to be formed under the Ministry of Defence. These moves came less than a year after Trump, arguing that "space is the world's new war-fighting domain", announced the creation of the United States Space Force and France launched its Space Defence Strategy in 2019, and attached a major space command to its existing air force to create the French Air and Space Force.

The covid-19 crisis has highlighted how the use of propaganda and manipulated influence is creating new and fast-developing challenges for policymakers. The above geopolitical aspects, supported by a pandemic that has shifted the focus of most economies to public health and containment, may mean that defence and security procurement will decrease globally in 2021. In the short term, procurement programmes are likely to be affected by the challenges posed by the pandemic for defence companies, such as cash flow issues and supply chain disruptions (particularly for those defence companies impacted by the severe downturn in the aerospace sector). In the long term, procurement budgets may need to prioritise expenditure on specific programmes. It is vital that procurement entities are able to make full use of relevant commercial innovations.

Therefore, we are pleased to present the fifth annual edition of *Lexology Getting the Deal Through – Defence and Security Procurement*.

# Canada

**Ben Mills**
Conlin Bedard LLP

## LEGAL FRAMEWORK

### Relevant legislation

1 | What statutes or regulations govern procurement of defence and security articles?

The procurement of goods and services for defence and security is governed by laws and regulations that pertain to procurement law generally and to security requirements specifically associated with the goods and services that are typically identified as being related to defence and security.

At the federal level, laws and regulations of general application include the Government Contracts Regulations and any applicable policies promulgated by the Treasury Board and Public Services and Procurement Canada. The government procures defence and security articles in a manner similar to other goods and services and uses a competitive solicitation process. While Canada has exempted security and defence-related procurements from the procurement disciplines of international trade agreements (such as the World Trade Organization Agreement on Government Procurement (GPA) and the Comprehensive Economic Trade Agreement (CETA)), Canada nonetheless conducts such procurement in a manner consistent with those agreements by using competitive solicitation processes that (subject to security concerns) are open to foreign suppliers. Absent a specific exemption being applied on the basis of, for example, national security, defence-related procurements are subject to the Canadian Free Trade Agreement (CFTA). The CFTA is a domestic trade agreement between Canada's federal, provincial and territorial governments. It includes disciplines similar to those set out in the GPA and CETA. However, only Canadian suppliers may challenge non-adherence to those disciplines.

Laws and regulations that specifically apply to the procurement of defence and security articles include the Defence Production Act, the Controlled Goods Regulations and the Security of Information Act.

The Defence Production Act address two key issues.

It grants the Minister of Public Services and Procurement Canada (whose department was formerly known as the Department of Public Works and Government Services) significant ministerial oversight of 'defence contracts' and powers to secure goods, technology and services necessary for the defence of Canada. For example, the Minister has the power to review amounts paid under a defence contract to ensure that a defence contractor is not being paid amounts 'in excess of the fair and reasonable cost of performing the contract together with a fair and reasonable profit'. Also, the Minister has the power to relieve a contractor 'from any claims, actions or proceedings for the payment of royalties for the use or infringement of any intellectual property rights' and to pay the holder of such rights 'reasonable compensation' for the infringement.

It creates the legislative framework and statutory offences with respect to the handling of 'controlled goods' pursuant to the Controlled Goods Regulations. The Controlled Goods Regulations, which are made under the Defence Production Act, govern the transfer of 'controlled goods'. Controlled goods are those listed in the Schedule to the Defence Production Act, which lists various articles and associated data that have military applications. Pursuant to the Controlled Goods Regulations, a firm that handles controlled goods must register with the government's Industrial Security Directorate and handle and transfer such goods in the manner prescribed by the regulations. Subject to certain limited exemptions, a firm may only grant access to persons registered with the Industrial Security Directorate.

The Security of Information Act is legislation designed to ensure that classified or protected information is safeguarded against unauthorised disclosure. Pursuant to the Security of Information Act, the government has implemented a series of policies, procedures and protocols associated with accessing, storing and handling of classified or protected information, which are administered by the Industrial Security Directorate.

### Identification

2 | How are defence and security procurements identified as such and are they treated differently from civil procurements?

Defence and security procurements are not identified as such. However, the solicitation documents pertaining to defence and security procurements will reference requirements that are unique to defence and security procurements, such as being subject to the Defence Production Act, Controlled Goods Regulations and security requirements.

### Conduct

3 | How are defence and security procurements typically conducted?

Defence and security procurements are conducted in the same manner as other procurements in that the government will use a request for proposal process to solicit bids. Complex procurements or those that involve access to classified information may involve an initial vetting of potential suppliers through a 'letter of interest' process, whereby the government requests that potential suppliers indicate their interest in participating in the procurement and may conduct an initial assessment of potential suppliers to ensure that bidders meet minimum requirements.

### Proposed changes

4 | Are there significant proposals pending to change the defence and security procurement process?

The procurement of sophisticated and expensive defence goods, such as ships, aircraft and vehicles, is complex. The government continues to look at ways of making the process more efficient and

less time-consuming. Also, the government continues to assess how defence procurement can be leveraged to meet socioeconomic goals, such as increased domestic employment or subcontracting or business opportunities for Canadian-based business. However, defence and security procurements have not changed in a material way in recent years.

**Information technology**

5 | Are there different or additional procurement rules for information technology versus non-IT goods and services?

There are no different or additional procurement rules for information technology. However, the contract resulting from the procurement will include provisions regarding ownership of intellectual property, which may be a specific concern to suppliers of information technology.

**Relevant treaties**

6 | Are most defence and security procurements conducted in accordance with the GPA or other treaty-based procurement rules, or does this jurisdiction commonly use the national security exemption to procure them?

Most defence and security procurements are conducted in a manner that accords with the GPA and other treaty-based procurement rules (such as those in CETA) in the sense that the solicitation documents reflect the procedural requirements of treaty-based procurement rules (such as including a clear statement of work, evaluation criteria, etc).

However, most defence and security procurements conducted in Canada are exempt from the GPA as defence and security goods are not included in Canada's schedule to the GPA, CETA and other international trade agreements. As a result, the non-discrimination and national treatment provisions of the GPA, CETA and other international trade agreements do not apply. Equally, the procurement dispute process under such treaties does not apply.

Having said that, the government is a party to the CFTA with provincial and territorial governments. Absent the application of a specific exemption (such as national security), CFTA applies to the procurements for defence and security items. On that basis, CFTA prescribes the minimum procedural requirements for a procurement of defence and security articles and services and affords national and non-discrimination treatment to 'Canadian Suppliers'. Equally, 'Canadian Suppliers' have standing to bring a dispute to the Canadian International Trade Tribunal with respect to an alleged breach of the CFTA. The threshold to be considered a 'Canadian Supplier' is low and is defined as being 'a supplier that has a place of business in Canada' at which it 'conducts activities on a permanent basis that is clearly identified by name and accessible during normal business hours'. 'Foreign suppliers' often open an office in Canada as a means of supporting bidding efforts and also to qualify as 'Canadian suppliers'.

## DISPUTES AND RISK ALLOCATION

**Dispute resolution**

7 | How are disputes between the government and defence contractor resolved?

In the context of a dispute regarding the procurement process, a supplier that qualifies as a Canadian supplier has standing under the Canadian Free Trade Agreement (CFTA) to bring a procurement complaint to the Canadian International Trade Tribunal, which is Canada's bid dispute resolution authority. The government may invoke a 'national security exemption' that has the effect of precluding challenges under the CFTA or any other trade agreement.

Also, suppliers that cannot advance a complaint before the Canadian International Trade Tribunal owing to standing or jurisdictional considerations, may seek judicial review of the procurement decision by making an application to the Federal Court of Canada.

In a situation where the dispute relates to the contract between a successful bidder and the government, disputes will be resolved in accordance with any applicable contract provisions (such as mediation or arbitration) or otherwise resolved through the domestic court process applicable to contract disputes.

8 | To what extent is alternative dispute resolution used to resolve conflicts? What is typical for this jurisdiction?

Government contracts often include the potential use of alternative dispute resolution processes. However, these are normally only available with the consent of the government. Without such provisions or in the event that the government does not consent to using alternative dispute mechanisms, the typical jurisdiction for resolution of contract disputes would be the superior court of a province, such as the Ontario Superior Court of Justice. The Federal Court of Canada has concurrent (but not exclusive) jurisdiction over contract disputes involving the government as a defendant. The Federal Court of Canada does not have jurisdiction over disputes between contractors and subcontractors. Put another way, a contractor may start a proceeding against the government in Federal Court or, alternatively, in the superior court of a province. All other contract claims would normally be advanced in the superior court of a province.

**Indemnification**

9 | What limits exist on the government's ability to indemnify the contractor in this jurisdiction and must the contractor indemnify the government in a defence procurement?

Normally, the government limits its liability to a contractor to the full value of the contract. This would preclude claims for amounts that exceed the contract value.

It is only in rare circumstances that the government would put a limit on the contractor's liability. Often the government will seek guarantees from a contractor's parent company to ensure contractual performance.

**Limits on liability**

10 | Can the government agree to limit the contractor's liability under the contract? Are there limits to the contractor's potential recovery against the government for breach?

Yes, the government may agree to limit the contract's liability under the contract. However, the government tends to be reluctant to do so.

There are no statutory or regulatory limits to the contractors' potential recovery against the government for breach. However, the government's standard contracting documents limit liability to a stated amount, which is often identified as limitation of expenditure or limitation of liability.

**Risk of non-payment**

11 | Is there risk of non-payment when the government enters into a contract but does not ensure there are adequate funds to meet the contractual obligations?

The contracting procedures used by the government require Treasury Board approval for major contracts, which entails that funds have been budgeted and allocated to meet the terms of payment. The government is not known to have defaulted on a payment owing to a lack of funds.

**Parent guarantee**

12 | Under what circumstances must a contractor provide a parent guarantee?

The government may seek a parent guarantee in circumstances where there is a concern regarding the contractor's financial capability to fulfil the contract requirements. The assessment of a contractor's financial capability is based on a review of its audited financial statements and other relevant information. In a situation where the contractor is a subsidiary of a larger corporate structure, the government will often require the parent organisation provides a guarantee, particularly with respect to complex or major procurements.

## DEFENCE PROCUREMENT LAW FUNDAMENTALS

**Mandatory procurement clauses**

13 | Are there mandatory procurement clauses that must be included in a defence procurement contract or that will be read into the contract regardless of their actual inclusion?

At the most basic level, the Government Contracts Regulations require that Canada solicits bids for government contracts by giving public notice or inviting suppliers to participate.

Also, the Government Contracts Regulations include terms that are deemed to be included in any government contract such as:

- the contractor has not paid any contingency fee to obtain the contract;
- the contractor's accounts and records shall be subject to audit;
- the contractor has not committed any specified offences; and
- the Access to Information Act applies to information received under the contract.

**Cost allocation**

14 | How are costs allocated between the contractor and government within a contract?

The allocation of costs between the contractor and government will vary depending on the contract.

For example, in the context of service type contracts that include the provision of commodity-type goods that can vary in costs over time (such as fuel), the government may reimburse the contractor for such costs without any markups.

Also, in certain circumstances, the government may use a 'cost-plus' model where the contractor is compensated for its costs plus a reasonable markup for profit. In such circumstances, standard government contracting provisions apply to define what is an appropriate 'cost' for reimbursement.

**Disclosures**

15 | What disclosures must the contractor make regarding its cost and pricing?

This depends upon the contract. If a 'cost-plus' model is used, then there is significant disclosure regarding the contractor's costs and pricing. This is most often an issue in the context of contracts that have a large service component (such as retrofitting and repairs).

Also, standard government contracting clauses and legislation (such as the Defence Production Act) allow the government to conduct audits.

**Audits**

16 | How are audits of defence and security procurements conducted in this jurisdiction?

Audits are conducted by government officials pursuant to accounting and audit rules of general application, and pursuant to any applicable contract provisions.

**IP rights**

17 | Who gets the ownership rights to intellectual property created during performance of the contract? What licences are typically given and how?

The Treasury Board's Policy on Title to Intellectual Property Arising Under Crown Procurement Contracts provides that:

> *The objective of this Policy is to enhance Canada's economic growth by increasing commercialization of Intellectual Property. To this end, the contractor is to own the rights to Foreground Intellectual Property created as a result of a Crown Procurement Contract.*

This position is subject to certain exceptions and exemptions.

'Foreground intellectual property' means intellectual property 'first conceived, developed, produced or reduced to practice as part of the work under a Crown Procurement Contract'. The government would maintain a broad licence to any foreground intellectual property.

A variety of exceptions and exemptions exists with regard to this general position, including national security requirements; statutory and regulatory requirements or prior obligations of the government regarding the intellectual property at issue; and where the purpose of the procurement contract is incompatible with the contractor owning the foreground intellectual property, such as when the purpose of the contract is to generate knowledge and information for public dissemination or relates to the development of intellectual property owned by the government.

**Economic zones**

18 | Are there economic zones or other special programmes in this jurisdiction commonly utilised by foreign defence and security contractors for financial or other procurement related benefits?

No.

**Forming legal entities**

19 | Describe the process for forming legal entities, including joint ventures, in this jurisdiction.

Legal entities, such as corporations, are formed pursuant to the Business Corporations Acts in effect throughout Canada's various jurisdictions (ie, federal, provincial and territorial). Joint ventures may take on the form of a corporate entity or may be formulated on the basis of a contractual relationship.

**Access to government records**

20 | Are there statutes or regulations enabling access to copies of government records? How does it work? Can one obtain versions of previous contracts?

The Access to Information Act allows a person to request documents in the possession of departments and agencies of the government. The process for making a request is simple. A requester completes a form describing the documents or information sought and the office in the government department where the documents or information are likely

to be stored. An initial nominal payment is required with the request. A further fee for making reproductions may also apply.

Contracts (or redacted portions thereof) may be exempt from disclosure on various grounds, including that the disclosure of the information would be contrary to national security interests, include personal information or include third-party information such as trade secrets, confidential commercial information or information the disclosure of which would prejudice the third party's competitive position.

The Access to Information process has been criticised as being slow in providing access to documents.

**Supply chain management**

21 What are the rules regarding eligible suppliers and supply chain management and anti-counterfeit parts for defence and security procurements?

There are no rules of general application. This would be addressed on a contract-by-contract basis.

## INTERNATIONAL TRADE RULES

**Export controls**

22 What export controls limit international trade in defence and security articles? Who administers them?

Exports from Canada are subject to the Export and Import Permits Act, which authorises the creation of an Export Control List. The exportation of articles listed on the Export Control List must be specifically authorised by a permit issued by the Minister of Global Affairs.

**Domestic preferences**

23 What domestic preferences are applied to defence and security procurements? Can a foreign contractor bid on a procurement directly?

A foreign contractor may bid on a defence and security procurement directly. Subject to security concerns, defence and security procurements are generally open.

However, major defence and security procurements require the successful bidder to commit to Industrial and Technological Benefits (ITB), which generally provide that the successful bidder is to make certain investments in Canada or carry out certain work in Canada. The ITB programme is designed to foster investment in Canada in specified sectors, including manufacturing, aerospace and technology. Normally, the ITB commitment is equivalent to the value paid by Canada to the successful bidder.

**Favourable treatment**

24 Are certain treaty partners treated more favourably?

No.

**Sanctions**

25 Are there any boycotts, embargoes or other trade sanctions between this jurisdiction and others?

Yes, the government has imposed trade sanctions on various jurisdictions through the United Nations Act (which implements United Nations Security Council sanctions) and the Special Economic Measures Act (which implements autonomous sanctions issued by the government of Canada). Also, Canada adopted the Justice for Victims of Corrupt Foreign Officials Act, which allows Canada to impose an asset freeze and a dealings prohibition against individuals who, in the opinion of the Governor in Council, are responsible for or complicit in gross violations of internationally recognised human rights or are foreign public officials or their associates, who are responsible for or complicit in acts of significant corruption.

Measures under the United Nations Act and the Special Economic Measures Act are currently in place with respect to the following jurisdictions:

- Central African Republic;
- the Democratic Republic of the Congo;
- Eritrea;
- Iran;
- Iraq;
- Lebanon;
- Libya;
- Nicaragua;
- Myanmar;
- North Korea;
- Russia;
- Somalia;
- South Sudan;
- Sudan;
- Syria;
- Ukraine (linked to Russia's ongoing violations of Ukraine's sovereignty and territorial integrity);
- Venezuela;
- Yemen; and
- Zimbabwe.

Canada has also taken measures against specific individuals and groups on the basis of their activities or associations, such as terrorist entities, including Al-Qaida and the Taliban.

**Trade offsets**

26 Are defence trade offsets part of this country's defence and security procurement regime? How are they administered?

Yes, defence trade offsets are part of Canada defence and security procurement regime. The government has adopted the ITB Policy. The ITB programme is administered by Industry Canada. Under the ITB Policy, contractors awarded defence procurement contracts are required to undertake business activities in Canada, equal to the value of the contract. Bidders are required to articulate the proposed business activities in their respective proposals submitted in response to the procurement and bids are evaluated on the basis of the 'value proposition' that the bidder proposes to Canada at the time of the bid. After a contract is awarded, the contractor is required to start fulfilling its commitments and to identify further business activities in Canada, as may be required to meet its overall ITB obligation (ie, 100 per cent of contract value). For example, if contractor's value proposition includes specific commitments and activities equal to 75 per cent of the contract value, it will be required to identify additional activities equal to 25 per cent of the contract value after the contract is awarded.

## ETHICS AND ANTI-CORRUPTION

**Private sector appointments**

27 When and how may former government employees take up appointments in the private sector and vice versa?

Former government employees are subject to restrictions associated with their employment. Generally, former government employees must undergo a 'cooling-off' period before they may join a private-sector employer that has significant dealings with government.

The government hires employees from the private sector. Such employees are subject to conflict-of-interest guidelines.

**Addressing corruption**

28 | How is domestic and foreign corruption addressed and what requirements are placed on contractors?

Domestic and foreign corruption is addressed through criminal laws of general application, which include the Criminal Code and the Corruption of Foreign Public Officials Act. Also, the government has adopted the Integrity Regime, which is a set of contractual provisions and associated policies (such as the Ineligibility and Suspension Policy) that have the effect of prohibiting bidders and contractors that have been convicted of specific offences from participating in procurements. The offences that may result in disqualification range from offices related to the participation in a criminal organisation, fraud against the government or bid rigging. Disqualification may result from the commission of an offence as articulated as being part of Canada's domestic law or a foreign equivalent to a listed domestic offence.

**Lobbyists**

29 | What are the registration requirements for lobbyists or commercial agents?

Lobbyists or commercial agents are required to register under lobbyist registry legislation. With respect to procurements conducted by the government, the applicable legislation is the Lobbying Act. The Lobbying Act requires lobbyist and commercial agents to file a registration identifying themselves, their clients, the topic of their lobbying activity and the government offices or officials that are being lobbied.

**Limitations on agents**

30 | Are there limitations on the use of agents or representatives that earn a commission on the transaction?

Yes. Pursuant to the Lobbying Act and standard contracting provisions, the paying of a commission to a third-party agent or representative is prohibited.

## AVIATION

**Conversion of aircraft**

31 | How are aircraft converted from military to civil use, and vice versa?

Not applicable.

**Drones**

32 | What restrictions are there on manufacture and trade of unmanned aircraft systems or drones?

Unmanned aircraft systems or drones for military purposes are subject to export and import controls.

## MISCELLANEOUS

**Employment law**

33 | Which domestic labour and employment rules apply to foreign defence contractors?

Domestic labour and employment rules apply to work done in Canada.

Pursuant to the Federal Contractors Program, contractors who bid on an initial goods and services contract, a standing offer, or a supply arrangement estimated at C$1 million or more (including applicable taxes) with the government must first certify their commitment to implement employment equity by signing the Agreement to Implement Employment Equity prior to contract award. Once an eligible contract is awarded to the contractor, the contractor is then required to meet Federal Contractors Program requirements, which include collecting of information regarding employment equity, carrying out a workforce analysis, establishing short- and long-term goals with respect to employment equity, and make reasonable progress and efforts in reaching those goals.

**Defence contract rules**

34 | Are there any specific rules that contractors, foreign or domestic, are bound by in defence contracts?

Not applicable.

35 | Do contractors avail themselves of these rules when they perform work exclusively outside of the jurisdiction?

Not applicable.

**Personal information**

36 | Must directors, officers or employees of the contractor provide personal information or certify that they fulfil any particular requirements to contract with a government entity?

The review of personal information of directors, officers and employees occurs in three contexts. First, to the extent that a security requirement applies to access sensitive or classified information either at the bidding stage or under the resulting contract, directors, officers or employees may be required to undergo a security check. Second, a security check is generally required to handle goods or technical information that are subject to the Controlled Goods Regulations. Third, the government has adopted the integrity regime, which consists of various contractual provisions that require bidders and contractors to certify that the bidder, contractor or related entities have not been convicted or charged with specified offences, which range from being part of a criminal organisation to competition law offences to frauds against the government.

**Licensing requirements**

37 | What registration or licensing requirements exist to operate in the defence and security sector in the jurisdiction?

There are no registration or licensing requirements that generally pertain to the defence and security sector as such. However, registrations may be required with respect to the handling of certain goods and technical data. For example, pursuant to the Controlled Goods Regulations, a company handling military-type goods or technical data is required to register with the Industrial Security Directorate and maintain a Controlled Goods Registration. Also, individuals who have access to classified or protected information and establishments that house such information will have to undergo a security assessment and adhere to relevant policies administered by the Industrial Security Directorate.

**Environmental legislation**

38 | What environmental statutes or regulations must contractors comply with?

Contractors are expected to comply with environmental statutes and regulations of general application. Environmental legislation exists at both the federal level of government and the provincial or territorial

level of government. As such, legislative and regulatory requirements depend on the jurisdiction in which the work is being conducted. As a general example, contractors would be expected to comply with the Canadian Environmental Protection Act and environmental legislation applicable in the provinces or territories in which they operate such as, for example, the Ontario Environmental Protection Act.

### 39 | Must companies meet environmental targets? What are these initiatives and what agency determines compliance?

At present, companies are not required to meet specific environmental targets. They are expected to meet any environmental laws of general application for work that is being conducted in Canada. The government has adopted the Policy on Green Procurement. This policy requires the procuring entity to consider the environmental impact of the procurement and to include measures in any resulting contract that lessen any adverse environmental impacts and, to the extent such measures are included, the enforcement becomes an issue of contract law.

### 40 | Do 'green' solutions have an advantage in procurements?

Green solutions do not have an advantage unless they are evaluated as part of the evaluation criteria expressly included in the solicitation documents.

## UPDATE AND TRENDS

**Key developments of the past year**

### 41 | What were the key cases, decisions, judgments and policy and legislative developments of the past year?

Canada amended the Canadian International Trade Tribunal Procurement Inquiry Regulations. The amendments remove the Tribunal's jurisdiction to conduct inquiries into procurement complaints in circumstances where the government has exempted the procurement from the application of the trade agreements on the basis of a national security exemption. Prior to the regulatory amendments, the Tribunal maintained jurisdiction to conduct an inquiry into procurements that were subject to national security exemptions. In such cases, the Tribunal would determine the ambit of the national security exemption at issue and then consider whether the Tribunal could inquire into, and provide a remedy regarding, the subject matter of the procurement complaint in light of the national security exemption. If so, the Tribunal would conduct its inquiry and make the appropriate remedy. If not, the Tribunal would decline to conduct an inquiry. The implication and effect of the regulatory amendments are that the Tribunal does not have any jurisdiction over a procurement that is subject to a national security exemption and may not conduct any inquiry when the exemption is invoked.

Canada also experienced significant controversy with respect to its application of deferred prosecution agreements (DPAs) under the Criminal Code. A DPA allows a person to avoid prosecution for specified offences if they agree to implement various measures to address alleged corrupt conduct and be subject to monitoring. The controversy arose when the attorney general was allegedly pressured to reconsider the use of a DPA with respect to a company accused of corrupt practices. The implications of this controversy are not known at this time. However, it is likely that there will be significant debate regarding the availability and use of DPAs in the future.

Also, there seems to be an increasing trend for Canada to engage in audit and cost review type of activities. Canada may engage in these activities on its own behalf. In addition, Canada may conduct price certifications at the request of allied governments (ie, certain Nato countries) seeking to conduct price review of Canada-based security and defence contractors in the context of non-competitive contracting processes. Equally, Canada may request an allied government conduct price certification reviews of companies based in the allied country that are seeking to supply defence and security goods and services to Canada.

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**Coronavirus**

### 42 | What emergency legislation, relief programmes and other initiatives specific to your practice area has your state implemented to address the pandemic? Have any existing government programmes, laws or regulations been amended to address these concerns? What best practices are advisable for clients?

The government of Canada and the provincial-territorial governments have implemented a number of measures, relief programmes and other initiatives to address coronavirus. These measures have been focused more broadly on the Canadian population and economy and are not specifically focused on the defence and security practice areas. Procurement efforts in Canada for goods and services related to coronavirus response have been coordinated by the government of Canada and there has been extensive reliance on the 'national security exemption' to conduct procurements in an expedited manner that does not conform with disciplines normally associated with the acquisition of such goods and services in Canada.

# France

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## LEGAL FRAMEWORK

### Relevant legislation

1 What statutes or regulations govern procurement of defence and security articles?

Contracts for defence and sensitive security equipment and services (MPDS) are public procurement contracts. Three public procurement codes have been successfully implemented since 2001. Furthermore, the French government has recently integrated public procurement rules into a single code, the Public Procurement Code (PPC). MPDS are public procurement contracts (PPC, article L. 2) and therefore governed, since 1 April 2019, by articles L. 1113–1, L. 2300–1 to L. 2397–3, and R. 2300–1 to R. 2397–4 of the PPC.

The EU Defence and Security Directive (DSPCR) (2009/81/EC) has been incorporated into French law and has resulted in the development of a series of legislative acts governing defence procurement (dated 2004, 2011, and finally 2016).

Other laws, regulations and policies are applicable to defence contracts, most notably the Standard administrative clauses which are specific to the French Defence Procurement Agency and the technical note of the Legal Affairs Department of the Ministry of Finance dated 1 January 2020.

General principles derived from the Treaty on the Functioning of the European Union also apply to defence procurements, including the principles of equal treatment, non-discrimination, transparency, proportionality and mutual recognition. However, due to the strategic nature of some defence procurement, many MPDS are subject to classification measures in accordance with the regulations governing the protection of secrecy (arising in particular from the Criminal Code and the Defence Code). Such contracts are, as a result, excluded from the public procurement rules, subject to certain exclusions.

### Identification

2 How are defence and security procurements identified as such and are they treated differently from civil procurements?

Article L. 1113–1 of the PPC defines MPDS as contracts concluded by the state or one of its public institutions that have one of the following activities:

- the supply of military equipment, including any parts, components or subassemblies thereof;
- the supply of sensitive equipment, including any parts, components or subassemblies thereof;
- works, goods and services directly related to military or sensitive equipment for any and all elements of its life cycle; and
- works and services for specifically military purposes or sensitive works and sensitive services.

However, some defence procurement is excluded from the application of the PPC. According to article 2515–1 of the PPC, this applies to:

- public procurement of financial services, excluding insurance services;
- public procurement of arms, ammunition or war materiel where the protection of the essential security interests of the state so requires; and
- public contracts for which the application of the regulation would require the disclosure of information contrary to the essential security interests of the state.

### Conduct

3 How are defence and security procurements typically conducted?

The PPC provides three main procedures for awarding MPDS.

First, those that are not subject to the PPC and can be directly awarded without the use of competitive procedures. These are expressly listed in article L. 2515–1 of the PPC.

Second, for MPDS falling within the scope of the PPC, a distinction is made between those that can be subject to a negotiated procedure and those that are subject to a formalised procedure.

For MPDS covered by a negotiated procedure, the availability of the negotiated procedure without prior publication or competition is greater than for public procurement in the traditional sector (articles R. 2322–1 to R. 2322–14 of the PPC). In such cases, the public entity is free to organise this procedure but must proceed in accordance with the normal principles of public procurement law.

Above certain specific thresholds (up to €443,000 before tax for supplies and services and €5,548,000 before tax for works contracts), the contracting authority may freely choose one of the following formalised procedures with publication and competition: restricted invitation to tender, competitive procedure with negotiation, or competitive dialogue.

Finally, for MPDS not expressly falling into these two categories and when the estimated value of the needs of the contracting authority is below the thresholds of a formalised procedure, the contracts will be subject to an adapted procedure that enables the public entity to award their contracts according to a transparent competitive tendering procedure freely determined according to the subject matter and special features of the contract.

### Proposed changes

4 Are there significant proposals pending to change the defence and security procurement process?

The European Commission reviewed the MPDS regime in 2016 and determined that no legislative changes were necessary. However, it has indicated that it will take a stricter approach to enforcing compliance

with the rules, as it found too many MPDS contracts were awarded without any competition.

**Information technology**

5 Are there different or additional procurement rules for information technology versus non-IT goods and services?

There are specific rules that relate to IT procurement. Most IT procurement will be undertaken under the general administrative clauses (CCAG) applicable to IT procurement (IT procurement CCAG), which was published on 16 October 2009 by a ministerial order of 16 September 2009. In many instances, the IT procurement CCAG will only apply to contracts that expressly refer to these clauses.

If the contracting authority chooses to refer to the IT procurement CCAG, it will have to adapt the provisions of the contract to reflect the specific features of IT procurement. This will be done through a set of special administrative clauses (CCAP), either to supplement or to derogate from the IT procurement CCAG (article R. 2112–3 of the PPC). If the contracting authority chooses not to refer to the IT procurement CCAG, it will have to include the provisions necessary for the management of these kinds of contracts in its CCAP.

It should be noted that the IT procurement CCAG was not adapted to the provisions of the ordinance of 23 July 2015 on public procurement and its two implementing decrees of 25 March 2016, which entered into force on 1 April 2016. The first decree relates to public procurement contracts in general, and the second, the MPDS Decree, to public procurement in the defence sector. However, this mechanism is still enforceable if the contracting authority chooses to refer to the IT procurement CCAG (see article 151 of the MPDS Decree).

**Relevant treaties**

6 Are most defence and security procurements conducted in accordance with the GPA or other treaty-based procurement rules, or does this jurisdiction commonly use the national security exemption to procure them?

The majority (70 per cent) of defence and security procurement in France is negotiated by mutual agreement. The predominance of this mode of awarding contracts is explained by the complexity of the transactions at stake, the necessity for a comprehensive exchange of information prior to the contract being awarded, as well as the willingness of the public authorities to support the industrial defence sector. However, the statistics published by the French Ministry of Defence do not provide for specific percentages regarding the use of the national security exemption. The Observatory of European Defence and Security Procurement published an eight-year review of the application of the DSPCR in June 2019. This review does not mention the number of contracts that are exempt from the normal requirement to compete openly, but it does show that 24 per cent of French defence contracts use a procedure that does not utilise prior publication.

## DISPUTES AND RISK ALLOCATION

**Dispute resolution**

7 How are disputes between the government and defence contractor resolved?

Two types of dispute settlement are usually used to resolve disputes: a conciliation procedure or a procedure before a French administrative judge. However, most defence and security contracts provide for an amicable settlement of disputes before the case is referred to the competent court.

In France, amicable settlements of defence and security disputes are referred to the National Committee for the Amicable Settlement of Disputes in Public Procurement (CCNRA). This committee is neither a court of law nor an arbitration body. Its mission is to seek legal and factual elements with a view to proposing an amicable and equitable solution (articles R. 2197–1 of the Public Procurement Code (PPC)). The CCNRA then issues opinions, which the parties are free to follow or to disregard.

Where a dispute is referred to a conciliator, the referral suspends the limitation period, which resumes if the solution proposed by the conciliator is rejected by the contracting authority. If the conciliation fails, the party who initiated it can refer the matter to the administrative court within the time limit that runs from notification of the administration's decision to refuse to follow the opinion of the conciliation committee. If a party prefers to bring the dispute before the administrative court, it must do so within two months of the rejection of its prior administrative complaint.

8 To what extent is alternative dispute resolution used to resolve conflicts? What is typical for this jurisdiction?

Conciliation procedures, procedures before a French administrative judge, and seeking an amicable settlement with the assistance of CCNRA are only attempted in disputes between the administration and a contractor, or the defence consortium and a security contractor, therefore a referral can only be done by the administration or the contractor. A referral to the CCNRA is not possible if the dispute is among members of the defence consortium holding the contract, or between a contractor and a tier 1 subcontractor, or a tier 1 subcontractor with a tier 2 subcontractor. However, there is nothing preventing any of the latter parties from trying to reach out-of-court settlements. If they choose to pursue litigation, the case can only be brought before a judicial judge, not an administrative judge.

**Indemnification**

9 What limits exist on the government's ability to indemnify the contractor in this jurisdiction and must the contractor indemnify the government in a defence procurement?

Public procurement is subject to an extensive system of law characterised by a balance of power that gives the public contracting party the means to enable it to impose its will on its contracting partner. The government has the right (even if there is no contractual clause stipulating it) to terminate the contract unilaterally for public policy reasons, subject to the total indemnification of the operator for the damage suffered (which is composed of the loss incurred and the lost profit). The government also has extensive power to impose unilateral modifications on the contract. The use of this prerogative must, however, not lead to the economic disruption of the contract. A judicial tool – unpredictability theory – provides an essential guarantee for the contractor against the risk of economic uncertainties. It provides that if certain conditions are met (in the case of an event that is unpredictable, independent from the will of the parties and that leads to the economic disruption of the public contract) the operator is obliged to continue to perform the contract. However, the government is required to pay a fee to the operator relative to any increased cost of performing the contract. In general, French administrative jurisprudence has set this percentage at 90 per cent of the losses caused by the unforeseen event. Furthermore, the French administrative courts provide compensation in a situation where the contractor carries out, under its own initiative and outside the scope of the contract, work that it considers necessary for the proper performance of the contract.

The government may request indemnification from the contractor in case of third-party claims for loss or damage to property, personal

injury, death, or damage to government property. The standard administrative clauses contain specific indemnities relating to damages resulting from aircraft, missiles and ammunition.

**Limits on liability**

10 | Can the government agree to limit the contractor's liability under the contract? Are there limits to the contractor's potential recovery against the government for breach?

The government usually limits its own liability under the contract. The public entity may stipulate a clause within special administrative clauses that limit a contractor's right to compensation in the event of unilateral termination of the contract on grounds of public interest. (See *CAA Versailles*, 7 March 2006, No. 04VE01381, *Cne Draveil and CE*, 4 May 2011, No. 334280, CCI of Nîmes, Uzès, Bagnols, Le Vigan). Furthermore, there is nothing to prevent contractual provisions from entirely excluding any right to compensation in the event of unilateral termination on grounds of public interest (CE, 19 Dec. 2012, No. 350341, AB Trans).

With regard to the reciprocal limitation of the contractor's liability, the contract may also provide that the public body's right to compensation for direct damage is limited in the case of a single contract to the total amount of the contract, or in the case of a split contract to the minimum amount of the contract with a purchase order. The contract award procedure will determine the extent to which this limit is negotiable.

**Risk of non-payment**

11 | Is there risk of non-payment when the government enters into a contract but does not ensure there are adequate funds to meet the contractual obligations?

The risk of non-payment for an undisputed, valid invoice by the French Defence Procurement Agency is perceived to be very low. The government's commitment to incur expenditure is subject to the availability of credit payment provided by the finance laws and the amending finance laws.

**Parent guarantee**

12 | Under what circumstances must a contractor provide a parent guarantee?

If a bidder is a special purpose vehicle set up specifically for a contract, the terms and conditions of the initial tender documentation usually require that the contractor must execute a parent guarantee for the benefit of the public entity and in accordance with a specific template. In such a case, failure to provide this guarantee will result in the disqualification of the contractor from the procurement process. Under French law, the granting by a company, in whatever form, of a guarantee to secure the obligations of an affiliated company must comply with its corporate purpose and corporate interest. If the contractor wishes to transfer its contracts to a special purpose vehicle after it is awarded, the Ministry of Defence usually requests that the shareholders of the special purpose vehicle execute a parent guarantee.

## DEFENCE PROCUREMENT LAW FUNDAMENTALS

**Mandatory procurement clauses**

13 | Are there mandatory procurement clauses that must be included in a defence procurement contract or that will be read into the contract regardless of their actual inclusion?

The standard administrative clauses (CAC Armement) is part of the procurement contract and is common to all defence services. The French Defence Procurement Agency (DGA) will typically seek to include certain standard clauses in its contracts. Primarily, these are the DGA standard clauses of 2014 that constitute a collection of standard contractual clauses relating to the most frequent cases encountered in defence or security contracts awarded under the previous Public Procurement Code (PPC) of 2006.

**Cost allocation**

14 | How are costs allocated between the contractor and government within a contract?

The CAC Armement does not provide any pricing methods. The allocation of costs will, therefore, be contained in a commercial agreement between the parties. Fixed or firm prices are the most common pricing methods for Contracts for defence and sensitive security equipment and services (MPDS). However, under public procurement rules, the procuring entity may conclude a framework agreement and then issue individual purchase orders for each required service. This volume-driven pricing is common in long-term MPDS contracts.

In order to take into account particular circumstances, such as urgency or the technical, functional or economic characteristics of defence equipment or a service, a joint decision of the minister responsible for defence and the minister responsible for the budget may authorise the insertion of a clause providing for a deferred payment (article L. 2391–5 and article R. 2391–18 of the PPC).

**Disclosures**

15 | What disclosures must the contractor make regarding its cost and pricing?

According to article 7.2 of the CAC Armement, a contractor is required to report on the costs that it will incur or has incurred in performing the contract. It must keep all accounting documents and data for at least five years from the date of completion of the contract. When it is subject to a cost control, it is required to provide, at the request of the procuring entity, cost statements showing a breakdown of the cost components, including volume of hours, hourly rates, procurement expenses and overhead costs.

**Audits**

16 | How are audits of defence and security procurements conducted in this jurisdiction?

Under the CAC Armement, the contract and related records shall be accessible to the contracting authority or its designated representative. The right of audit can be exercised at any time.

**IP rights**

17 | Who gets the ownership rights to intellectual property created during performance of the contract? What licences are typically given and how?

In France, in general, the private contracting party obtains the intellectual property resulting from a contract. Contractual relationships between public and private entities are governed by the French PPC and Chapter VII of the CAC Armement relating to IP. The main difference regarding contractual relationships concerns the use of the services produced, rather than their property rights. In return for the ownership of IP rights, the Ministry of Defence expects the right to disclose and use the IP for government purposes (including security and civil protection). By way of derogation from article 62 of the CAC Armament, the clauses of the contract may provide for certain scenarios where IP rights will be granted to the public entity.

**Economic zones**

18 Are there economic zones or other special programmes in this jurisdiction commonly utilised by foreign defence and security contractors for financial or other procurement related benefits?

In France, there are no special defence units located in special economic zones benefiting foreign defence and security contractors.

**Forming legal entities**

19 Describe the process for forming legal entities, including joint ventures, in this jurisdiction.

Under French law, the term 'joint venture' does not correspond to any specific legal situation. It refers, in fact, to any form of cooperation between companies that have in common their contractual and associative natures. The structure of a joint venture can be either purely contractual (collaboration agreement), or both contractual and corporate (collaboration agreement and a joint subsidiary). When this cooperation is expected to last, partners may wish to set up a new legal structure (usually a simplified joint-stock company or a company with limited responsibility structure is used for this). To establish a company, the parties must carry out the formalities of constituting a company required by the legislation applicable to the specific type of legal entity.

**Access to government records**

20 Are there statutes or regulations enabling access to copies of government records? How does it work? Can one obtain versions of previous contracts?

Under the French Code of Relations Between the Public and the Administrations (CRPA), there is a general right for the public to access information held by public bodies. As the Ministry of Defence is a public body, its contracts and records may, in principle, be requested by any involved entity. With regard to the rules of public procurement, a signed contract may be disclosed. However, this right of access must be exercised in compliance with industrial and commercial confidentiality protected by the provisions of article L. 311–6 of this Code. In addition to the information protected by industrial and commercial secrecy, the secrecy of documents classified as national defence secrets pursuant to article 413–9 of the Criminal Code is also protected by law. In addition, national defence secrets are considered to be heavily classified by article L311–5 of the CRPA, which provides that 'other administrative documents whose consultation or disclosure would prejudice . . . national defence secrecy . . . shall not be disclosed'.

Compliance with the principle of access to administrative documents is monitored by the Commission for Access to Administrative Documents, which has developed a doctrine on access to the various documents that may be involved in the award, conclusion and performance of public contracts.

**Supply chain management**

21 What are the rules regarding eligible suppliers and supply chain management and anti-counterfeit parts for defence and security procurements?

There are no specific rules regarding eligibility for MPDS contracts. Suppliers are generally considered eligible for public contracts if they meet the standard requirements of public procurements (both on the professional and the financial and economic side). Subject to limited exceptions, the defence procurement rules oblige an authority to reject tenders from bidders who have been convicted of certain serious offences.

Regarding supply chain management, the PCC and the CAC Armement include specific commitments by the contractor to ensure the security of supply. Furthermore, the first paragraph of article L. 2393–1 of the PPC defines the legal regime applicable to subcontracts for defence or security contracts. It provides that:

> *[The] holder of a defence or security contract may, under his responsibility, entrust another economic operator, referred to as a subcontractor, with the performance of part of his contract, including a supply contract, without this consisting in an assignment of the contract.*

The concept of a subcontractor used by the EU Defence and Security Directive is broader than in French national law, which excludes from its scope standardised contracts for goods or services that are not specifically designed to meet the needs of the public entity. The rules expressly permit authorities to consider the same exclusion grounds for subcontractors, as well as giving them broad rights (eg, to require a supplier to openly compete on some of the subcontracts or to flow down obligations regarding information security (article 2393–3 of the PCC)).

There are no specific rules regarding anti-counterfeit parts.

## INTERNATIONAL TRADE RULES

**Export controls**

22 What export controls limit international trade in defence and security articles? Who administers them?

The French regulation implementing Council Common Position 2008/944/CFSP defining common rules governing control of exports of military technology and equipment (the Common Position) and the Arms Trade Treaty, are contained within the French Defence Code (articles L2331–1 and s.).

The production and trade of defence items are subject to specific authorisation. An export licence is necessary to export defence articles outside the European Union and a transfer licence is necessary to export such items within the EU. The licences are delivered by the prime minister after advice from the Commission for Export of Defence Goods, which assesses each project taking into account:

- their consequences on peace and regional security;
- the respect by the country of destination of human rights;
- the protection of sensitive technologies; and
- the risk of use by non-authorised final users.

A specific regulation applies to dual-use items (ie, goods, software and technology that can be used for both civilian and military applications). On the basis of EU Regulation 428/2009, and its Annex I giving the list of the items concerned by this regulation, the export of such items outside the EU is subject to the grant of a licence.

**Domestic preferences**

23 What domestic preferences are applied to defence and security procurements? Can a foreign contractor bid on a procurement directly?

The Minister of Defence has stated that contracts awarded by the ministry must comply with the procurement rules described in the legislation on public procurement. The latest legislative text prohibits the introduction of a criterion based on national preference. In fact, so long as the foreign contractor undertakes to comply with the protocols, in particular that of the International Labour Organisation, nothing prevents it from bidding on a French procurement directly, even if the activity is located in its territory. Moreover, reserving contracts for

national suppliers can lead to a non-competitive situation, or even to a monopoly situation (Parliamentary Question No. 84337, Rep. Min of 16 September 2010).

**Favourable treatment**

24 | Are certain treaty partners treated more favourably?

The principle of European preference is stated in article L. 2353–1 of the Public Procurement Code (PPC) for defence and security contracts. This principle permits the exclusion of economic operators that are not EU member states or who do not belong to the European Economic Area (article L. 2342–7 of the PPC).

**Sanctions**

25 | Are there any boycotts, embargoes or other trade sanctions between this jurisdiction and others?

The EU implements embargoes and sanctions directed by the UN and also imposes its own autonomous embargoes and sanctions. The French government also has the power to impose national sanctions.

Embargoes and sanctions, depending on their type and ultimate aim, are targeted at individuals, entities, sectors or countries.

The map of all countries affected by embargoes and sanctions and a consolidated list of all persons subject to financial sanctions can be found on the French government website.

**Trade offsets**

26 | Are defence trade offsets part of this country's defence and security procurement regime? How are they administered?

Trade offsets are not part of France's defence and security procurement. Indeed, according to the interpretation set forth in the guidance note on offsets issued by the European Commission:

> *[Offset] requirements are restrictive measures which go against the basic principles of the Treaty [on the Functioning of the European Union] because they discriminate against economic operators, goods and services from other Member States and impede the free movement of goods and services.*

Although the guidance note mentions that offset requirements could, in certain strictly limited circumstances, be justified on the basis of article 346 TFEU, provided that the relevant member state can 'demonstrate that these requirements are necessary to protect its essential security interests', France has not, to our knowledge, relied on these provisions.

## ETHICS AND ANTI-CORRUPTION

**Private sector appointments**

27 | When and how may former government employees take up appointments in the private sector and vice versa?

The High Authority for Transparency in Public Life (HATVP) is responsible for controlling the new private activities of former ministers, former presidents of local executive authorities, and former members of independent administrative authorities. For a period of three years, any person who has held one of these positions must refer the matter to HATVP for consideration as to whether the new private activities are compatible with his or her former functions.

HATVP checks whether the planned activity raises criminal or ethical challenges.

On a criminal level, it examines whether the proposed activity exposes the person concerned to a criminal risk (ie, article 432–13 of the Penal Code prohibits a former public official from working for an undertaking that was subject to the supervisory or control powers of that former official when they still performed public functions, with which it has concluded contracts or in respect of which it has taken or proposed decisions).

On an ethical level, HATVP ensures that the activity envisaged does not undermine the dignity, probity and integrity of functions previously held, and examines whether the activity would lead the person involved to fail to comply with the requirement to prevent conflicts of interest enforced on him or her during his or her former public service, in particular when that activity is carried out in the same economic sector. Finally, it checks that the activity does not jeopardise the independent, impartial and objective functioning of the public institution in which he or she has carried out his or her duties.

Depending on the risks identified, HATVP may declare the activity as incompatible or formulate necessary reservations. The law provides that the HATVP may make public the opinions it issues after having received the comments of the person concerned and after having removed any information that infringes a secret protected by law.

Employees of the private sector who wish to join a public office are not subject to any specific regulation. They should, however, be mindful of any potential conflict of interest.

**Addressing corruption**

28 | How is domestic and foreign corruption addressed and what requirements are placed on contractors?

Corruption consists of two main actions – passive and active corruption – each constituting a separate offence, made up of different elements.

The offence of passive corruption as conceived in the field of public procurement is punishable by article 432–11 of the Criminal Code. This article states that the offending conduct is divided into two distinct, but similar, offences: passive corruption and influence peddling. These offences have in common the quality of the person likely to commit them, that of the corrupt.

Active corruption is provided for under French law by article 433–1 of the Criminal Code. The persons likely to commit active corruption are the same as those concerned by passive corruption. Furthermore, to comply with France's international commitments, the offences of foreign and international public corruption are provided for by articles 435–1 and seq of the Criminal Code.

With regard to related offences relevant to public procurement – such as bribery, embezzlement and misappropriation of public property and funds, revolving doors between public office and the private sector (pantouflage), forgery and use of forgeries, fraud, concealment, and money laundering – French law has fairly similar definitions, even if the sanctions regime is more or less severe. In particular, bribery is provided for by article 432–10 of the Criminal Code and is punishable by five years' imprisonment and a fine of €75,000.

The Sapin II Law broadened the protection afforded to whistle-blowers. However, whistle-blowers are required first to inform their managers, then a public authority and, only as a last resort, the public media. Any abusive reports (ie, reports made in bad faith) will incur civil liability. Moreover, the French Anti-Corruption Agency (AFA) has developed recommendations to assist public and private entities in the corruption prevention process (Act No. 2016–1691 of 9 December 2016 on transparency (Sapin II Law, article 3–2°). The AFA published its Best Practice Guidelines on the prevention and detection of breaches of the duty of probity online in 2017. It particularly insists on the need for contractors to set up an 'internal alert system'.

### Lobbyists

29 What are the registration requirements for lobbyists or commercial agents?

Regulation of interest representation and lobbying, and of the professionals who undertake these activities was first introduced in French Law by Sapin Law II. This law entrusts responsibility for the implementation and management of a monitoring system to a specially created authority, the HATVP.

Since 1 July 2017, it is mandatory for interest representatives to be registered in a detailed numerical list overseen by the HATVP, in which they must provide information on their organisation, lobbying activities and the resources allocated to them. A ministerial order of 4 July 2017 established the list of ranges relating to the detailed numerical list of interest representatives.

### Limitations on agents

30 Are there limitations on the use of agents or representatives that earn a commission on the transaction?

In the public procurement sector, it is uncommon to use success fee-based agents and intermediaries in a way that is comparable to other markets. In practice, some contractors use external assistance to help them understand the procurement process. They should, however, be mindful of any specific disclosure requirements. Registration may also be required where the agent's activity falls within the list of ranges of a ministerial order of 4 July 2017 which require interest representatives to register in a detailed numerical list overseen by the HATVP, for which they must provide information on their organisation, lobbying activities and the resources allocated to them.

## AVIATION

### Conversion of aircraft

31 How are aircraft converted from military to civil use, and vice versa?

As military aircraft are designed with a certification basis that is very different from civil requirements, obtaining a civil certificate for military aircraft would often be too difficult and costly. Certificates of airworthiness can, nevertheless, be granted for specific uses on a case-by-case basis. The process for obtaining a certificate of airworthiness is delegated to France's Civil Aviation Safety Organisation.

The conversion of civil aircraft for military purposes would require meeting the certification specifications set by military standards.

### Drones

32 What restrictions are there on manufacture and trade of unmanned aircraft systems or drones?

Drones designed or modified for military use require a licence to be exported from France.

Civil drones will often be considered as dual-use goods and therefore be also subject to export controls. Indeed, civil drones often contain items covered by Category 6 of Annex I of EU Regulation 428/2009, such as infrared video cameras, lasers and other regulated parts.

## MISCELLANEOUS

### Employment law

33 Which domestic labour and employment rules apply to foreign defence contractors?

There are no specific statutory employment rules that apply exclusively to foreign defence contractors in France. The parties can choose the governing law that applies to the employment contract. Nevertheless, to ensure maximum protection for the worker, the employee could not be deprived of certain mandatory provisions if he or she habitually works in France (including working time provisions, days off, paid holidays, minimum salary, overtime, and rules relating to health and safety). Foreign employees temporarily seconded to France will also benefit from certain French labour legal requirements during the secondment. This will ensure that the secondment will not deprive the seconded employee of the rights they would have been granted under a French employment contract.

### Defence contract rules

34 Are there any specific rules that contractors, foreign or domestic, are bound by in defence contracts?

The most notable are the standard administrative clauses and the technical note of the Legal Affairs Department of the Ministry of Finance dated 1 August 2019.

35 Do contractors avail themselves of these rules when they perform work exclusively outside of the jurisdiction?

If a contractor provides goods or services to the French government, the laws, regulations and policies detailed above will apply even if the work is performed outside France.

### Personal information

36 Must directors, officers or employees of the contractor provide personal information or certify that they fulfil any particular requirements to contract with a government entity?

Companies will be asked to provide information about their directors and certain other employees as part of the pre-qualification questionnaire process, and will usually be required to sign different statements certifying that directors and certain other personnel have not been convicted of certain offences and that the contractor, or each member of the defence consortium, is not subject to the categories of exclusion provided for in articles L. 2341–1 to L. 2341–3 or articles L. 2141–7 to L. 2141–10 of the Public Procurement Code (PPC). Moreover, any candidate for contracts where national defence secrecy is at stake must submit a file allowing his or her company to be authorised at the various levels of defence secrecy. In such cases, employees' personal information would need to be provided to the Ministry of Defence so that relevant checks could be carried out.

### Licensing requirements

37 What registration or licensing requirements exist to operate in the defence and security sector in the jurisdiction?

There are no specific licensing or registration requirements to operate in the defence and security sector in France. However, depending on the nature of the particular project and its degree of sensitivity, there are specific rules governing security clearances. In addition, under the terms of article L. 2331–1 of the Defence Code, war materiel, weapons

and ammunition are classified into four categories (A to D). In this respect, the Internal Security Code provide for a specific regime for the detention of each category. Finally, the production and trade of defence items are subject to the grant of a specific authorisation.

**Environmental legislation**

38 | What environmental statutes or regulations must contractors comply with?

In France, defence contractors will face different environmental legislation depending on their operations, or products or services they provide. They could be subject to regulatory restrictions in relation to as air emissions, water discharge, water pollution, noise and waste disposal, and face responsibility for electrical waste and electronic equipment, and restrictions on hazardous substances within such equipment. Applicable requirements may also incorporate energy efficiency, carbon emissions and energy consumption. Contractors involved with nuclear substances are subject to a separate and additional set of environmental obligations, as well as strict nuclear waste disposal restrictions.

Furthermore, France has a fairly elaborate framework for extra-financial transparency and declaration on corporate social and environmental responsibility. Several laws have introduced mandatory non-financial reporting for listed companies (2010 NRE Law, 2012, 2015 energy transition law and 2017). Defence contractors will also have to comply with social and environmental soft law rules governing their strategies and activities (article 1833 of the Civil Code as amended by the Action Plan for Business Growth and Transformation). In addition, France looks set to deepen its legislative framework in this area by adopting a bill that will create a process for public certification of social performance and environmental issues.

39 | Must companies meet environmental targets? What are these initiatives and what agency determines compliance?

In France, companies do not have mandatory environmental targets to meet. Meeting a standard of environmental and social responsibility is voluntary. Yet the harmonisation of methodologies, making the reporting exercise more streamlined, and working on accompanying guides are essential to ensure that the environmental impacts of companies' activities are better taken into account.

40 | Do 'green' solutions have an advantage in procurements?

French public procurement law takes into account sustainable development and environmental protection. In particular, the PPC allows environmental considerations as award criteria, provided they are related to the subject matter of the contract or to its conditions of execution (article R2152–7 of the PPC). The special conditions for the performance of a contract for defence and sensitive security equipment and services (an MPDS) may, in particular, include elements of a social or environmental nature that take into account the objectives of sustainable development by reconciling economic development, protection and enhancement of the environment and social progress' (article R2312–4 of the PPC).

## UPDATE AND TRENDS

**Key developments of the past year**

41 | What were the key cases, decisions, judgments and policy and legislative developments of the past year?

In a recent judgement, the French Administrative Supreme Court has clarified the scope of defence and security procurements. In March 2019, the Maritime Affairs Branch of the Ministry of Ecological and Social Transition launched a consultation according to an adapted procedure for the supply of semi-automatic guns of 9x19mm calibre and their cases, magazine holders and ancillary services. In concrete terms, this contract aims at modernising the weapons used to control certain regulated fisheries and to combat poaching.

In order to exclude this contract from qualifying as a contract for defence and sensitive security equipment and services (an MPDS), the French Administrative Supreme Court reasoned that 'the exercise of police missions at sea', such as those for which these firearms were intended to be used, does not constitute a military purpose within the meaning of the public procurement rules. Since weapons intended for use in maritime monitoring and surveillance are not specifically designed for military purposes, the MPDS regime was excluded, and that although these firearms constitute equipment that is included in the European Council's list of sensitive materials, as set out in Council Decision No. 255/58 of 15 April 1958, the French Administrative Supreme Court judged that this circumstance 'is not sufficient, on its own, to qualify the supply contracts for this equipment as defence and security contracts' (CE 18 December 2019, No. 431696, Société Sunrock).

**Coronavirus**

42 | What emergency legislation, relief programmes and other initiatives specific to your practice area has your state implemented to address the pandemic? Have any existing government programmes, laws or regulations been amended to address these concerns? What best practices are advisable for clients?

The defence and security sector has been impacted by covid-19 as procurement projects have been disrupted. French authorities took several measures to help suppliers to cope with the impact of the pandemic, including issuing the following:

- Ordinance No. 2020–319 dated 25 March 2020 to facilitate the performance of public contracts and concessions during the covid-19 pandemic. The Ordinance applies to public procurement contracts, concessions and other public contracts that were in effect on 12 March 2020 and were signed up to two months after the end of the covid-19 state of health emergency (article 1).
- Ordinance No. 2020–460 dated 22 April 2020 that amended certain provisions of Ordinance No. 2020-319 to provide greater flexibility and security for public procurement actors (article 20).
- Ordinance No. 2020–560 dated 13 May 2020 setting the time limits applicable to various procedures during the period of the health emergency.
- Ordinance No. 2020–738 dated 17 June 2020 on various measures relating to public procurement.
- Decree No. 2020–1261 of 15 October 2020, that simplifies the advance payments systems in public contracts. And
- Passing Law No. 2020–1525 dated 7 December 2020 (Acceleration and Simplification of Public Action) that includes several items modifying the Public Procurement Code (PPC), in particular, facilitating access to public procurement for companies in difficulty but also for small and medium-sized enterprises.

In the context of the covid-19 pandemic, flexible rules have been implemented in relation to defence transactions. The French Defence Procurement Agency (DGA) could award certain public procurement contracts without launching any tender procedure (article 2515–1 of the PPC). It could also apply the negotiated procedure without prior publication or competition (articles R. 2322–1 to R. 2322–14 of the PPC) or an adapted procedure which enables the DGA to award its contracts according to a transparent competitive tendering procedure determined according to the contract's subject matter and special features. More specifically, the DGA could order health care equipment or call on service providers because of 'an imperative urgency resulting from external circumstances' that could not have been foreseen and prevents it from complying with the normal tender procedure timeframe (article R. 2122–1 of the PPC).

As part of the government's plan, the use of calls for projects is being stepped up as this method allows for less restrictive competition in terms of criteria and deadlines.

During the performance of defence contracts, if contractors were unable to perform all or part of their contracts, it was possible to modify the initial contract without launching a new procurement procedure. The public purchasers had the possibility to award substitute contracts for the performance of the services without having to wait until the end of the health emergency and without its former co-contractor incurring liability.

Private operators could also request financial support from public purchasers, including advance payments that may exceed 60 per cent of the contract amount or the relevant purchase order without being obliged to provide a guarantee on first demand for advance payments exceeding 30 per cent of the contract amount.

More generally, the public purchasers, including the DGA, have tried to facilitate and accelerate payments due to their contractors and subcontractors.

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# Germany

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## LEGAL FRAMEWORK

### Relevant legislation

1 What statutes or regulations govern procurement of defence and security articles?

Above the EU thresholds, public procurement for defence and security goods, services or construction works in Germany is governed by:

- Directive 2009/81/EC of the European Parliament and of the Council of 13 July 2009 concerning the coordination of procedures for the award of certain works contracts, supply contracts and public services contracts in the fields of defence and security;
- the German Act Against Restraints for Competition;
- the Procurement Regulation for Defence and Security; and
- the Procurement Regulation for Construction Works (VOB/A).

Below the EU thresholds, public procurement for defence and security goods, services or construction works is governed by

- the corresponding federal or state budgetary law;
- the Procurement Regulation for Contracts Below the EU Thresholds;
- VOB/A; and
- possibly corresponding state procurement law.

### Identification

2 How are defence and security procurements identified as such and are they treated differently from civil procurements?

Defence and security procurement is defined in Directive 2009/81/EC as procurement of military equipment, including:

- any parts, components or subassemblies thereof;
- sensitive equipment, including any parts, components or subassemblies thereof;
- works, goods and services directly related to military or sensitive equipment; and
- works and services for specifically military purposes or sensitive works and sensitive services.

As with other procurement directives, the value of the relevant contracts must be above the EU financial threshold to fall within the scope of EU and national procurement law. The applicable thresholds are, as of 1 January 2020, €428,000 for goods and service contracts and €5,350,000 for works contracts. Contracts with values below these thresholds are not covered by the Defence and Security Directive.

It is with regard to the structure and basic principles that the system is similar to the general rules on public procurement. Nevertheless, there are some differences, such as the fact that the contracting authority is free to choose between a restricted procedure and a negotiated procedure, while the possibility of an open procedure does not exist. Another special rule is that, in addition to the traditional grounds for exclusion and the lack of ability, there are further grounds for exclusion for bidders from public procurement procedures. They may also be excluded because they lack reliability and because exclusion is justified on grounds of national security. Specific rules also apply to protect classified information and to safeguard information and there may also be specific rules on security of supply.

### Conduct

3 How are defence and security procurements typically conducted?

Defence and security procurement for the German military can be divided into three groups. The first group comprises of the procurement process for operational products, the scope for which is defined by the German military's Customer Product Management Process. This is an internal framework guideline for the capability-based determination of requirements, the cost-efficient and timely procurement of operational products and services, and their efficient use. The industry is involved in all phases of the process, within the limits set by public procurement law. The second area involves the procurement of standard and military goods and services for military missions. The third area involves the procurement of complex services. The Federal Office of Defence Technology IT and In-Service Support, and the Federal Office for Infrastructure, Environmental Protection and Services of the Bundeswehr are ultimately responsible for central military procurement.

The Procurement Authority of the Federal Ministry of the Interior is in charge of non-military security procurement for federal institutions. This applies, in particular, to security procurement for the Federal Police, Customs and the Federal Administration in general. As far as security procurement at the state level is concerned, the procurement office or the requesting body is generally responsible.

The restricted procedure and the negotiated procedure with publication of a contract notice are the standard procedures for defence and security contracts. In these two constellations, the contracting authority publishes a call for competition in the course of an EU call for tenders. Where the procedure is restricted, the contracting authority shall invite a limited number of candidates taking part to submit tenders. The corresponding bids are not subject to any further negotiation. A limited number of candidates shall be invited by the contracting authority to submit tenders in the negotiated procedure. These tenders then become the subject of negotiations.

Exceptionally, a negotiated procedure without publication of a contract notice is also permitted. The contracting entity may choose such a procedure in the following scenarios:

- no tenders or no suitable tenders have been submitted within the framework of a restricted procedure or a negotiated procedure with prior publication of a contract notice;
- the contract may only be awarded to a specific supplier for technical reasons or reasons connected with the protection of exclusive rights;

- the time limits for a restricted or negotiated procedure with publication of a contract notice are incompatible with the urgency of the crisis for which goods or services are required; or
- the time limits for a restricted or negotiated procedure with publication of a contract notice cannot be complied with because of very urgent reasons caused by an unforeseeable event and not attributable to the contracting authority and, therefore, an exception is absolutely necessary.

In general, military and civil security goods or services may be procured without a public call for competition, where the national security exemptions to EU and the Agreement on Government Procurement (GPA) procurement rules apply, or for intelligence purposes. Instead, these contracts are awarded through restricted negotiated procedures in accordance with the specific security requirements for the goods and services concerned.

**Proposed changes**

4 | Are there significant proposals pending to change the defence and security procurement process?

On 4 April 2020, the law on accelerated procurement in the field of defence and security and on the optimisation of procurement statistics entered into force. It is intended to increase the procurement opportunities for military and civil security authorities, to specify the legal requirements for procurement statistics in more detail and to introduce clarifications and examples of rules for improved use of procurement law scope within the framework of European law.

The impact of these changes on procurement processes will become apparent in the near future.

**Information technology**

5 | Are there different or additional procurement rules for information technology versus non-IT goods and services?

There are no specific procurement rules, but there are nuances to the procurement of IT goods at a contractual level. Contracting authorities generally use standardised contract templates called EVB–IT contracts. The EVB–IT contracts are specifically standardised for the purchase of IT goods and services. To prevent the contractor from being subject to foreign laws, obliging the contractor to pass on confidential information to foreign government or security authorities, these contracts generally contain corresponding 'no spy' clauses. This confidential information may have been made available to the contractor in the course of the tendering procedure or the performance of the contract. In addition, to ensure that unauthorised third parties (eg, foreign governments or security authorities) do not have access to the system or the software, there are contractual conditions that guarantee that IT products are free of secret access points.

**Relevant treaties**

6 | Are most defence and security procurements conducted in accordance with the GPA or other treaty-based procurement rules, or does this jurisdiction commonly use the national security exemption to procure them?

In addition to EU procurement rules, Germany is bound by the GPA procurement rules. German contractors have generally applied these regulations to military and non-military security contracts following the implementation of EU Directive 2009/81/EC on contracts in the fields of defence and security into German law. Nevertheless, the national security exemption and the arms exemption under article 346 of the Treaty on the Functioning of the European Union (TFEU) are still applied in many cases, especially in the field of arms procurement. However, there has been a decline in the use of these exemptions, largely as a result of strict judicial interpretation and a changing political climate.

However, the application of article 346 TFEU again comes into focus to the extent that a strategy paper adopted by the Federal Cabinet to strengthen the security and defence industry has extended the list of relevant key technologies to include, among others, surface shipbuilding, preventing a Europe-wide tendering obligation in this area. This is linked to the law on accelerated procurement in the field of defence and security and on the optimisation of procurement statistics that entered into force on 4 April and extended the national scope of application of article 346 TFEU to these key technologies.

## DISPUTES AND RISK ALLOCATION

**Dispute resolution**

7 | How are disputes between the government and defence contractor resolved?

There are no arbitration clauses contained in either the standard contractual terms of the German military or in those of other German security authorities. Therefore, the civil courts usually deal with the disputes between the government and the contractors. For disputes during the procurement procedures, special public procurement tribunals exist.

8 | To what extent is alternative dispute resolution used to resolve conflicts? What is typical for this jurisdiction?

The agreement of an alternative dispute resolution with the German military is only considered on an ad hoc basis due to the fact that the German military will not deviate from its standard terms for smaller contracts. On the other hand, for larger contracts, the German military may agree arbitration clauses on a case-by-case basis.

**Indemnification**

9 | What limits exist on the government's ability to indemnify the contractor in this jurisdiction and must the contractor indemnify the government in a defence procurement?

If the state breaches the contract with the contractor, German law requires the state, like any private client, to indemnify the contractor for the damage reasonably and foreseeably caused by the breach. On the other hand, if damages result from a breach by the contractor, the contractor has the obligation to indemnify the state for any damages.

**Limits on liability**

10 | Can the government agree to limit the contractor's liability under the contract? Are there limits to the contractor's potential recovery against the government for breach?

Limitation of the contractor's contractual liability can be agreed upon. However, in recent years the procurement authorities have been very strict on enforcing unlimited contractual liability clauses.

**Risk of non-payment**

11 | Is there risk of non-payment when the government enters into a contract but does not ensure there are adequate funds to meet the contractual obligations?

Generally speaking, there is no legal risk of non-payment. German contracting authorities are bound by their contracts, as is the case for any private undertaking. Moreover, sufficient funds have to be achieved available before the contract is awarded.

**Parent guarantee**

12 | Under what circumstances must a contractor provide a parent guarantee?

The cases in which a contractor is required to provide a parent guarantee are generally those in which the contractor itself does not meet the financial and economical requirements set out in the procedural documents. A parent guarantee might, therefore, be presented as an alternative. However, the adequacy of such parent guarantee as a way of attaining the financial requirements will be for the contracting authority to decide.

## DEFENCE PROCUREMENT LAW FUNDAMENTALS

**Mandatory procurement clauses**

13 | Are there mandatory procurement clauses that must be included in a defence procurement contract or that will be read into the contract regardless of their actual inclusion?

There are no procurement clauses that must be included in a defence contract or that are necessarily implied. However, there are a great number of varying standard terms and conditions and legal regulations that are commonly included in the contract by the contracting authority. In all cases, public contracts are also subject to the price control provisions of Price Regulation No. 30/53, which contains binding rules on the pricing of public contracts.

**Cost allocation**

14 | How are costs allocated between the contractor and government within a contract?

Where contracts are awarded on the basis of a competitive procedure, the contracts in question generally contain fixed prices or a mix of fixed and variable price elements. Cost accounting elements can also be included. In the case of contracts that have been awarded without competitive procedures, most contracts contain cost-oriented fixed prices or extra cost prices, and the distribution of costs between the contractor and the state depends on individual agreements. The actual distribution of costs between the contractor and the state in these cases depends on the individual agreement.

**Disclosures**

15 | What disclosures must the contractor make regarding its cost and pricing?

To verify that prices are reasonable, contracting authorities may require tenderers to explain their prices during the award procedure and during price controls and sometimes many years after the contract has been fulfilled.

**Audits**

16 | How are audits of defence and security procurements conducted in this jurisdiction?

The Ministry of Defence reviews procurements for the military. On the other hand, in the case of non-military procurements, audits are the responsibility of the supervisory authority, which is usually the Ministry of the Interior. The relevant ministry also reviews procurements at the ministerial level in internal audits. In other situations, the Federal Audit Office or the competent State Audit Office is responsible for audits.

**IP rights**

17 | Who gets the ownership rights to intellectual property created during performance of the contract? What licences are typically given and how?

The ownership of intellectual property rights are individually governed by the contracts.

**Economic zones**

18 | Are there economic zones or other special programmes in this jurisdiction commonly utilised by foreign defence and security contractors for financial or other procurement related benefits?

We are not aware of any such economic zones or programmes in Germany.

**Forming legal entities**

19 | Describe the process for forming legal entities, including joint ventures, in this jurisdiction.

The limited liability company (GmbH) represents the most common form of commercial legal personality. A notarial shareholder agreement is a prerequisite for the formation of a GmbH, whereby the notary must verify the identity of the shareholders by means of valid identification documents at the time the agreement is notarised. Furthermore, the minimum share capital of a GmbH is €25,000 and the company must be registered in the commercial register. The entry in the commercial register requires the confirmation of the managing director to the effect that the share capital to be contributed by the shareholders is available to the company. This is usually combined with an account statement as proof. A list of shareholders signed by the managing director must also be submitted with the application for registration.

The Civil Code Partnership is a simple partnership based on the provisions of the German Civil Code and the simplest form of company under German law. It can be described as a simple and practical instrument suitable for temporary joint ventures, in particular for tenders or as an intermediate step in the formation of a permanent joint venture structure. There are no formal prerequisites for its formation. Furthermore, neither capital nor registration is required.

**Access to government records**

20 | Are there statutes or regulations enabling access to copies of government records? How does it work? Can one obtain versions of previous contracts?

As a rule, government contracts are not published or passed on to third parties. However, everyone (including foreigners) has the right to access official information held by public authorities under the Freedom of Information Act of the Federation and the states. It is generally believed that this should include records of previous procedures for awarding public contracts, including previous contracts. However, access may be denied, among other things, in cases where disclosure could prejudice international relations, the military, public safety or other security interests, or in order to protect classified information and other official secrets or trade secrets (including confidential information and intellectual property rights of third parties). The disclosure of past government contracts will often be barred by one of these exemptions.

**Supply chain management**

21 | What are the rules regarding eligible suppliers and supply chain management and anti-counterfeit parts for defence and security procurements?

There are no special defence and security procurement-related rules regarding eligible suppliers, supply chain management and anti-counterfeit parts.

Economic operators will be considered eligible to participate in public procurement procedures if they meet the eligibility criteria named by the tendering authority in the tender notice. Eligibility criteria in accordance with EU and national regulations may include requirements of professional suitability, financial and economic standing and technical or professional ability and certain compliance self-declarations. All criteria must be connected with the tendered goods, services or construction work. If the tendering procedure or the contract requires access to classified information in accordance with the German Security Clearance Act bidders must also fulfil certain security requirements.

Regulations on supply chain management (especially commitments by the contractor to ensure the security of supply for the duration of the contract and even in the event of a crisis or war) are included on a case-by-case basis in the tendering authorities' standard terms and conditions.

## INTERNATIONAL TRADE RULES

**Export controls**

22 | What export controls limit international trade in defence and security articles? Who administers them?

Germany has very strict export control regulations, especially the German Foreign Trade Act, the Foreign Trade Regulation and the Military Weapons Control Act. These regulations govern the terms and procedures for the export of military equipment and dual-use products. The manufacture, trade, brokering and transport of military weapons and equipment, as well as certain dual-use goods, are subject to government permission. The licence under the War Weapons Control Act is issued by the Ministry of Economic Affairs, upon consultation with the Ministry of Defence and the Foreign Office. Export licences for weapons, military equipment and certain dual-use goods are issued by the Federal Office for Economic Affairs and Export Control (BAFA). Due to Germany's history, the decisions to grant or withhold licences are often highly political. The German government pays particular attention to ensuring that the goods will not be misused to commit human rights violations or to exacerbate a crisis. Decisions on licences for exports of military equipment are primarily based on foreign and security policy considerations, and not on commercial or labour-market interests. These strict German rules also apply to parts of military equipment and often means that common European defence products cannot be exported to third parties, even if the contracting parties are not German. On 16 October 2019, Germany and France agreed on new common export regulations for common defence products.

**Domestic preferences**

23 | What domestic preferences are applied to defence and security procurements? Can a foreign contractor bid on a procurement directly?

European and national public procurement regulations prohibit discrimination against economic operators purely on the grounds of their nationality. Therefore in general, German public procurement procedures are open to all economic operators from the EU, the European Economic Area (EEA) and Agreement on Government Procurement member states. However, on a case-by-case basis and due to the prominence of security and confidentiality concerns in defence and security matters, bidders from non-EU, non-EEA or non-Nato countries might be excluded from the tendering procedures.

For this purpose, a contracting authority's tender documents must state that it reserves the right to reject tenders on defence and security grounds.

In order to protect specific security interests, a contracting authority may also require:

- proof of a national security audit, and only accept the audit's result if it is recognised as equivalent on the basis of intelligence cooperation between the countries concerned;
- the presentation of a certificate ensuring the permissibility of the transport of equipment, including additional supplies, during crisis situations;
- an undertaking regarding access to and the confidentiality of classified information; and
- the fulfilment of additional requirements set out in certain security regulations, such as the measures formulated in the EU Directive on security of network and information systems (the NIS Directive) to ensure a common high level of protection of network and information systems.

**Favourable treatment**

24 | Are certain treaty partners treated more favourably?

European and national public procurement regulations prohibit favourable treatment due to certain national or treaty statues.

**Sanctions**

25 | Are there any boycotts, embargoes or other trade sanctions between this jurisdiction and others?

Germany adheres to United Nations and EU boycotts, embargoes and other trade sanctions. A list of country and personal related weapon embargoes can be found on BAFA's website.

As of 22 July 2020, embargoed countries include:

- Armenia;
- Azerbaijan;
- Belarus;
- the Central African Republic;
- China;
- the Democratic Republic of the Congo;
- Iran;
- Iraq;
- Lebanon;
- Libya;
- Myanmar;
- North Korea;
- Russia;
- Somalia;
- South Sudan;
- Sudan;
- Syria;
- Venezuela; and
- Zimbabwe.

**Trade offsets**

26 | Are defence trade offsets part of this country's defence and security procurement regime? How are they administered?

Offset deals are not part of the EU and German defence procurement regulations, since they are generally incompatible with the procurement law principles of equal treatment and transparency.

## ETHICS AND ANTI-CORRUPTION

**Private sector appointments**

27 | When and how may former government employees take up appointments in the private sector and vice versa?

According to the Federal Civil Servants Act, retired civil servants and former civil servants with pension benefits are obliged to report any gainful employment or other employment which is connected with their official activity in the last five years before the termination of the civil service and which could be detrimental to official interests.

If officials retire at the normal retirement age, the obligation to notify the Commission ends three years after the end of their service. In other cases after five years.

The administrative authority must prohibit the activity if it will prejudice the service's interests. This prohibition is effective until the period during which the former civil servant is obligated to notify the authority ends.

**Addressing corruption**

28 | How is domestic and foreign corruption addressed and what requirements are placed on contractors?

Corruption is punishable under different sections of the German Criminal Code. Criminal offences include bribery of German and EU public officials and German soldiers, members of parliament, commercial bribery and bribery of non-EU foreign officials.

Although there is no true enterprise criminal law in Germany, an economic operator may be subject to fines if its employees commit corruption offences on behalf of the company. Economic operators with employees have been found guilty of corruption in a court of law are excluded from participation in public procurement procedures for a period of up to five years. However, before the bidder can be excluded, it must be permitted to present its case and have the opportunity to set out measures it will take to prevent any further wrongdoing.

The competition register set up and maintained by the Federal Cartel Office provides contracting authorities with information on grounds for exclusion within the meaning of competition law. Prior to registration, a company concerned has the opportunity to comment on the data collected within two weeks and to point out any errors.

**Lobbyists**

29 | What are the registration requirements for lobbyists or commercial agents?

There are no formal registration requirements for lobbyists and commercial agents.

**Limitations on agents**

30 | Are there limitations on the use of agents or representatives that earn a commission on the transaction?

There are no formal limitations on the use of agents or representatives. However, contracts issued by the Federal Ministry of Defence or its subordinates usually include standard terms requiring the approval of intermediaries or brokers. Approval will only be granted if it is commercially appropriate and there are no disadvantages for the contracting authority.

## AVIATION

**Conversion of aircraft**

31 | How are aircraft converted from military to civil use, and vice versa?

Military aircraft may be converted to civil use if the armed services give up control of the aircraft and the aircraft is fully demilitarised. For civil use, the former military aircraft has to obtain or retain all necessary certificates and permits generally required for civil aircraft. The use of a civil aircraft for military purposes requires that the aircraft is under control of the armed services and certified by the German Military Aviation Authority.

**Drones**

32 | What restrictions are there on manufacture and trade of unmanned aircraft systems or drones?

In general, the aviation laws and regulations governing the inspection and certification of aircraft also apply to unmanned air systems, both autonomous and remotely piloted. Systems that do not exceed a certain weight, use a type of special propulsion and are not or only used in certain areas are excluded from certain regulations.

## MISCELLANEOUS

**Employment law**

33 | Which domestic labour and employment rules apply to foreign defence contractors?

Foreign defence contractors must adhere to German labour and employment regulations if they permanently operated in Germany or post employees in Germany. These regulations included provisions on equal treatment and non-discrimination, hiring and laying off employees, minimum wages, working conditions, health and safety measures and protective measures for pregnant women. Violations of these labour and employment laws may, besides other punishments, lead to an exclusion from further public contracting procedures.

**Defence contract rules**

34 | Are there any specific rules that contractors, foreign or domestic, are bound by in defence contracts?

Foreign and domestic defence contractors must adhere to all applicable regulations on the production, handling, transport, export and use of weapons and other relevant military goods. In addition, if the contract involves access to classified information, contractors must observe all applicable regulations regarding the security of such information. However, foreign security clearances from EU and Nato member states might be accepted on a case-by-case basis.

35 | Do contractors avail themselves of these rules when they perform work exclusively outside of the jurisdiction?

No. With the possible exclusion of labour and employment regulations, a contractor is usually bound by all applicable regulations, even if they perform work exclusively outside Germany.

**Personal information**

36 | Must directors, officers or employees of the contractor provide personal information or certify that they fulfil any particular requirements to contract with a government entity?

Economic operators participating in a public procurement procedure must generally declare, and possibly certify, that their directors, officers and leading employees have not been convicted of certain criminal offences. Usually, a self-declaration by the bidder is sufficient. If the contract involves access to classified information, personal security clearances are required for all personnel who might be involved with the contract or have access to classified information.

**Licensing requirements**

37 | What registration or licensing requirements exist to operate in the defence and security sector in the jurisdiction?

Aside from the aforementioned regulations governing access to classified information and manufacturing, trade, brokering and transport of military weapons and equipment as well as certain dual-use goods, there are no additional general registration or licensing requirements to operate in the defence and security sector in Germany.

**Environmental legislation**

38 | What environmental statutes or regulations must contractors comply with?

There are no specific environmental statutes or regulations for defence and security contractors. On a case-by-case basis, exemptions might be available from general environmental statutes or regulations for defence goods or services.

The contracting authority may require tenderers to comply with certain standards for environmental management and prove this by presenting certificates issued by independent organisations. The contracting authorities refer either to the Community eco-management and audit scheme or environmental management standards based on the relevant European or international standards and certified by bodies conforming to Community legislation or European or international certification standards.

39 | Must companies meet environmental targets? What are these initiatives and what agency determines compliance?

There are no specific environmental targets for defence and security contractors. The contracting authority might choose, however, to include environmental targets either as performance requirements or as evaluation criteria in a public procurement procedure. The use of these requirements and criteria in the defence and security sector is currently very rare.

40 | Do 'green' solutions have an advantage in procurements?

The contracting authority might choose to include environmental issues and requirements either as performance requirements or as evaluation criteria in a public procurement procedure.

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## UPDATE AND TRENDS

**Key developments of the past year**

41 | What were the key cases, decisions, judgments and policy and legislative developments of the past year?

On 2 April 2020, the law on accelerated procurement in the defence and security sector and on the improvement of procurement statistics entered into force. The act specifically modifies the procurement regulations in order to enable accelerated procurement for the military and civilian security authorities. The clarifications and typical examples are designed to help ensure that procurement procedures can be used more quickly and consistently by the procuring agencies.

**Coronavirus**

42 | What emergency legislation, relief programmes and other initiatives specific to your practice area has your state implemented to address the pandemic? Have any existing government programmes, laws or regulations been amended to address these concerns? What best practices are advisable for clients?

On 19 March 2020, the Federal Ministry of Economics and Energy published a circular on the application of public procurement law in connection with the procurement of services to stem the spread of the novel coronavirus. However, this Circular does not only apply to the defence and security sector. In this respect, it is explicitly stated that the centrally formulated requirements apply to the application of the negotiated procedure without competitive tendering, which means that a sufficient degree of urgency can be assumed.

In addition, several federal states have increased the value thresholds, at least temporarily.

# India

**Kabir Bogra**
Khaitan & Co

## LEGAL FRAMEWORK

### Relevant legislation

1 What statutes or regulations govern procurement of defence and security articles?

India does not have an overarching statute governing procurement of defence and security articles. Procurements by the government and its agencies are broadly governed by the General Financial Rules 2017 (GFR), which provides the framework under which all government procurements are undertaken.

The Defence Acquisition Procedure (DAP) and the Defence Procurement Manual (DPM) are the principal regulations for defence and security procurements undertaken by the Ministry of Defence (MoD). The DAP and DPM are based on government procurement principles contained in the GFR, but hold the bidders and vendors to a higher standard of compliance and administrative scrutiny.

The DAP, introduced in 2020, governs the procurement of long-term strategic assets (classified as capital procurements) and is indicative of the country's defence production policy. It also serves as an important tool to understand the manner in which defence procurement contracts are likely to be interpreted by the MoD in the event of an ambiguity. The DPM governs the procurement of non-strategic and bulk procurements of goods such as uniforms, non-military stores etc (classified as revenue procurements).

Apart from the DAP and DPM, government procurements are also subject to the policies and directives issued by the Central Vigilance Corruption (CVC), the apex anti-corruption monitoring institution in India. The CVC periodically issues binding instructions required to be followed across ministries for procurements.

### Identification

2 How are defence and security procurements identified as such and are they treated differently from civil procurements?

Both defence and civil procurements are conducted under the principles provided in the GFR. A few noticeable differences in procedure between defence and civil procurements are as under:

- The defence establishment (navy, air force and army) seeking to procure articles is required to present a detailed report justifying the procurement, which is required to be approved by a committee. The approval is called the Acceptance of Necessity (AoN), which is the point of initiation of the procurement process.
- Procurements of defence and security articles follow a defined categorisation process, based on the domestic availability of the articles and capability of the Indian industry to manufacture the same. Each category has a separate procedure for the procurement process.
- Participation by foreign vendors in procurement contracts for defence and security articles under the DAP exceeding 20 billion rupees in value necessarily require offset obligations to be undertaken and discharged by the foreign bidder. The range of offset varies between 30 per cent to 50 per cent of the contract value.

### Conduct

3 How are defence and security procurements typically conducted?

Defence procurements are usually conducted through an open tender system consisting of a two-stage bid process. The process follows the sequence as provided hereunder:

- The requirements are published as a Request for Information, soliciting interest from manufacturers.
- Based on the information received from the manufacturers, the technical requirements are formulated and approval by a committee constituted for this purpose. The committee provides its approval through an AoN.
- A request for proposal (RFP) is issued within six months of the AoN. The issuance of the RFP implies the formal initiation of the bid process.
- The bidders are invited to participate in a pre-bid meeting to seek clarifications on any technical, commercial or interpretative aspect of the RFP.
- Subsequently, the bidders are required to submit separate commercial and technical bids. The DAP also provides for establishment of several technical committees to evaluate each aspect of the bid.
- The technical bid is evaluated first and bidders that meet the technical requirements are invited to undertake field trials.
- Post completion of the field trials, the commercial bids are opened, and preference is typically given to the bidder that quotes the lowest price. However, in certain circumstances, a vendor with superior technical product at a higher price may be chosen.
- After selection of the vendor, contract negotiations are initiated to finalise the contract.

The procurement frameworks also envisage exceptional situations where an open tender system may not be feasible, such as:

- procurements below a de minimis value undertaken through direct orders placed on known vendors;
- procurements in emergency or crisis situations undertaken through a fast track procedure;
- procurements for sensitive equipment and systems undertaken directly at government levels; and
- procurements for products for which only a sole vendor is available.

For the above situations, the procurement process is curtailed, involves fewer procedural steps and is executed faster.

**Proposed changes**

4 Are there significant proposals pending to change the defence and security procurement process?

The last significant amendment to the procurement process was undertaken in September 2020, with the issuance of the new DAP, which supersedes the 2016 iteration, As the amendments to the public procurement regime are recent, there are no significant proposals pending to change or overhaul the procurement process. Incremental amendments and revisions are frequently undertaken to facilitate the procurement process and provide operational guidance to bidders and contractors.

**Information technology**

5 Are there different or additional procurement rules for information technology versus non-IT goods and services?

The procurement process under the GFR and the DPM does not distinguish between IT and non-IT products and services, therefore, the process and rules remain identical for procurement. However, the latest version of the DAP, which was issued in September 2020, introduced a separate procedural framework for the procurement of information technology products (including software and hardware elements). This procedural framework is broadly similar to others under the DAP, but is customised to meet the characteristics of information technology contracts.

**Relevant treaties**

6 Are most defence and security procurements conducted in accordance with the GPA or other treaty-based procurement rules, or does this jurisdiction commonly use the national security exemption to procure them?

India is not a signatory to the Agreement on Government Procurement (GPA) of the World Trade Organization nor to the model procurement law issued by the United Nations Commission on International Trade Law (UNCITRAL). Consequently, the Indian procurement laws are not modelled on either the GPA or the UNCITRAL Model Law.

The Law Commission of India has recommended the adoption of principles and concepts from the GPA and UNCITRAL model law. Based on the recommendation, the Public Procurement Bill, 2012 has been tabled before the parliament. However, the bill has been pending before the legislature for the several years and is not expected to be enacted into legislation in the foreseeable future.

## DISPUTES AND RISK ALLOCATION

**Dispute resolution**

7 How are disputes between the government and defence contractor resolved?

Arbitration is the preferred mode of dispute resolution in government procurements, including those for defence and security articles. Certain frameworks, such as the General Financial Rules 2017 (GFR), may also permit dispute resolution through civil remedies through the courts of India.

Procurement contracts under Defence Acquisition Procedure (DAP) and Defence Procurement Manual (DPM) mandate arbitration to be governed by the laws of India and the seat of arbitration to be India. Subject to the nature, value and strategic importance of the procurement, the power to appoint arbitrators may vest solely with the buyer, with both parties or with an independent body such as the International Chamber of Commerce or its Indian counterpart. The burden of cost of arbitration may also be defined in the contract, which may be shared between the parties or left to the arbitrator or arbitral tribunal to decide.

8 To what extent is alternative dispute resolution used to resolve conflicts? What is typical for this jurisdiction?

Alternative dispute resolution through arbitration is the preferred and de facto mode of resolving conflicts between the government and contractors, and between the contractors and subcontractors.

**Indemnification**

9 What limits exist on the government's ability to indemnify the contractor in this jurisdiction and must the contractor indemnify the government in a defence procurement?

The government typically does not provide any indemnities under defence and security procurement contracts. However, with evolution of the DAP and introduction of new procurement avenues, such as leasing of equipment, limited indemnities may be negotiated with the government depending on the nature of the transaction. On the contractor's side, the standard contract clauses require the contractor to indemnify the government against infringement of third-party intellectual property rights in the goods or services purchased from the contractor.

While technically not an indemnity, defence procurement contracts also require the contractor to execute bank guarantees for performance parameters and anti-corruption compliances. It is not uncommon for these instruments to be invoked in defence procurement contracts for failure to adhere to certain aspects of the contract, such as indigenous content requirements, delivery schedule, quality parameters, bribery and undue influence, etc.

**Limits on liability**

10 Can the government agree to limit the contractor's liability under the contract? Are there limits to the contractor's potential recovery against the government for breach?

The standard contract document under the DAP does not contain any clauses limiting the contractor's liability, however, contractors may negotiate with the government for inclusion of limitations on their liability. Regardless of whether the government agrees to limit the contractor's liability, the provisions of the Indian Contract Act 1872 (ICA) permit an aggrieved party to seek compensation only to the extent of loss or damage that may naturally arise from a breach that could reasonably have been foreseen at the time of execution of the contract.

The courts in India consider damages to be restitutive and not punitive in nature, hence are reluctant to award punitive damages. Therefore, the liability of both the contractor and the Ministry of Defence (MoD) would be limited to direct losses, in the absence of any express clauses to the contrary.

There are no statutory or regulatory restrictions on any claim of damages sought against the government. The Indian courts do not accord any special privileges to the government with respect to contractual disputes.

**Risk of non-payment**

11 Is there risk of non-payment when the government enters into a contract but does not ensure there are adequate funds to meet the contractual obligations?

Defence and security acquisitions are undertaken based on firm budgetary allocations. Therefore, the likelihood for a shortfall of funds in a defence procurement is extremely unlikely. Defence budgets are occasionally revised mid-year by allocating unspent funds by other ministries to meet the requirement of unforeseen procurements.

**Parent guarantee**

12 | Under what circumstances must a contractor provide a parent guarantee?

In circumstances where the prime bidder or contractor is unable to tender the bank guarantee mandated to be submitted as part of the bid, the MoD will require the parent to submit such guarantee on behalf of the bidder or contractor. It is standard practice by the MoD to require bidders to submit bank guarantees against all payment streams that MoD is required to make to the prime bidder or contractor.

## DEFENCE PROCUREMENT LAW FUNDAMENTALS

**Mandatory procurement clauses**

13 | Are there mandatory procurement clauses that must be included in a defence procurement contract or that will be read into the contract regardless of their actual inclusion?

India is a common-law jurisdiction and upholds the sanctity of contracts and the intention of the parties as reflected in the contractual terms. Therefore, while the procurement process is governed by the relevant framework such as the Defence Acquisition Procedure (DAP) or the General Financial Rules 2017 (GFR), the contract between the buyer and the vendor is the principal document governing the transaction.

Procurement frameworks such as the DAP and the GFR mandate certain clauses to be included in the contract executed between the buyer and seller. For example, the DAP mandates that standard clauses relating to the use of agents, the penalty for use of undue influence, access to books of accounts, arbitration and clauses related to governing law must be accepted by the seller.

Apart from the above, general principles of law may be read into the contract under the laws of India. For example, the Indian Contract Act 1872 (ICA) mandates that a party to a contract must act in good faith. Therefore, even in the absence of an express clause in the contract, the courts may interpret the buyer to have a right to terminate the contract for mala fide acts undertaken by the vendor, such as misrepresentation of facts.

**Cost allocation**

14 | How are costs allocated between the contractor and government within a contract?

Contracts involving the outright purchase of goods and materials from the vendor typically do not demarcate costs between the contractor and the government. The vendor is responsible for all costs incurred up to the delivery of the goods, including the cost of conducting field trials. In certain procurements of high volume but low-value products, the government may reimburse the cost of goods used in trials.

The DAP provides for cost-sharing for specific types of procurements in relation to products identified by the Ministry of Defence (MoD) for long-term indigenous development and production. For such procurements, the MoD bears up to 100 per cent of the cost of development of the prototype and provides facilities, items and consumables for field trials and testing of the prototypes.

**Disclosures**

15 | What disclosures must the contractor make regarding its cost and pricing?

Cost and pricing disclosures depend on the applicable procurement framework and categorisation of the procurement. For certain types of procurements under the GFR or the Defence Procurement Manual (DPM) on fixed-rate bases, the bidders are not required to provide costing information and must only submit their price bid for the procurement.

For procurements under the DAP, the bidders are required to make the following disclosures with respect to price:

- cost of basic equipment;
- cost of technology transferred (if applicable);
- cost of recommended manufacturer spare parts;
- cost of maintenance tools and test equipment;
- cost of operating manual and technical literature for equipment and spare parts;
- cost of training aids such as simulators, films, charts, etc;
- cost of the recommended training period;
- cost of freight and transit insurance;
- cost of annual maintenance; and
- cost escalations due to inflation.

In addition to the above, it is standard practice for bidders to specify the validity period of the prices quoted in the tender submissions and to state that the cost and prices quoted are applicable only to the configuration offered for the procurement.

**Audits**

16 | How are audits of defence and security procurements conducted in this jurisdiction?

The Comptroller and Auditor General of India (CAG) is the apex constitutional authority that undertakes the audit of all government departments and procurements undertaken by them. The CAG conducts performance and compliance audits of all government procurements and issues a report containing its observations with respect to compliance with legal frameworks and achievement of defined objectives. CAG reports are submitted to the Parliament of India and are publicly accessible.

Internal audits of vendors and procurements may also be undertaken by an individual ministry. For example, the DAP empowers the MoD to conduct audits to ascertain compliance with indigenous content requirements, discharge of offset and costing claims under a procurement category. During such an audit, the MoD (as a customer) is contractually permitted to access the records maintained by the vendor and visit the manufacturing location to verify the authenticity of claims made by the vendor or its suppliers.

**IP rights**

17 | Who gets the ownership rights to intellectual property created during performance of the contract? What licences are typically given and how?

Defence procurements, under most categories of the DAP, entail the outright purchases with minimal design and development requirement. Therefore, the creation of intellectual property during the performance of a contract is not common.

If the government funds the design and development of prototypes, it may retain a non-exclusive licence with government purpose rights in the technical data, software and technology created in the programme. It is pertinent to mention that the funding and development of prototypes are limited to a specific procurement category, namely the 'Make' category, in which participation is restricted to only Indian-owned and controlled entities.

**Economic zones**

18 Are there economic zones or other special programmes in this jurisdiction commonly utilised by foreign defence and security contractors for financial or other procurement related benefits?

The government is in the process of establishing defence manufacturing corridors in the states of Tamil Nadu and Uttar Pradesh in India. Apart from these two industrial corridors, several states have identified and allocated land for defence manufacturing. Establishing an industrial unit in these designated corridors does not provide any specific tax incentives but significantly reduces the administrative cost and effort to establish a business.

Industrial units established for export purposes are permitted a host of exemptions, available at both central and state level, which include benefits such as exemption from input taxes and refund of output taxes. State governments may also offer subsidised electricity rates and waiver of fees and approvals.

**Forming legal entities**

19 Describe the process for forming legal entities, including joint ventures, in this jurisdiction.

Legal entities such as companies and limited liability partnerships are formed under the procedures defined under their respective legislation. The standard process involves applying with the name of the proposed legal entity, the antecedents of the promoters, the proposed capital and the name, objects and by-laws governing the legal entity.

Joint ventures can be incorporated or unincorporated in nature. Unincorporated joint ventures are formed by parties without setting up a separate legal entity and are typically governed by the contractual terms between the party for the venture. Incorporated joint ventures follow the process outlined above for the formation of legal entities.

In incorporated joint ventures, the ownership of the legal entity is governed by the shareholder agreements incorporated into the by-laws of the legal entity. Foreign ownership in joint ventures engaged in defence manufacturing is subject to ownership restrictions according to the foreign investment norms of India. Recently, the government has announced an increase in foreign ownership from 49% to 74%, which has been a widely acclaimed reform. However, investment proposals are subject to clearance from a national security perspective.

**Access to government records**

20 Are there statutes or regulations enabling access to copies of government records? How does it work? Can one obtain versions of previous contracts?

The Right to Information Act 2005 (RTI) empowers any citizen of India to request information and documents pertaining to the functioning of a government ministry or department, including government-owned enterprises and autonomous organisations. However, the RTI mechanism contains certain exceptions based on which the government can deny the request for information. These exceptions include disclosure of information likely to compromise the national security of India, commercial and trade secrets, confidential information relating to the parliament or state legislatures, information likely to impede a running investigation, information likely to endanger the life or physical safety of any person, etc.

To obtain information under the RTI mechanism, the applicant (being an Indian citizen) is required to apply online on the RTI website of the relevant ministry or department. Each ministry and department is required to have a designated Public Information Officer (PIO), who reviews the application and decides whether the disclosure of the information would be subject to any of the exceptions under law. Subject to such determination, the PIO will either supply or deny the sharing of information with the applicant. In case of denial of information, the applicant may enter the appeal process to argue against withholding of the information.

RTI applications seeking specific information or contracts from the MoD are likely to be denied under the exception for national security. In the event any vendor specific information is sought to be obtained from the MoD, the MoD would be statutorily bound to seek the consent of the third party before offering such information.

**Supply chain management**

21 What are the rules regarding eligible suppliers and supply chain management and anti-counterfeit parts for defence and security procurements?

Each request for proposal issued by the MoD is required to mention the applicable procurement category, which may, in turn, specify the eligibility criteria of suppliers. For example, procurements under the Indian Designed Developed and Manufactured category can only be undertaken from companies owned and controlled by resident Indian nationals. In certain procurements, the MoD may also specify financial eligibility criteria to ensure the capability of suppliers to fulfil the contract. Entities related to blacklisted suppliers are also frequently denied participation in procurements under the DAP.

In terms of supply chain management, bidders for procurements under the DAP are required to assume responsibility for misconduct or non-performance by entities in their supply chain, including sub-vendors and offset partners. Therefore, the discovery of any counterfeit parts by the MoD is likely to be considered as a material breach of the contract by the main contractor under the principal supply contract.

## INTERNATIONAL TRADE RULES

**Export controls**

22 What export controls limit international trade in defence and security articles? Who administers them?

Export controls in India are specified under the Foreign Trade Policy issued by the Ministry of Commerce and administered through the office of the Director General Foreign Trade (DGFT).

Defence and security articles are defined under the Special Chemicals, Organisms, Materials, Equipment and Technology (SCOMET) list. The SCOMET list identifies categories of dual-use and military goods and technologies considered sensitive and requiring protection from unauthorised proliferation. These export controls have been instituted in pursuance of India's entry into multilateral non-proliferation treaties including the Wassenaar Arrangement and the Australia Group.

To undertake exports of SCOMET articles, an exporter is required to apply for authorisation to the DGFT. The application is reviewed by an inter-ministerial group to assess the end use and adequacy of proliferation controls in the destination country. The process usually takes 45 to 60 working days.

**Domestic preferences**

23 What domestic preferences are applied to defence and security procurements? Can a foreign contractor bid on a procurement directly?

Defence and security procurements, whether under the GFR or the DAP, have a stated preference for domestic suppliers. Under the GFR, all procurements of a specified threshold value and available from domestic suppliers are required to be fulfilled from such suppliers. For larger procurements, the government is required to exhaust domestic suppliers

before considering foreign vendors. The preference for domestic sources includes requiring goods and services to incorporate a specified percentage of local content by value.

The DAP also specifies a preference for domestic suppliers. During the categorisation phase of initiating a procurement under the DAP, the MoD evaluates sources for procuring the articles and typically opts for categories allowing only domestic bidders, if such suppliers are available. Procurements from domestic suppliers also incorporate local content norms provided under the DAP. Global bids are invited if the domestic industry is unable to supply the articles. In a global tender, foreign vendors are permitted to bid independently or in partnership with an Indian entity. However, participating with an Indian entity in a global tender does not accord any preference to the bidder.

**Favourable treatment**

24 | Are certain treaty partners treated more favourably?

Defence procurements undertaken by India have historically not been linked to any bilateral or multilateral treaties. Recently, India has executed several agreements with the United States for cooperation in military logistics and communications interoperability. However, adherence to the agreements is not contingent on either country procuring defence products and articles from each other.

**Sanctions**

25 | Are there any boycotts, embargoes or other trade sanctions between this jurisdiction and others?

India has implemented trade sanctions announced by the United Nations Security Council. Therefore, India prohibits trade in specified goods with the Republic of Iran, Democratic People's Republic of Korea, the Islamic Republic of Iran and Somalia. Further, India does not trade with the Islamic State and Al-Qaeda affiliates. It is relevant to highlight that India does not recognise unilateral sanctions imposed by any individual country.

**Trade offsets**

26 | Are defence trade offsets part of this country's defence and security procurement regime? How are they administered?

Offsets are applicable to procurements under the Defence Acquisition Procedure (DAP) undertaken from foreign sellers and valued higher than 20 billion rupees, with exceptions for single-vendor situations and inter-government procurements. The governing principles for offsets are specified in the offset guidelines under the DAP and are administered by a specialised body under the supervision of the Ministry of Defence (MoD), called the Defence Offsets Management Wing (DOMW). The DOMW has the following primary roles in the procurement process:

- formulating the offset guidelines;
- monitoring the discharge of offset obligations (including audit and review of yearly progress);
- participating in the technical and commercial evaluation of offset proposals; and
- administrating penalties under offset contracts.

The standard offset obligation is defined as 30 per cent of the value of the procurement contract but may be higher subject to the discretion of the MoD. Offset obligations may be discharged through specified routes in the DAP, including the purchase of eligible products and services from the domestic industry, direct equity investment or supply of equipment to defence companies in India, transfer of technology to Indian companies, etc. The offset norms have undergone significant revisions with the DAP 2020 compared to previous iterations. The notable changes include enhanced multipliers for various offset routes, an overhaul of the list of products and services eligible for discharge of offsets, and improved viability of transfer of technology and investment-in-kind routes.

In terms of the procurement process, offset obligations are incorporated into the request for proposal issued by the MoD to eligible vendors. As part of the bid submissions, bidders are required to submit separate technical and commercial offset proposals for the same. The vendor is required to select eligible Indian partners and notify the quantum of offsets that will be fulfilled through each partner. The vendor may modify its Indian partners and their share of the offsets, subject to the overall offset obligation remaining the same.

The vendor has to undertake the mandatory compliance to submit rolling claims to the DOMW along with documentary evidence in support of the claim of the fulfilment of offsets. If the vendor is unable to meet its offset obligations within the prescribed period, the MoD may choose to terminate the main contract, impose liquidated damages and blacklist or suspend dealings with the vendor for future contracts.

## ETHICS AND ANTI-CORRUPTION

**Private sector appointments**

27 | When and how may former government employees take up appointments in the private sector and vice versa?

Government employees may take up appointments in the private sector either by taking voluntary retirement or after reaching the age of superannuation, subject to service rules applicable to their employment. Service rules typically specify a period between one to two years of retirement, within which the employee must take prior permission from the government to take appointments in the private sector. After such period, government employees are not required to take permission but may be required to make certain declarations to their parent organisation before accepting appointments.

Employment with the government in India is undertaken through entrance tests. As employment with the government is a career decision, the government does not have a mechanism to employ people from the private sector beyond the selection process. Appointments from the private sector are usually undertaken on temporary contractual basis for advisory positions in special committees and task forces.

**Addressing corruption**

28 | How is domestic and foreign corruption addressed and what requirements are placed on contractors?

Government procurements in India are required to adhere to a high standard of ethical conduct. All procurement frameworks prohibit both buyers and sellers from engaging in any activity that may be construed as having influenced the decision to award the contract.

The scope of such activities includes the offer or supply of any bribe, gift, consideration, reward, favour, any material or immaterial benefit or other advantages to government officials involved in the bidding process with a view to inducing awarding the contract to a vendor. Further, bidders are prohibited from engaging any person to intercede, facilitate or recommend the award of the contract. Collusion between bidders to influence the outcome of the procurement also constitutes unethical conduct under the procurement frameworks.

For defence and security procurements under the DAP, prospective bidders are required to submit a legal undertaking, in the form of an Integrity Pact, to refrain from unethical and corrupt activities specified in the regulations. Further, bidders are also required to furnish a bank guarantee as security against such conduct. If the MoD gains knowledge of the bidder having engaged in such activities, the bank guarantee is typically invoked in addition to blacklisting, suspending dealings and initiating punitive proceedings under any other law.

### Lobbyists

29 What are the registration requirements for lobbyists or commercial agents?

The General Financial Rules 2017 (GFR) provides that each procuring ministry may require agents to be registered in such manner as the ministry may prescribe. Therefore, the requirement for registration of agents varies across ministries. Typically, the use of agents in procurements would either require registration or be prohibited completely.

The procurements by the MoD under the DAP require mandatory registration of commercial agents. The process of registration involves applying to the MoD with details of the bidder and its agents, including the contractual and commercial terms agreed between the parties. Failure to register or declare agents would attract penal implications that extend to fines, rescinding of contract or blacklisting of a vendor from future procurements.

### Limitations on agents

30 Are there limitations on the use of agents or representatives that earn a commission on the transaction?

Depending on the framework applicable to the procurement, commission structures for agents are either regulated or prohibited. Further, where permitted, the scope of the agent's role plays an important part in determining whether the commission arrangement steps into the boundaries of unethical conduct. Most procurement frameworks read with applicable vigilance guidelines prohibit remuneration for an agent based on the success or failure in obtaining a contract.

## AVIATION

### Conversion of aircraft

31 How are aircraft converted from military to civil use, and vice versa?

India does not have a clearly defined legislative framework for conversion of military aircraft to civil aircraft and vice versa. A civil aircraft can be deployed for military uses, subject to requisite permissions from the Ministry of Defence (MoD).

Military aircraft sought to be used either temporarily or permanently for civil purposes would require registration with the Directorate General of Civil Aviation (DGCA). Further, such aircraft would be subject to compliances and applicable standards under the Aircraft Act 1934, the Aircraft Rules 1937 and the Civil Aviation Requirements prescribed by the DGCA.

### Drones

32 What restrictions are there on manufacture and trade of unmanned aircraft systems or drones?

Manufacturing unmanned aircraft systems (UAS) is a regulated activity and requires both the product and the manufacturing facility to be licensed by the Ministry of Commerce. The sale and operation of unmanned aircraft are regulated by the DGCA. The DGCA categorises UAS based on their weight and flying range and provides for specific operational conditions for each category of UAS. Any person seeking to use unmanned aircraft in India is required to obtain an operators permit from the DGCA.

From an international trade perspective, both import and export of UAS are restricted. Import of UAS into India requires a licence from the DGCA, whereas exports are subject to restrictions under the Wassenaar Arrangement and require prior authorisation from the Ministry of Commerce.

## MISCELLANEOUS

### Employment law

33 Which domestic labour and employment rules apply to foreign defence contractors?

Domestic labour and employment rules are not applicable to companies that do not have any presence in India. The labour and employment laws are applicable to entities that have been incorporated under the laws of India or have a presence in the country through a permanent establishment.

India has mature jurisprudence with respect to labour and employment laws, and the applicability of the laws varies based on the nature and size of the business. The Indian labour and employment laws cover aspects such as minimum wages, employee remuneration including bonus and gratuity, health and life insurance benefits, employee safety, maternal benefits, etc. The government has recently announced significant reforms in labour and employment laws, which are expected to be made effective over 2021.

### Defence contract rules

34 Are there any specific rules that contractors, foreign or domestic, are bound by in defence contracts?

Defence contracts are governed by the procurement framework governing the transaction (ie, the Defence Acquisition Procedure (DAP) or the Defence Procurement Manual (DPM)) read with advisories from the Central Vigilance Corruption, the apex anti-corruption monitoring institution in India. Accordingly, defence contractors are bound by the terms of the contract, which in turn is derived from the procurement framework.

35 Do contractors avail themselves of these rules when they perform work exclusively outside of the jurisdiction?

Defence procurement frameworks, such as the DAP, are not expressly extra-territorial in their scope and applicability. However, any act undertaken at any place in violation of undertakings and representations given by the contractor in the procurement process would entail the Ministry of Defence (MoD) exercising its contractual rights, which include the right to cancel the tender or terminate the contract, blacklist the vendor, invoke bank guarantees and initiate criminal prosecution in India.

### Personal information

36 Must directors, officers or employees of the contractor provide personal information or certify that they fulfil any particular requirements to contract with a government entity?

The General Financial Rules 2017 (GFR) and the DAP do not require directors, officers and employees of the contractor to provide personal information or certifications. However, the government reserves the discretion to require key management personnel of the contractor to submit information in certain eventualities, for example, foreign citizens visiting secured facilities are required to submit personal information for verification by the Ministry of Home Affairs.

### Licensing requirements

37 What registration or licensing requirements exist to operate in the defence and security sector in the jurisdiction?

Foreign vendors supplying defence and security articles manufactured outside India are typically not required to procure registrations or licences in India. Registration and licensing requirements are triggered

if the operations involve import, manufacture or sale of regulated defence and security articles in India. The licensing requirements are extensive and vary based on the nature of the product, nature of activity, distribution model and location of operations.

**Environmental legislation**

38 | What environmental statutes or regulations must contractors comply with?

Environmental safety in India is administered and enforced both by the central government and the state government. The regulations apply to manufacturing and production activities undertaken in India. Such activities necessitate compliance with air, ground and water standards and may require industries to install specialised pollution control equipment or establish emission treatment plants. Environmental regulations also apply to the importation of hazardous substances (including chemicals); however, the burden of compliance for such imports is on the importer and not the foreign supplier.

The principal legislation that governs environmental protection is the Environmental Protection Act 1986, the Water (Prevention and Control of Pollution) Act 1974 and the Air (Prevention and Control of Pollution) Act 1981 and the rules framed under these laws. The environmental law regulations also include specialised legislation that is applicable to specific industries.

39 | Must companies meet environmental targets? What are these initiatives and what agency determines compliance?

Entities that have industrial facilities in India are required to adhere to applicable environmental norms on emissions and waste disposal, enforced jointly by the Central Pollution Control Board and the State Pollution Control Boards constituted under environmental legislation. Failure to meet compliance is strictly enforced and can result in heavy penalties and closure of units.

40 | Do 'green' solutions have an advantage in procurements?

India does not recognise environmental responsibility as a qualification or procurement criteria, therefore 'green' solutions do not receive any preference consideration nor provide any other advantage in government procurement.

## UPDATE AND TRENDS

**Key developments of the past year**

41 | What were the key cases, decisions, judgments and policy and legislative developments of the past year?

There were two key developments for the defence and security sector in India over the past year. The first is the release of the Defence Acquisition Procedure 2020 (DAP), which introduced significant changes in the offset norms and new categories of procurement, such as leasing, in addition to changes in the standard contract provisions and other procedural reforms. The DAP reflects the preference to domestic sources of critical equipment and platforms, while also enhancing foreign vendors' abilities to discharge offsets in global tenders.

The second key development is the proposed increase in foreign investment limits in the Indian defence manufacturing industry from 49 per cent to 74 per cent. While the increased limits bode well for foreign vendors seeking to establish partnerships with Indian companies, the increased limits come with notable riders including enhanced discretionary powers to the government to review investments on national security grounds. Subject to necessary approvals, foreign vendors can now transition to majority control over their existing investments and partnerships in India.

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**Coronavirus**

42 | What emergency legislation, relief programmes and other initiatives specific to your practice area has your state implemented to address the pandemic? Have any existing government programmes, laws or regulations been amended to address these concerns? What best practices are advisable for clients?

The Ministry of Defence (MoD) has extended all existing contracts, including delivery timelines, by a period of four months in view of difficulties faced by the industry during the pandemic. Accordingly, the period between 25 March 2020 to 24 July 2020 was deemed to be a force majeure event, which would not be factored into delays by the vendor in achieving delivery timelines. Vendors were also not subject to the imposition of contractual liquidated damages during this period.

It is relevant to highlight that the four-month extension is not automatically applicable to contracts with foreign vendors, who are required to approach the MoD to seek the extension based on the circumstances in their country. Foreign vendors are thus advised to specifically seek such extensions from the MoD. It is recommended that domestic vendors also notify the MoD of the revised timelines under their existing contracts.

# Italy

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## LEGAL FRAMEWORK

### Relevant legislation

1 | What statutes or regulations govern procurement of defence and security articles?

Procurement of defence and security works, equipment and services by contracting authorities in Italy is regulated by legislative decree 20 April 2016, No. 50, sections 159-163, (the Public Procurement Code (PPC)), enacting European Union public procurement directives 2014/23, 2014/24 and 2014/25/EU. The PPC, in principle, applies to all public procurement contracts but carves out defence and security procurement which falls under special legislation. Legislative decree 15 November 2011, No. 208, the Military Procurement Code (MPC), which enacted EU Directive 2009/81/EC, is considered a special set of procurement rules applicable to certain defence and security contracts that prevails over the general PPC rules. The MPC, however, mostly makes selective references to the general PPC rules, introducing minor deviations. There are defence and security contracts that may fall outside the scope of both the PPC and MPC and are only subject to general EU Treaty principles. The Italian Ministry of Defence has published two enactment regulations, one for contracts under MPC (presidential decree 13 March 2013, No. 49) and one for contracts under the PPC (presidential decree 15 November 2012, No. 236).

### Identification

2 | How are defence and security procurements identified as such and are they treated differently from civil procurements?

The subject matter of the contract (ie, military/classified items; works, supply and services related to military/classified items; works and services aimed at specific military purposes) determines the application of the MPC to contracts above EU special thresholds (currently €428,000 for supply and services and €5,350,000 for works). The MPC introduces several exceptions to general PPC rules. Such exceptions are mostly aimed at guaranteeing the necessary level of protection for security and defence interests involved in defence and security contracts by ensuring that sensitive information is not divulged and is not handled by economic operators who have not obtained the necessary security clearances.

### Conduct

3 | How are defence and security procurements typically conducted?

General principles of the Treaty on the Functioning of the European Union (TFEU) apply to all defence and security procurement. Three of the five types of tender procedures envisioned by the civil procurement rules – restricted, negotiated with or without a prior notice and competitive dialogue – are provided for by the MPC.

The publication of a notice or a request for offers is the usual start of the procedure, followed by the submission of documents showing the financial standing, technical capability and (where required) possession of security clearances by the candidates or tenderers. Such a pre-qualification phase may or may not be run jointly with the submission of technical and economic bids, with the most economically advantageous tender being the more frequent award criterion. However, contract terms and conditions are unilaterally drafted by contracting authorities and are almost invariably non-negotiable. As such, terms and conditions are advertised when soliciting requests for participation and bids, and often economic operators can only decide whether they are willing to accept them and submit an offer or whether they would rather not participate in the tender.

The assessment of bids is based on objective, transparent and non-discriminatory criteria. In particular, when the award follows a competitive bidding procedure, equality of treatment and transparency principles require that no substantial modification of the contract is permitted without a retender.

### Proposed changes

4 | Are there significant proposals pending to change the defence and security procurement process?

Article 8, paragraph 11, of Law Decree 16 July 2020, No. 76 (the Simplifications Decree), converted with amendments by Law 11 September 2020 No. 120, provides that the Italian government has to approve an enactment regulation relating to defence and security procurements. No such regulation has been approved yet.

### Information technology

5 | Are there different or additional procurement rules for information technology versus non-IT goods and services?

No. Information technology goods and services may fall under the PPC or MPC, depending on the subject matter of the contract.

### Relevant treaties

6 | Are most defence and security procurements conducted in accordance with the GPA or other treaty-based procurement rules, or does this jurisdiction commonly use the national security exemption to procure them?

The MPC is based on TFEU principles and the number of contracts that do not fall under either the MPC or the PPC is limited. Italian courts consider the general exception provided by article 346 TFEU as an exception to be narrowly interpreted and affirm the applicability of TFEU principles to all defence and security procurement.

## DISPUTES AND RISK ALLOCATION

### Dispute resolution

7 How are disputes between the government and defence contractor resolved?

Disputes concerning the award procedure are reserved for administrative courts, which have general jurisdiction on the award of public procurement contracts. Disputes concerning contractual obligations are reserved for civil courts. Arbitration and out-of-court settlement procedures are permitted only in relation to contractual obligations.

8 To what extent is alternative dispute resolution used to resolve conflicts? What is typical for this jurisdiction?

There is no specific rule on the use of alternative dispute resolution (ADR) in the Military Procurement Code (MPC). ADR models (eg, arbitration and amicable settlement) are provided by the Public Procurement Code (PPC) and are applicable to defence and security contracts. The use of arbitration – which is only admissible if it is provided for in the initial tender notice or invitation and is authorised by the governing body of the contracting authority – is very common in works and long-term supply-and-service contracts, and is used more frequently in disputes between contractors and subcontractors than between contracting authorities and prime contractors.

Arbitrators have to be registered with the Arbitration Chamber managed by the Italian National Anti-Corruption Authority (ANAC), which acts as a regulator of public procurement.

### Indemnification

9 What limits exist on the government's ability to indemnify the contractor in this jurisdiction and must the contractor indemnify the government in a defence procurement?

General rules on limitation of liability set out by the Italian Civil Code render invalid any limitations covering grossly negligent or wilful conduct. Contracting authorities are liable for non-performance, but normally do not provide any indemnity for contractors. Contractors are usually required to indemnify the contracting authority in relation to several issues that may cause liability during contract performance, mainly resorting to insurance policies (eg, third-party claims, product liability and personnel protection).

### Limits on liability

10 Can the government agree to limit the contractor's liability under the contract? Are there limits to the contractor's potential recovery against the government for breach?

Public contracts awarded by contracting authorities – including military and defence contracts – generally do not provide limitations on liability, and such limitations cannot be negotiated once the contract is awarded, as they would amount to an impermissible modification of the contract.

There is no statutory limitation on the ability of the contractor to recover against a contracting authority for breach of contract, and, in general, the burden of proof when asserting government liability is less strict than the one applicable to private parties.

### Risk of non-payment

11 Is there risk of non-payment when the government enters into a contract but does not ensure there are adequate funds to meet the contractual obligations?

The risk of non-payment exists as in any other public contract. However, normally defence and security procurement procedures are launched only after the necessary funds are secured by the relevant administration. There is no specific rule prioritising payments to prime contractors, while general procurement contracts rules make it possible for subcontractors to obtain payment directly from the contracting authority if the prime contractor fails to fulfil its obligations.

### Parent guarantee

12 Under what circumstances must a contractor provide a parent guarantee?

The only guarantees that are required in relation to the performance of a public procurement contract are bank guarantees or insurance guarantees. The requirement of a parent company guarantee is not envisioned by PPC or MPC rules.

## DEFENCE PROCUREMENT LAW FUNDAMENTALS

### Mandatory procurement clauses

13 Are there mandatory procurement clauses that must be included in a defence procurement contract or that will be read into the contract regardless of their actual inclusion?

The standard draft contract, which is set forth as an attachment to the contract notice, or the invitation to tender, is non-negotiable, but, pursuant to a general Civil Code principle, clauses declared mandatory by a statute have to be read into a contract regardless of their actual inclusion. There are no defence- or security-specific clauses, the inclusion of which is required or automatic. In public procurement contracts in general, the most well-known mandatory clauses provided by national legislation are those concerning the traceability of payments (aimed at making every transfer of monies paid from the contracting authority traceable through the chain of subcontractors and suppliers of the prime contractor) and the clauses making it mandatory for successful tenderers to ensure employment continuity for personnel of past contractors (also known as 'social' clauses).

### Cost allocation

14 How are costs allocated between the contractor and government within a contract?

Cost allocations between the government and contractor are usually defined by the contract itself, preferably through a fixed or firm price mechanism.

### Disclosures

15 What disclosures must the contractor make regarding its cost and pricing?

Cost and price assessments are common, with at least three main purposes.

Within a competitive tender procedure, they may be aimed at verifying whether a price/offer by a tenderer is reliable and sustainable, and has not been the result of optimistic assumptions or underestimated costs (abnormally low tenders). Such an assessment is also aimed at verifying whether mandatory costs have been factored into the price offered by a potential supplier (eg, minimum wages for the workforce,

or costs that cannot be subject to rebates as those necessary to ensure compliance with rules on health and safety on the workplace).

Within a non-competitive negotiated procedure, a cost analysis based on information disclosed by the prospective contractor according to Ministry of Defence guidelines is aimed at establishing the price for the goods and services to be purchased.

During the execution of a procurement contract, they may be aimed at establishing new prices for unforeseen additional goods and services required by the contracting authority and price adjustments required by unforeseen circumstances.

**Audits**

16 | How are audits of defence and security procurements conducted in this jurisdiction?

General Public Procurement Code (PPC) rules afford contracting authorities with wide powers to audit and inspect contractors' activities to verify their performance. Cost and price assessments are also routinely carried out, especially in long-term contracts associated with military programmes. There is no limitation or timeline that can predict when audits or assessments will be carried out. The Italian National Anti-Corruption Authority (ANAC) – the anti-bribery independent authority, which also acts as the public procurement sector regulator and enforcer – also has supervisory powers and may request information and conduct inspections in relation to tender procedures and procurement contracts performance.

**IP rights**

17 | Who gets the ownership rights to intellectual property created during performance of the contract? What licences are typically given and how?

There are no statutory rules allocating intellectual property rights created during the performance of a defence and security procurement contract differently from any other procurement contract. If the intellectual property is the result of contracted research and development activity it will be owned by the contracting authority. Otherwise, unless there are specific provisions in the contract, it will be owned by the contractor.

**Economic zones**

18 | Are there economic zones or other special programmes in this jurisdiction commonly utilised by foreign defence and security contractors for financial or other procurement related benefits?

We are not aware of any such economic zones or programmes in Italy.

**Forming legal entities**

19 | Describe the process for forming legal entities, including joint ventures, in this jurisdiction.

Joint ventures can be formed by mere contractual agreements, without creating a new entity, when parties enter into cooperation agreements. Corporate joint ventures can be created by incorporating a company pursuant to the Civil Code. In general, while contractual joint ventures can be created by the parties without resorting to a public notary, corporate joint ventures require the assistance of a public notary. The public notary takes care of validating the articles of association and the company by-laws, registering the new entity with the Company Register.

**Access to government records**

20 | Are there statutes or regulations enabling access to copies of government records? How does it work? Can one obtain versions of previous contracts?

Access to public administration documents is generally allowed for interested parties by national legislation on transparency and on administrative procedures (Law 7 August 1990, No. 241 and Legislative Decree 25 May 2016, No. 97). The PPC also provides specific rules granting access to public procurement procedures documents. Restrictions apply during the tender procedure, but after the award, any information that is not covered by trade or commercial secrets, or is not classified, can be disclosed upon request, including versions of previous contracts. A trend towards enhanced transparency in public contracts is underway, with recent legislation stating that most information on public contracts has to be published on contracting authorities' websites and that any citizen may obtain information on public contracts without providing any specific reason or interest.

**Supply chain management**

21 | What are the rules regarding eligible suppliers and supply chain management and anti-counterfeit parts for defence and security procurements?

Eligibility of suppliers in defence and procurement is subject to the same criteria provided by the PPC and EU procurement directives, with limited deviations. Contractors having people convicted of particular crimes, including terrorism, fraud, bribery and money laundering cannot participate in public tenders. Furthermore, financial, technical and professional requirements proportionate to the public tender subject matter can be set by the contracting authority to select eligible suppliers. Similar rules apply also to subcontractors. Technical and professional requirements may also refer to the supply chain characteristics.

## INTERNATIONAL TRADE RULES

**Export controls**

22 | What export controls limit international trade in defence and security articles? Who administers them?

Pursuant to EU general rules on the export of military and dual-use items, national enactment legislation (Law 9 July 1990, No. 185 for military items and Legislative Decree 15 December 2017, No. 221 for dual-use items) provides a licensing framework for exports and, in certain cases, for intra-EU transfer of controlled items and technology. Separate directorates of the Ministry of Foreign Affairs are responsible for the issue of export licenses, while Italy's customs and law enforcement agencies are responsible for policing and enforcement.

Italy does not maintain national controlled items lists that differ from the EU Military list and the Annexes to EU dual-use regulation (No. 428/2009).

**Domestic preferences**

23 | What domestic preferences are applied to defence and security procurements? Can a foreign contractor bid on a procurement directly?

The PPC and the Military Procurement Code (MPC) do not provide any domestic preference rules, but, as in other countries, when such rules do not apply, it is not uncommon that contracts are directly awarded to national contractors.

**Favourable treatment**

24 | Are certain treaty partners treated more favourably?

Agreement on Government Procurement signatories, EU members and countries that have bilateral treaties with Italy granting reciprocity of treatment are the only partners who may participate in defence and security procurement procedures launched by Italian contracting authorities.

**Sanctions**

25 | Are there any boycotts, embargoes or other trade sanctions between this jurisdiction and others?

Italy has no boycott, embargo or trade sanctions in place other than those imposed by the EU, pursuant to United Nations general positions. The responsibility for related policy measures lies with the Ministry of Foreign Affairs, while the Ministry of Economy is responsible for financial measures and enforcement.

**Trade offsets**

26 | Are defence trade offsets part of this country's defence and security procurement regime? How are they administered?

Trade offsets are part of the Italian defence and security procurement regime and were regulated by two Ministry of Defence directives of 2002 and 2012. Industrial compensation is, however, currently less frequent due to their inherent limited compatibility with EU rules.

## ETHICS AND ANTI-CORRUPTION

**Private sector appointments**

27 | When and how may former government employees take up appointments in the private sector and vice versa?

National civil service regulation (Legislative Decree 30 March 2001, No. 165) forbids employees leaving public service from accepting private employment in industries that are subject to the regulatory or supervisory powers of their former office for three years after termination of their employment (the anti-pantouflage rule). In the event of an infringement, both the former civil servant and the private employer risk serious penalties. There is no reverse prohibition, save for general rules aimed at preventing conflicts of interest.

**Addressing corruption**

28 | How is domestic and foreign corruption addressed and what requirements are placed on contractors?

Bribery and international bribery are punished as criminal offences with incarceration and financial penalties by the Italian criminal code. Bribes can take the form of monetary payments or any other advantage. Giving, offering or agreeing to give a bribe is an offence, as is accepting, asking for or agreeing to accept a bribe.

Public administrations are bound to adopt procedures, ethics codes, and organisation models specifically aimed at preventing corruption, pursuant to law 6 November 2012, No. 190. The Italian National Anti-Corruption Authority (ANAC) has anti-bribery enforcement powers and regulates the public procurement sector.

**Lobbyists**

29 | What are the registration requirements for lobbyists or commercial agents?

Italy does not have specific legislation on lobbying. Minimal measures have been introduced in parliament regulations for lobbyists active in the rulemaking process, but a broader set of rules on lobbyists is being discussed by the current political majority and might be the subject of special legislation.

**Limitations on agents**

30 | Are there limitations on the use of agents or representatives that earn a commission on the transaction?

There is no specific statutory limitation on the use of paid intermediaries, but the defence and security procurement system is devised to foster direct participation of undertakings in transparent and non-discriminatory tender procedures. As a result, resorting to local agents, especially for foreign bidders, is not as common as it might be in other jurisdictions, especially because intermediaries not possessing the necessary participation requirements would not be in a position to place bids or participate in tenders.

## AVIATION

**Conversion of aircraft**

31 | How are aircraft converted from military to civil use, and vice versa?

While civil aircraft airworthiness is harmonised throughout the EU, subject to EU regulations and European Union Aviation Safety Agency policing, regulating the airworthiness of military aircraft is largely left to each state. It is, therefore, complicated to convert military aircraft to civil use, but it has been done several times. An example is the EH–101 helicopter (which is now known as the AW101), which was originally designed as a military helicopter but was subsequently certified for civil use. For the same reasons, it might be easier to convert a civil aircraft to military use, even though the higher military requirements have to be met.

**Drones**

32 | What restrictions are there on manufacture and trade of unmanned aircraft systems or drones?

Italy's national rules on drones complement EU regulations on unmanned aerial systems (UAS) recently adopted and expected to enter into force in July 2020 (EU Regulation 2019/45 on unmanned aircraft systems and on third-country operators of UAS and EU Regulation 2019/947 on the rules and procedures for the operation of unmanned aircraft).

The use of drones is regulated by the Italian Civil Aviation Authority (ENAC) which has adopted its own regulation starting from 15 December 2019. This temporary regulation will remain in force until a final regulation enters into force, which is scheduled for 2022.

Military UAS systems are subject to military items restrictions (ie, a government licence is required to manufacture, sell, hold, maintain, import and export such equipment). Military UAS systems are considered strategic assets, therefore entities manufacturing or developing military UAS systems are subject to foreign direct investment restriction provisions set forth by Law Decree 12 January 2012, No. 21. Such provisions afford the government broad special powers to impose conditions or to veto transactions or corporate decisions affecting entities developing UAS technology or manufacturing UAS systems.

## MISCELLANEOUS

### Employment law

33 | Which domestic labour and employment rules apply to foreign defence contractors?

No specific rule applies only to foreign defence contractors. Italian labour legislation applies to any worker habitually working in Italy, irrespective of any choice of law made in the employment contract.

### Defence contract rules

34 | Are there any specific rules that contractors, foreign or domestic, are bound by in defence contracts?

The replies above describe the specific rules applicable to foreign and domestic defence contractors.

35 | Do contractors avail themselves of these rules when they perform work exclusively outside of the jurisdiction?

Rules on defence contracts still apply even if the contractor performs its work outside the jurisdiction.

### Personal information

36 | Must directors, officers or employees of the contractor provide personal information or certify that they fulfil any particular requirements to contract with a government entity?

Yes. When participating in a tender or submitting a bid for entering into a public contract, directors, officers, sole shareholders or majority shareholders and even certain employees have to provide personal information, such as name, date and place of birth of themselves and of persons of legal age living in the same household, for the purpose of allowing anti-organised crime infiltration background checks. Furthermore, the same director, officers, employees, sole or majority shareholders have to file declarations attesting that they have not been convicted of crimes such as bribery, fraud, money laundering or terrorism. Finally, if contracts entail the handling of classified information or items, security clearances need to be obtained through a process that requires disclosing personal information and provided to the contracting authority.

### Licensing requirements

37 | What registration or licensing requirements exist to operate in the defence and security sector in the jurisdiction?

To hold, manufacture, store, maintain, sell military items and technology in Italy, a licence issued by a provincial government office is required. Importing and exporting military items requires that an economic operator is registered in the national register of undertakings operating in the defence sector and that export licences are obtained prior to any import, export or intra-EU transfer transaction. Harsh criminal penalties, including incarceration, can be incurred in the case of infringement.

### Environmental legislation

38 | What environmental statutes or regulations must contractors comply with?

The Italian environmental code (Legislative Decree 3 April 2006, No. 152) sets forth emissions limits, licensing requirements and rules on waste disposal that apply to any works, or production or manufacturing processes. Procurement contracts and tender selection rules can incorporate environmental purposes or require economic operators to meet minimal environmental criteria set out by ministerial decrees.

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39 | Must companies meet environmental targets? What are these initiatives and what agency determines compliance?

There are no special environmental targets set out by defence and security procurement rules. However, environmental targets and criteria can be part of the procurement process. Furthermore, broader environmental targets may derive from general policies (eg, greenhouse gas reduction or renewable energy production increase) or by specific provisions of environmental authorisations, licences and management systems applying to the specific operations of an economic operator involved in the performance of defence and security procurement contracts.

40 | Do 'green' solutions have an advantage in procurements?

Recent legislation on minimal environmental criteria in public procurement contracts allows contracting authorities to award premium points to bids containing environmental-friendly solutions with respect to the production of goods and services and life cycle management. Minimal environmental criteria are set out in the Public Procurement Code's enactment legislation and are updated by the Ministry of Environment, with reference to activity and product categories. Only contract-specific green solutions may grant advantages in the procurement process.

## UPDATE AND TRENDS

### Key developments of the past year

41 What were the key cases, decisions, judgments and policy and legislative developments of the past year?

Law Decree 16 July 2020, No. 76 (the Simplifications Decree), converted with amendments by Law 11 September 2020, No. 120, introduced a number of important temporary and derogatory provisions in order to accelerate public investment by simplifying procurement procedures and lowering thresholds. With regard to the defence and security sector, article 8, paragraph 11 of the Simplifications Decree provides that the Italian government has to approve an enactment regulation relating to a defence and security procurement. No such regulation has been approved yet.

### Coronavirus

42 What emergency legislation, relief programmes and other initiatives specific to your practice area has your state implemented to address the pandemic? Have any existing government programmes, laws or regulations been amended to address these concerns? What best practices are advisable for clients?

In order to address the coronavirus pandemic, public procurement legislation was amended by Law Decree 17 March 2020, No. 18 (the Cura Italia Decree), converted with amendments by Law 24 April 2020, No. 27, which introduced temporary provisions on the awarding and executing of public contracts. Further provisions were included in Law Decree 19 May 2020, No. 34 (the Relaunch Decree). Clients are recommended to constantly monitor the measures taken in the public procurement sector, which is currently characterised by a high level of regulatory changes.

# Japan

**Go Hashimoto and Yuko Nihonmatsu**

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## LEGAL FRAMEWORK

### Relevant legislation

1 What statutes or regulations govern procurement of defence and security articles?

Procurement by the Ministry of Defence is governed by a complex set of laws and regulations stipulated at a country level, such as the Public Accounting Act, as well as official directives and circular notices stipulated independently by the Ministry of Defence. These laws, regulations and official directives undergo reviews following changes in social circumstances and the environment that affect defence and security procurement and other factors. In particular, on 1 October 2015, following the establishment of the Acquisition, Technology and Logistics Agency (ATLA), amendments were made to a large number of related rules and regulations. The main laws and regulations governing the procurement of defence and security articles follow.

**Laws and regulations**

- The Public Accounting Act;
- the Act on Prevention of Delay in Payment under Government Contracts;
- the Act on the Responsibility of Government Employees who Execute the Budget;
- the Cabinet Order on Budgets, the Settlement of Accounts, and Accounting;
- the Temporary Special Provisions of Cabinet Order on Budgets, the Settlement of Accounts, and Accounting; and
- the Rules on Administrative Handling of Contracts.

**Official directives**

- The Official Directive regarding the Implementation of Procurement of Equipment and Services;
- the Official Directive regarding Supervision and Inspection of Procurement Items;
- the Official Directive regarding Calculating Basis for Target Price of Procurement Items; and
- the Detailed Regulations on Administrative Handling of Contracts under the jurisdiction of the Ministry of Defence.

**Official directives of the ATLA**

- The Official Directives regarding Contract Administration at the ATLA;
- the Official Directive regarding Supervision and Inspections of Procurement Items procured by Central Procurement;
- the Official Directive regarding the Administration of Target Price Calculation by the ATLA; and
- the Official Directive regarding Cost Audit Administration by the ATLA.

**Notices, circular notices, etc, of the ATLA**

- The Outline of Contract Administration Handling;
- the Administration Outline for Administration of Target Price Calculation by the ATLA;
- the Administration Outline for Official Directive regarding Cost Audit Administration by ATLA; and
- the Implementation Outline of System Investigation and Import Investigations, etc, for Central Procurement.

### Identification

2 How are defence and security procurements identified as such and are they treated differently from civil procurements?

The procurement of defence and security articles is, for the most part, the responsibility of the ATLA. This agency is subject to official directives and circular notices etc stipulated independently by itself or the Ministry of Defence. In this sense, procurement by the agency is treated separately from civil procurement.

### Conduct

3 How are defence and security procurements typically conducted?

According to the Guidance for Bid and Contract (ATLA Public Notice No. 1 of 1 October 2015, as amended), the procedure for the procurement of defence and security articles can be summarised as follows:

- To become a procurement counterparty, an entity applies to undergo bid participation eligibility screening and completes a screening process. If eligible, the applicant's name is recorded in the register of qualified bidders. The applicant is sent a notice with the results of the eligibility screening.
- If a general competitive bidding procedure is being followed, a public notice is made announcing the procurement. In cases of designated competitive bidding or if a discretionary contract is being offered, a regular notice is sent to the relevant counterparty.
- The selected counterparty pays a bid deposit to the Chief Secretary Treasurer of the ATLA (revenue), unless they are exempt from paying a deposit under the public notice or the regular notice.
- The bid participant, or the government counterparty negotiating a discretionary contract, submits a bid document or an estimate. There is also an electronic bidding and bid-opening system (central procurement).

The bidder offering the lowest tendered price, that is equal to or lower than the target price (or is equal or lower than the target price plus the sum of the consumption tax rate and the local consumption tax rate, expressed as a percentage) is the successful bidder.

However, if the bid is conducted following the Method of Comprehensive Evaluation, the bidder must indicate its price,

performance, capability, technology etc in its application. In these cases, the successful bidder is the bidder:

- that tenders a price within the target price;
- that has the performance, capability, technology etc to meet the requested minimum requirements of the bid, and that are critical to reaching the performance specified in the public notice or public announcement of the bid (including the bid instructions); and
- that receives the highest score out of the bidders, according to the Method of Comprehensive Evaluation.

When the successful bidder is determined (or, in the case of a discretionary contract, when the negotiation results in an agreement), the counterparty submits a contract in accordance with the prescribed procedures and pays the contract deposit (unless they are exempt). The contract is deemed concluded when the certifying officer certifies the contract. Then an officer in charge of 'acts to assume debts' and the counterparty together sign and seal the contract.

**Proposed changes**

4 | Are there significant proposals pending to change the defence and security procurement process?

At the time of writing, no legislative bills have been submitted to the Diet.

**Information technology**

5 | Are there different or additional procurement rules for information technology versus non-IT goods and services?

The Ministry of Defence has established information security management standards by importing international standards commonly used by private companies inside and outside of Japan. The Ministry requires companies that build information systems to implement measures pursuant to such standards (eg, ISO/IEC27001, ISO/IEC27002, JIS27001 and JIS27002), and constantly reviews measures by monitoring international standards and social trends.

In particular, the Ministry contractually requires counterparty companies to implement information security management systems for procurement, consisting of three parts:

- the Basic Policy ('securing information security of procurement of equipment and services');
- the Standards; and
- an (audit) Implementation Outline pursuant to international standards regarding information security management etc.

Implementation of the above measures is ensured through voluntary audits carried out by the company and audits conducted by the Ministry.

Companies that build information systems for the Ministry are required to establish an information security management system similar to the three-part process summarised above. The information security management system and the company building it are subject to audits by the Ministry, pursuant to the (audit) Implementation Outline, to confirm the system complies with the Basic Policy and Standards implemented by the Ministry, and that the information security measures taken in accordance with the Implementation Outline prepared by the company are conducted properly.

The Ministry applies equivalent information security measures to the supply of certain equipment other than information systems.

**Relevant treaties**

6 | Are most defence and security procurements conducted in accordance with the GPA or other treaty-based procurement rules, or does this jurisdiction commonly use the national security exemption to procure them?

The Ministry of Defence is subject to the Agreement on Government Procurement (GPA) and procurement of defence and security articles is conducted in accordance with the GPA. Further, government procurement is regulated by economic partnership agreements (EPAs) and therefore must be conducted in accordance with them. EPAs that Japan is a party to include:

- the Comprehensive and Progressive Agreement for Trans-Pacific Partnership;
- the Japan–Australia EPA;
- the Japan–Chile EPA;
- the Japan–European Union EPA;
- the Japan–India EPA;
- the Japan–Indonesia EPA;
- the Japan–Mexico EPA;
- the Japan–Peru EPA; and
- the Japan–Philippines EPA.

## DISPUTES AND RISK ALLOCATION

**Dispute resolution**

7 | How are disputes between the government and defence contractor resolved?

In addition to regular litigation proceedings, complaints regarding government procurement can be resolved at the Office for Government Procurement Challenge System (CHANS) established by the Cabinet Office.

There are no special dispute resolution procedures that are only applicable to defence and security contractors.

8 | To what extent is alternative dispute resolution used to resolve conflicts? What is typical for this jurisdiction?

Litigation is the typical method used to resolve conflicts, and out-of-court dispute resolutions are rarely used. Since 1996, there have been no cases filed with CHANS against the Ministry of Defence.

**Indemnification**

9 | What limits exist on the government's ability to indemnify the contractor in this jurisdiction and must the contractor indemnify the government in a defence procurement?

Indemnity by the government is conducted in accordance with article 29, paragraph 3 of the Constitution.

However, the government is not allowed to enter into guarantee agreements with respect to liabilities owed by companies or other juristic persons (article 3 of the Act on Limitation of Government Financial Assistance to Juridical Persons). However, in a court precedent (Yokohama District Court, Judgement, November 15, 2006; HT(1239)177), a loss indemnity agreement by a local government was deemed null and void as being in breach of article 3 of the Act on Limitation of Government Financial Assistance to Juridical Persons.

The liability of a contractor under a defence and security articles procurement agreement is provided in the contract it entered into with the government. However, the government would rarely claim indemnity from a contractor unless required to in the Civil Code (eg, defect liabilities, etc).

**Limits on liability**

10 Can the government agree to limit the contractor's liability under the contract? Are there limits to the contractor's potential recovery against the government for breach?

There are no laws or regulations that restrict the government from limiting the liability of a defence and security articles contractor under a contract, or to restrict the defence and security articles contractor from recovering loss or damages from the government owing to a breach of contract. Limitations, if any, are subject to the terms and conditions of each contract.

**Risk of non-payment**

11 Is there risk of non-payment when the government enters into a contract but does not ensure there are adequate funds to meet the contractual obligations?

When the government enters into a procurement contract, it must normally conduct an 'act to assume national treasury debts' (article 15 of the Fiscal Act). As the necessary budget is secured by this act, there is no risk of non-payment.

**Parent guarantee**

12 Under what circumstances must a contractor provide a parent guarantee?

A parent guarantee is necessary if it is clearly required under the bid terms. A parent guarantee may be required when the procurement is conducted through a special purpose vehicle, for example.

## DEFENCE PROCUREMENT LAW FUNDAMENTALS

**Mandatory procurement clauses**

13 Are there mandatory procurement clauses that must be included in a defence procurement contract or that will be read into the contract regardless of their actual inclusion?

When the government determines the successful bidder in a tender or the counterparty to a discretionary contract, the contract officer, among others, must prepare a written contract that includes the particulars of the purpose of the contract, the contract price, performance period and contract guarantee, and other necessary matters (article 29–8, paragraph 1 of the Public Accounting Act and article 100 of the Cabinet Order on Budgets, the Settlement of Accounts, and Accounting). For the Ministry of Defence, a contract must be prepared for 'each successful bid, etc', and must be prepared for all defence and security articles, without exception.

Further, a contract will not become final and binding until signed and sealed by both the contract officer and the counterparty, and the preparation of a written contract by such signing and sealing is one of the requirements for the conclusion of contracts.

There are no particular clauses that would be read into a contract without actually being included therein.

**Cost allocation**

14 How are costs allocated between the contractor and government within a contract?

The General Terms and Conditions published by the Ministry of Defence do not refer to contract expenses. It is considered normal for each party to bear its own expenses.

**Disclosures**

15 What disclosures must the contractor make regarding its cost and pricing?

The contractor must submit a bid form or an estimate sheet to the Ministry of Defence.

The contractor has no legal obligation to disclose any information, but when the government enters into certain contracts specified by a cabinet order or statute that cause expenditures to be incurred by the national government, the government must publish information concerning the contract price, among other things.

**Audits**

16 How are audits of defence and security procurements conducted in this jurisdiction?

As part of an effort throughout the government to 'ensure the appropriateness of public procurement', the Ministry of Defence has been expanding the use of the Method of Comprehensive Evaluation and streamlining its bidding procedures. In addition, in response to a number of cases in 2012 of overcharging and manipulation of product test results by contractors, the Ministry of Defence has been working on measures to prevent a recurrence of these problems, such as enhanced system inspections, reviewing penalties and ensuring the effectiveness of supervision and inspections, and is putting more effort into the prevention of misconduct, improving fairness and transparency and ensuring contracts are appropriate.

Further, with the aim of strengthening checks and balances, the Acquisition, Technology and Logistics Agency (ATLA) has established an Audit and Evaluation Division to carry out internal audits, as well as conducting multi-layered checks on the ATLA from both inside and outside through audits by the Inspector General's Office of Legal Compliance and deliberations at the Defence Procurement Council, the members of which are external academics. Further, it is also making efforts towards raising compliance awareness by enhancing its education division and providing thorough education on legal compliance to its personnel.

In the case of defence and security procurement, the supplier's records of costs are inspected in relation to the production cost of procured defence and security articles, in accordance with the contractual terms, etc (eg, a special clause regarding securement of reliability of documents and implementation of system inspection or a special clause on securement of reliability of documents related to contracts concerning import goods, etc, and implementation of import procurement inspections) and whenever needed, cost audits are conducted to confirm that the price of each item's cost and consumption quantity is appropriate.

**IP rights**

17 Who gets the ownership rights to intellectual property created during performance of the contract? What licences are typically given and how?

Under the special terms published by the Ministry of Defence, the Ministry requires all rights to any copyright-protected work created during the performance of a contract to be transferred to the Ministry and a 'certificate of transfer of copyright' and a 'certificate of non-exercise of author's moral rights' to be submitted with the work product.

**Economic zones**

18 Are there economic zones or other special programmes in this jurisdiction commonly utilised by foreign defence and security contractors for financial or other procurement related benefits?

No.

**Forming legal entities**

19 | Describe the process for forming legal entities, including joint ventures, in this jurisdiction.

**Advance preparations**

Determine basic matters (eg, organisational form, stated capital, business descriptions and succession of assets) and check whether there is another company of the same trade name at the same location of the proposed head office with the legal affairs bureau.

**Prepare of articles of incorporation**

Determine the matters that must be stated in the original articles of incorporation (eg, the purposes, the trade name, the location of the head office, the minimum amount of contributed assets, the name or organisational name, and the address of the incorporator) and other matters, and have the articles of incorporation notarised by a notary public.

**Contribution**

The incorporator pays the money to be contributed in full, or tenders property, other than monies, with respect to the shares issued at incorporation without delay after subscribing for the shares that were issued at incorporation.

**Appointment of officers at incorporation**

The incorporator appoints directors at incorporation without delay after the completion of capital contribution. The company auditors are appointed; if required. The appointment of officers at incorporation is determined by a majority vote of the incorporators.

**Examination by directors at incorporation**

At incorporation, the directors at incorporation examine whether the capital contribution has been completed and whether any incorporation procedures are in breach of any laws, regulations or the articles of incorporation.

**Appointment of directors at incorporation**

If the company has a board of directors, a representative director at incorporation is appointed (decided by a majority vote of the directors at incorporation).

**Registration of incorporation**

The incorporation must be registered with the relevant government agencies (ie, the tax office, the prefectural tax office, the municipal government (regarding taxes or national pensions), the labour standards office (regarding employment insurance and workers' accident compensation insurance) and the pension office (regarding health insurance and employee pensions)) within two weeks from the latter of the date of termination of examination by the directors at incorporation or the date designated by the incorporator.

**Access to government records**

20 | Are there statutes or regulations enabling access to copies of government records? How does it work? Can one obtain versions of previous contracts?

In accordance with the Act on Access to Information Held by the Administration, any person may request that the head of an administrative organ disclose administrative documents. This request must be complied with, except in the following cases.

**Information concerning an individual**

Where it is possible to identify a specific individual from a name, date of birth or other description contained in the information (including cases where it is possible to identify a specific individual through comparing the requested information with other information) and when it is not possible to identify a specific individual, but disclosure of the information is likely to harm the rights and interests of an individual.

However, the following information is excluded from these prohibitions:

- information concerning a business operated by the individual;
- information that is public, or that is scheduled to be made public, pursuant to laws, regulations or custom;
- information that must be disclosed to protect a person's life, health, livelihood or property; and
- information that, in whole or in part, pertains to the substance of an individual's duties, or his or her performance of these duties, when the said individual is:
- a public officer;
- an officer or an employee of an incorporated administrative agency;
- a local public officer; or
- an officer or an employee of a local incorporated administrative agency.

In addition, the following exclusions apply to information concerning a juridical person or other such entities (excluding the state, incorporated administrative agencies, local public entities and local incorporated administrative agencies (juridical persons)), except where disclosure is required to protect a person's life, health, livelihood or property:

- information concerning the business of an individual operating the said business, except for information:
  - that is likely to harm the rights, competitive position or other legitimate interests of the juridical person or the individual if disclosed;
  - that is customarily not disclosed by a juridical person or an individual but was voluntarily provided in response to a request by an administrative organ on the condition of non-disclosure, or for which it is found reasonable that such a condition be set due to the information's nature or circumstances of the disclosure;
  - for which there are reasonable grounds for a head of an administrative organ to find that disclosure will likely:
    - harm national security;
    - harm a relationship of mutual trust with another country or an international organisation;
    - create a disadvantage in negotiations with another country or an international organisation; or
    - impede:
      - the prevention, suppression or investigation of crimes;
      - the maintenance of prosecutions;
      - the implementation of punishments; or
      - other matters concerning maintenance of public policy; or
- that concerns internal deliberations, examinations or consultations conducted by or between state organs, incorporated administrative agencies, local public entities or local incorporated administrative agencies, where disclosure is likely to:
  - cause unjust harm to the open exchange of opinions or the neutrality of decision-making;
  - cause unjust confusion among citizens; or
  - bring unjust advantages or disadvantages to specific individuals; and
- information concerning the affairs or business of a state organ, an incorporated administrative agency, a local public entity or a local incorporated administrative agency, where disclosure is likely to hinder the proper execution of the said affairs or business or presents the following risks:

- making it difficult to accurately understand the facts concerning affairs pertaining to audits, inspections, supervision, examinations, imposition or the collection of taxes; facilitate wrongful acts regarding such affairs, or make it difficult to discover such wrongful acts;
- unjustly damaging a property benefit of the state, an incorporated administrative agency, a local public entity or a local incorporated administrative agency concerning affairs pertaining to contracts, negotiations or administrative objections and litigations;
- unjustly hindering the fair and efficient execution of affairs pertaining to research and study;
- hindering the maintenance of impartial and smooth personnel practices in the affairs pertaining to personnel management; and
- causing damage to legitimate interests arising from corporate management regarding the business of an enterprise managed by a state or a local public entity, an incorporated administrative agency or a local incorporated administrative agency.

**Supply chain management**

21 What are the rules regarding eligible suppliers and supply chain management and anti-counterfeit parts for defence and security procurements?

Any person who falls under the descriptions of articles 70 and 71 of the Cabinet Order on Budgets, the Settlement of Accounts, and Accounting (article 70 of the foregoing Cabinet Order) may not participate in competitive bidding, other than for construction work.

In addition, the contracting officer may disallow a person falling under the following items to participate in competitive bidding if the sale, lease, contracting or another form of contract is put out to tender pursuant to article 29–3, paragraph 1 of the Public Accounting Act (an open tender), unless there are special grounds for allowing them:

1 a person who is incapable of concluding the relevant contract;
2 a person who received an order of commencement of bankruptcy proceedings and has not had their rights restored; or
3 a person who falls under any of the items of article 32, paragraph 1 of the Act on Prevention of Unjust Acts by Organised Crime Group Members (Act No. 77 of 1991) (article 17 of the foregoing Cabinet Order).

A contract officer may also prevent a person who falls under the following categories (and their proxies, manages and employers) from participating in open tenders for a period of no more than three years:

1 a person who intentionally carried out construction, manufacturing or any other service in a careless manner or acted fraudulently with regard to the quality or volume of an object in the course of performing a contract;
2 a person who obstructed the fair implementation of a tender, hindered a fair price from being reached or colluded with others to obtain an unlawful profit;
3 a person who obstructed a successful bidder from entering into a contract or obstructed a party to a contract from performing the contract;
4 a person obstructed an official from performing the official's duties regarding a supervision or inspection;
5 a person who has not performed a contract without a justifiable reason;
6 a person who intentionally, and based on false facts, claimed the price of fulfilling a contract exceeded the price that was fixed when signing the contract;
7 a person facing a denomination under the 'Outline of denomination, etc concerning procurement of defence and security articles, etc and services'; and
8 a person who employs a proxy, manager or any other employee who is not eligible to participate in an open tender pursuant to items (1) to (4) above and (1) to (7) in the performance of a contract.

There are no specific rules regarding supply chain management and anti-counterfeit parts relating to defence and security procurements.

## INTERNATIONAL TRADE RULES

**Export controls**

22 What export controls limit international trade in defence and security articles? Who administers them?

With regard to export controls that limit international trade in defence and security articles, the Foreign Exchange and Foreign Trade Act (FEFT) stipulates certain provisions relating to security trade controls, which are enforced by the Ministry of Economy, Trade and Industry.

**Domestic preferences**

23 What domestic preferences are applied to defence and security procurements? Can a foreign contractor bid on a procurement directly?

There is no mechanism for applying domestic preferences to defence and security procurements. For the acquisition of defence and security articles, a number of acquisition methods are currently adopted, including domestic development, international co-development or production, domestic production under licence, utilisation of civilian goods, importing etc. The appropriate method is selected depending on the characteristics of the particular defence and security articles in question. The Analysis and Assessment of the Acquisition Program, the new Acquisition Strategy Plan and Acquisition Plan published by Acquisition, Technology and Logistics Agency (ATLA) on 31 August 2017, adopts a policy of domestic development, production and maintenance for certain items.

The Guidance for Bid and Contract (ATLA Public Notice No. 1 of 1 October 2015) contains provisions pursuant to which foreign business operators may apply to undergo eligibility screening to participate in tenders, which indicates that it is possible for foreign companies to directly participate in procurement tender. However, a Japanese trading company will usually carry out procurement on behalf of a foreign company.

**Favourable treatment**

24 Are certain treaty partners treated more favourably?

There are no treaty partners that are treated more favourably.

**Sanctions**

25 Are there any boycotts, embargoes or other trade sanctions between this jurisdiction and others?

**Exports**

In Japan, export controls are conducted under the Foreign Exchange Act, the Export Control Order, the Foreign Exchange Order, and the Ministerial Ordinance on Goods.

There are export controls that require the permission or approval of the Minister of Economy, Trade and Industry.

Defence and security articles that require permission to be exported include:

*[Weapons], articles related to weapons of mass destruction, articles related to conventional weapons and articles that are likely to be used for development, etc of weapons of mass destruction or conventional weapons.*

'Articles related to weapons of mass destruction' refers to articles related to nuclear, chemical and biological weapons and missiles.

'Articles related to conventional weapon' refers to state-of-the-art materials processing, electronics, computers, communication devices, sensors or lasers, navigation equipment, marine-related equipment and propulsion devices.

Exports subject to approval includes all exports of articles bound for North Korea.

**Imports**

Primary import controls applicable to defence and security articles include restrictions on specified regions under which approval is required to import from specified countries of origin or places of shipment. Pursuant to this restriction, approval of the Minister of the Economy, Trade and Industry is required to import weapons originated or shipped from Eritrea, and Type I Designated Substances defined in the Act on the Prohibition of Chemical Weapons and the Regulations of Specific Chemicals (Chemical Weapons Control Act) originating or shipping from specified countries or regions.

Further, in terms of current economic sanctions, the approval of the Minister of the Economy, Trade and Industry is required to import any articles originating or shipping from North Korea, therefore weapons originating or shipping from Liberia are effectively prohibited.

Articles that require approval regardless of the country of origin or the place of shipment include:

1 explosives;
2 military aircraft and engines for military aircraft;
3 tanks, other armed vehicles, and components thereof;
4 warships;
5 military armaments, guns and other firearms;
6 other weapons, bombs, swords, spears and similar weapons;
7 components of the items listed in (1) to (7); and
8 substances specified under the Chemical Weapons Control Act.

**2017 Amendments to the Foreign Exchange and Foreign Trade Act**

Amendments to the FEFT were promulgated on 24 May 2017 and came into effect on 1 October 2017. These strengthened penalties of regulations concerning the importing or exporting and trade of technologies, and administrative sanctions concerning import and export regulations.

**2019 Amendments to the Foreign Exchange and Foreign Trade Act**

The notice on inward direct investment was amended with effect from 1 August 2019 in order to effectively prevent the outflow of security-critical technologies and damage to the foundation of Japan's national defence industry and technologies, and similar situations that could have serious impacts on Japan's national security. The amendments also introduced a requirement to give advance notification of inward direct investment in businesses related to cybersecurity.

**Trade offsets**

26 | Are defence trade offsets part of this country's defence and security procurement regime? How are they administered?

There are no trade offsets at the moment, although the Ministry of Defence is considering their introduction.

## ETHICS AND ANTI-CORRUPTION

**Private sector appointments**

27 | When and how may former government employees take up appointments in the private sector and vice versa?

There are no restrictions preventing former public officers from taking up appointments in the private sector, or vice versa.

However, the following actions and appointments are generally prohibited:

- A public officer, while currently in office, communicating with an 'interested enterprise' (including enterprises defined by law) regarding the officer assuming a position in the enterprise or a subsidiary corporation, while he or she is offering a contract for defence and security articles to the enterprise or is executing or is obviously intending to offer to execute such a contract with the enterprise. (Contacts of less than ¥20 million are excluded from this prohibition.)
- A public officer engaging in communications with an enterprise (not limited to interested enterprises) with the aim of having another public officer or former public officer assume a position in the enterprise or a subsidiary corporation.
- A former public officer, in the course of his or her duties as an employee of an enterprise, demanding or requesting that the division of the government agency he or she held a position in performs, or does not perform, certain acts in relation to a contract with the enterprise or in relation to administrative measures being made against the enterprise that employs them. In these cases, what actions are prohibited depend on the employee's position during his or her time in public office. There is no time limit on this prohibition regarding contracts and administrative measures employee was involved in as a public officer; it is two years with respect to other cases.

If a former public officer obtains a position at an enterprise immediately after leaving office, they will be suspected of breaching the restrictions on communications with enterprises. In practice, individuals wait at least three months before assuming a position in the private sector after leaving public office. These restrictions also apply to public officers with fixed terms of office and those hired under a public-private personnel exchange.

Further, to ensure transparency, public officers or former public officers must file notices with certain prescribed persons, including the Minister of Defence, if, while in office, they promise to assume a position in an enterprise after leaving office, or they assume a position in an enterprise within two years after retiring from a managerial position in public office (except where a notice in relation to promising to assume a position after leaving office was filed). Certain information contained in these notices filed is made public.

**Addressing corruption**

28 | How is domestic and foreign corruption addressed and what requirements are placed on contractors?

There are no special restrictions related to bribery that specifically target government procurement. Such matters are generally covered by the offence of bribery under the Criminal Code. The main crimes under the Criminal Code regarding bribery that are applicable to enterprises are any bribe:

- made to a public officer in relation to the performance of his or her official duties;
- made upon request to a potential public officer in relation to the performance of official duties for which he or she is expected to be responsible;

- made upon request from a public officer in relation to the performance of his or her official duties to a person other than the said public officer (the person receiving the bribe is not required to be a public officer);
- made to a former public officer, in relation to the former officer conducting an unlawful act, or refraining from conducting a reasonable act, upon request while they were in office; or
- made to a public officer as a reward for conducting an unlawful act or refraining from conducting a reasonable act in the course of his or her duties upon request, or arranging for another public officer to do so.

The specifications of procured of defence and security articles are generally precise so there is no market price for them. In many cases, contracts are executed upon calculating an estimated price using cost accounting with a view to preventing overcharging by contractors. Contractual special clauses are generally required for cost accounting and management for the purpose of preventing overcharging by contractors, and cost audits are conducted. In such audits, the supplier's records of costs are inspected in relation to the production cost of procured defence and security articles, in accordance with the contractual terms, etc (eg, a special clause regarding securement of reliability of documents and implementation of system inspection or a special clause on securement of reliability of documents related to contracts concerning import goods, etc, and implementation of import procurement inspections) and whenever needed, cost audits are conducted to confirm that the price of each item's cost and consumption quantity is appropriate.

Other than the above, cartels (bid rigging) and similar acts are prohibited under the Anti-Monopoly Act, and obstructions of auctions are prohibited under the Criminal Code, the Unfair Competition Prevention Act and the Act on Elimination of Involvement in Bid Rigging. There are also punishments for failure to act, and criminal penalties or administrative monetary penalties apply in the case of violations.

Any enterprise that violates any of the restrictions or requirements stated above, engages in acts unfairly or in bad faith, makes false statements in tendering documents, performs a contract negligently without due care, or breaches a contract, will be denominated from procurements for defence and security articles for one month to three years depending on the degree of seriousness of the violation. In cases where an enterprise refuses to comply with system survey, which is a system survey prescribed in Article 1, Paragraph 2, Item 3 of the Implementation Guidelines for Measures to Ensure the Reliability of Data Submitted by Contract Recipients, it will remain denominated until it resumes the research. In addition, enterprises that have capital ties or personal relationships which means a case where an officer of one company serves concurrently as an officer of another company with a denominated enterprise may be barred from participating in open or selective tendering procedures for agreements for similar types of defence and security articles.

Public officers are subject to the National Public Service Ethics Code to ensure public trust in the fairness with which public officers execute their duties. Pursuant to this Code, public officers are prohibited from engaging in the following acts:

1 receiving a gift of money, goods or real estate from an interested party;
2 borrowing money from an interested party;
3 receiving services free of charge from an interested party;
4 receiving an assignment of private equity from an interested party;
5 receiving entertainment and paid dining from an interested party;
   - a public officer may dine with an interested party if the public officer pays his or her own costs, but a public officer needs to file a notice needs to be filed with the Ethics Supervisory Officer if each party's payments exceed ¥10,000 for one party's cost, except in certain specific cases (eg, buffet parties);
6 indulging other forms of entertainment with an interested party (eg, going on a pleasure trip, playing golf or playing mahjong), whether or not the officer and the interested party (or parties) share the costs; and
7 demanding an interested party engage in the activities listed in (1) to (6) with a third party, (however, the prohibition does not apply if an interested party makes an offer to engage in such activities with a third party).

Any public officer violating items (1) to (7) can be subject to disciplinary action. There are no sanctions applicable to the interested party.

As defined in the Code, 'interested parties' includes enterprises with which a public officer has executed, offered to execute, or obviously intends to offer to execute a contract for defence and security articles in relation to which the public officer is involved in administering. Any interested party the public officer served within the previous three years are regarded as interested parties for at least three years after the transfer of this public officer. In addition, if an interested party of a public officer contacts a second public officer in order to have the official exercise his or her influence, based on his or her government position relative to the first public officer, the interested party of the first public officer shall also be deemed to be an interested party of the second public officer.

### Lobbyists

29 What are the registration requirements for lobbyists or commercial agents?

There are none.

### Limitations on agents

30 Are there limitations on the use of agents or representatives that earn a commission on the transaction?

No.

## AVIATION

### Conversion of aircraft

31 How are aircraft converted from military to civil use, and vice versa?

In August 2010, the Ministry of Defence finalised guidelines for designing a system to convert military aircraft to civil use, and put a system in place for companies wishing to conduct such conversions in 2011. Technical documents for the conversion of the engines used on ShinMaywa US–2 rescue flying boats and Kawasaki P–1 fixed-wing patrol aircraft have been disclosed and published upon requests from commercial enterprises. In December 2016, the Acquisition, Technology and Logistics Agency (ATLA) announced it had entered into an agreement with IHI Corporation on the conversion to civil use of IHI's F7–10 engines used on P–1 aircraft in order to sell F7–10 engines to the Japan Aerospace Exploration Agency.

The Ministry of Defence rarely procures aircraft configured for civilian use for conversion to military use, preferring to purchase equipment that has already been converted for military use.

**Drones**

32 What restrictions are there on manufacture and trade of unmanned aircraft systems or drones?

Under the Aircraft Manufacturing Industry Act, aircraft and rotorcraft with a structure that people cannot board and a gross weight of 150 kilogrammes or more fall under the definition of 'aircraft' and are subject to restrictions on methods of manufacturing and repair. The primary such restrictions are:

- the manufacturing or repair (including modification) of aircraft is subject to a licensing system (ie, permission of the Minister of Economy, Trade and Industry is required for each plant);
- manufacturing or repair must be conducted by permitted business operators in a manner approved by the Minister of Economy, Trade and Industry, which must also be confirmed by an aircraft inspector; and
- permitted business operators may, as a rule, only deliver a manufactured or repaired aircraft to others along with a manufacturing confirmation document prepared by an aircraft inspector.

On 10 December 2015, the Ministry of Economy, Trade and Industry announced it would request manufacturers, importers and sellers of unmanned aircraft to make voluntary efforts to identify the owners of unmanned aircraft.

## MISCELLANEOUS

**Employment law**

33 Which domestic labour and employment rules apply to foreign defence contractors?

Labour and employment rules are domestic laws and as such do not apply unless a contractor has an office and employs employees in Japan. If an enterprise has an office and employees in Japan, it must pay Japanese labour insurance and employee pension insurance. Having the proper labour insurance and employee pension insurance policies in place, and not being slack in payment of premiums, are generally requirements to qualify for participating in open and selective tendering procedures.

**Defence contract rules**

34 Are there any specific rules that contractors, foreign or domestic, are bound by in defence contracts?

No.

35 Do contractors avail themselves of these rules when they perform work exclusively outside of the jurisdiction?

Not applicable.

**Personal information**

36 Must directors, officers or employees of the contractor provide personal information or certify that they fulfil any particular requirements to contract with a government entity?

One trigger for disqualification from bidding is being a 'juridical person or other organisation in which a designated organised crime group member serves as an officer thereof', an 'organised crime group member' being a person falling under any of the items of article 32, paragraph 1 of the Act on Prevention of Unjust Acts by Organised Crime Group Members (Act No. 77 of 1991) (article 17 of the foregoing Cabinet Order). As a result, enterprise bidders are required to submit a pledge at the time of bidding, declaring that none of their 'officers, etc' belongs to an organised crime group.

**Licensing requirements**

37 What registration or licensing requirements exist to operate in the defence and security sector in the jurisdiction?

There are no registrations or licensing requirements.

**Environmental legislation**

38 What environmental statutes or regulations must contractors comply with?

**Green Purchasing Act**

The Green Purchasing Act came into force in 2001.

Following this act, the national government must endeavour to select 'eco-friendly goods' with low environmental impact during procurement processes, in particular:

- goods featuring recyclable resources;
- products with low environmental impact, due to the ability to reuse or recycle the product, or being made from raw materials or parts with low environmental impacts; and
- services that have low environmental impacts.

In response to this, the Ministry of the Environment established a basic policy applicable to all governmental agencies in respect of a wide variety of procurement items. The Ministry of Defence also set its own corresponding procurement goals in 2016. However, the procurement goals of the Ministry of Defence primarily target stationery, office supplies, air conditioners, lighting and general official vehicles. In regard to goods and services that form key defence and security items, the targets are limited to the construction of public facilities, tires for passenger cars, two-stroke engine oil and disaster supplies.

**Green Contract Act**

The Green Contract Act came into force in 2007.

This act went further than the Green Purchasing Act, requiring the national government to endeavour to promote procurement contracts with serious consideration for the reduction of greenhouse gas emissions. In its response, the Cabinet established a basic policy that covers six types of contracts:

- the purchase of electricity;
- the purchase and lease of automobiles;
- the procurement of vessels;
- the design of governmental building renovations (such plans must guarantee that reductions in the cost of powering the renovated building will exceed the cost of the renovation);
- other building designs; and
- industry waste disposal.

In response to the above, specific fuel economy and other environmental performance requirements may be set out in procurement specifications for many defence articles, among other requirements.

39 Must companies meet environmental targets? What are these initiatives and what agency determines compliance?

Requirements for specific fuel consumption and other environmental performance indicators may be provided in the specifications for bidding on the six types of contracts covered by the Green Contract Act. These contracts are:

- the purchase of electricity;
- the purchase and lease of automobiles;

- the procurement of vessels;
- the design of governmental building renovations;
- other building designs; and
- industry waste disposal.

In such cases, enterprises must submit bids that meet such requirements. An evaluation will be conducted by the Acquisition, Technology and Logistics Agency (ATLA), which is the agency managing procurement.

40 | Do 'green' solutions have an advantage in procurements?

No. However, bids may be required to meet specific fuel consumption and other environmental performance indicators to be accepted.

## UPDATE AND TRENDS

### Key developments of the past year

41 | What were the key cases, decisions, judgments and policy and legislative developments of the past year?

There are no updates at this time.

### Coronavirus

42 | What emergency legislation, relief programmes and other initiatives specific to your practice area has your state implemented to address the pandemic? Have any existing government programmes, laws or regulations been amended to address these concerns? What best practices are advisable for clients?

The Measures against Pandemic Influenza etc Act has been revised to address the coronavirus pandemic in Japan.

No legislation or amendments have been made due to the pandemic that would have a significant impact on the field of defence and security. However, the ministerial ordinance of the Foreign Exchange and Foreign Trade Act (FEFT) was revised to allow the deferment of reporting obligations under the FEFT. But such obligations must be fulfilled without delay when it becomes possible to do so.

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# Mexico

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## LEGAL FRAMEWORK

### Relevant legislation

1 | What statutes or regulations govern procurement of defence and security articles?

Article 134 of the Mexican Constitution provides the general principles for public procurement in Mexico at the federal and state levels. The Law of Acquisitions, Leases and Services of the Public Sector (the Public Procurement Law), together with its ruling (the Regulation of the Public Procurement Law) comprise the main legal framework under which all federal public procurement for defence and security matters are regulated, and detail the general constitutional principles.

At the local level, procurement for security goods and equipment is regulated in state and municipality's public procurement legal framework, all of which contain somewhat similar provisions to those contained in the Public Procurement Law and its ruling.

### Identification

2 | How are defence and security procurements identified as such and are they treated differently from civil procurements?

Defence and security procurements are identified as cases where the exceptional procedure under article 41, subsection IV of the Public Procurement Law is to be used. Owing to their special status, they are treated differently from standard civil procurements in the understanding that all defence and security procurements are exempt from being mandatorily awarded by means of a prior public procurement public bidding process. This is the general principle followed by all public agencies before engaging in any commercial relationship with third parties to ensure the best contractual conditions available in the market for Mexico.

### Conduct

3 | How are defence and security procurements typically conducted?

The Public Procurement Law provides that, prior to the execution of any public procurement agreement (including those related to defence and security), market research must be conducted to verify the existence and availability of the required goods and assets, whether the respective manufacturer or distributor is national or foreign, and the estimated price.

After the market research has been conducted, the respective defence or security government body that requires the acquisition of defence- or security-related assets must substantiate its reasons in connection to why such procedure should not be executed via the traditional public bidding process but by a direct award process instead.

At the local level, this procedure might differ from those contemplated in the local applicable law.

### Proposed changes

4 | Are there significant proposals pending to change the defence and security procurement process?

Currently, there are no pending proposals or amendments in the Federal Congress to the Public Procurement Law and its ruling that could amend or modify the defence and security procurement process, nor its legal framework.

### Information technology

5 | Are there different or additional procurement rules for information technology versus non-IT goods and services?

No. Nevertheless, according to the Public Procurement Law, the defence or security government body interested in acquiring or leasing any goods or services that require or have advanced technical specialities or technological invocations, must use the 'points and percentages' or 'price-performance ratio' evaluation methods.

The points and percentages evaluation method is used to grade the proposals of all bidders in a public bidding process in which certain points are attributed to bidders who have disabilities or companies that employ people with disabilities (at least 5 per cent of their total employees must have disabilities), small and medium companies that produce innovative technological goods, and companies that have put in place and practice gender equality policies.

The price-performance ratio evaluation method is used to assure the best price, in accordance to the benefit to be obtained by a certain acquisition or lease to be executed by the federal defence government bodies.

### Relevant treaties

6 | Are most defence and security procurements conducted in accordance with the GPA or other treaty-based procurement rules, or does this jurisdiction commonly use the national security exemption to procure them?

All defence and security procurements are conducted in accordance with the national security rules and regulations (including the exemption to procure them).

## DISPUTES AND RISK ALLOCATION

### Dispute resolution

7 | How are disputes between the government and defence contractor resolved?

According to the Sixth Title of the Public Procurement Law (the Dispute Resolutions), there are different dispute resolution procedures that may be applied to solve disputes between the government and contractors.

**Disconformity procedure**

This procedure is purely administrative. It is filed before the Ministry of Public Affairs, or directly through the Compranet website when the dispute relies on procedural grounds regarding the different instances of a public bidding. CompraNet is the government's electronic public information system for public procurement. Its use is mandatory for the subjects indicated in article 1 of the Public Procurement Law.

**Conciliatory procedure**

This procedure is filed before the Ministry of Public Affairs whenever a party of a public procurement agreement considers that a counterparty has breached its obligations. The Ministry of Public Affairs conducts a conciliatory hearing to attempt to negotiate a solution between the parties. The agreed solution is written in a binding special agreement.

**Arbitration and other alternative dispute resolution methods**

The parties to a certain public procurement agreement can agree to an arbitration proceeding or another dispute resolution procedure, such as mediation and conciliation, with regard to the interpretation or execution of the agreements. However, parties are forbidden from agreeing to an alternative dispute resolution method with regard to disputes in connection to the early termination of the agreements, or termination by a breach.

**Administrative courts**

If no alternative dispute resolution method has been agreed to by the parties, or if such methods are forbidden by law, the disputes will be solved by the competent federal courts of Mexico.

These dispute resolution procedures are applicable only to federal public procurement processes, and such processes may differ from those contained in the local public procurement laws and regulations. We strongly recommend reviewing the specific local applicable law, since each of the 32 Mexican states has its own specific applicable laws.

8 To what extent is alternative dispute resolution used to resolve conflicts? What is typical for this jurisdiction?

Alternative dispute resolution procedures are commonly used by contractors and government agencies to solve disputes. A clause stating this is usually included in the public procurement contracts.

**Indemnification**

9 What limits exist on the government's ability to indemnify the contractor in this jurisdiction and must the contractor indemnify the government in a defence procurement?

**Governmental indemnification**

All payments in favour of the contractor to be paid by the corresponding government body must not exceed 20 calendar days after delivery of the corresponding invoice, the delivery of the goods or assets, or the rendering of the corresponding services. In the case of a breach to the payment obligations of the corresponding government body, the government body must pay all financial expenses (limited to the interest rate established in the Federal Income Law, for extension regarding unpaid taxes). These financial expenses will be calculated over all unpaid amounts and counted in calendar days until the contractor is fully paid.

**Contractor indemnification**

As stated in the Public Procurement Law, all contractors must guarantee the advanced payments (for their total amount) and the full compliance of the agreement. Usually, this guarantee is 10 per cent of the total amount of the agreement, but it may be waived in public procurements related to defence and security procurements. Also, contractors are obliged to guarantee all latent defects of the goods delivered or services rendered.

Parties are allowed to agree on a contractual penalty if the contractor delays delivering the goods, assets or services under the corresponding public procurement agreement. Such a penalty must not exceed the total amount of the agreement compliance guarantee (required to be granted by the contractor in favour of corresponding government body) and must be determined taking in consideration the goods and assets or services that were not timely delivered or executed.

The above-mentioned indemnification provisions are only applicable to federal procurement processes. Indemnification provisions may vary at the local level and, therefore, we strongly suggest reviewing the specific local applicable law, since each of the 32 Mexican states have specific applicable laws.

**Limits on liability**

10 Can the government agree to limit the contractor's liability under the contract? Are there limits to the contractor's potential recovery against the government for breach?

All contractors must guarantee the full compliance of their agreement. The amount of this guarantee is determined by the corresponding government body in the bidding documents, executed in the case of non-compliance of the agreement, and will constitute the limit of the contractor's liability under the corresponding contract.

In the case of a breach to the payment obligations of the corresponding government body, the government body pays all financial expenses (limited to the interest rate established in the Federal Income Law, for extension regarding unpaid taxes) to the contractor. These financial expenses will be calculated over all unpaid amounts and counted in calendar days until the contractor is fully paid.

The above-mentioned provisions are applicable only to federal procurement processes. Liability limitation provisions may vary at the local level and, therefore, we strongly suggest reviewing the specific local applicable law as each of the 32 Mexican federal states has specific applicable law.

**Risk of non-payment**

11 Is there risk of non-payment when the government enters into a contract but does not ensure there are adequate funds to meet the contractual obligations?

Yes. Although all federal government expenses and contracting procedures are originally approved and stated in the Federal Expenditure Budget, there is still a minor risk of a payment default. In case of a default, the corresponding government body, at the contractor's request, must pay all financial expenses according to the rate established by the Federal Income Law. Such expenses shall be calculated on the unpaid amounts and shall be computed by calendar days from the date the agreed term expired, until the date on which the contractor is fully paid.

**Parent guarantee**

12 Under what circumstances must a contractor provide a parent guarantee?

The Public Procurement Law provides that all contractors guarantee:

- all advanced payments (for their total amount);
- full compliance with the agreement (usually, the corresponding guarantee is for the 10 per cent of the total amount of the agreement, but this may be waived in public procurements related to defence and security); and
- contractors are also obliged to guarantee all latent defects of the goods delivered or services rendered.

Government officials of the corresponding government body will set the conditions and amounts on which the guarantees will be granted, taking into consideration the contractor's compliance history.

The above-mentioned guarantees will be granted either in favour of the Treasury or in favour of the contracting government body, depending on which government body is a party to the main public procurement agreement.

## DEFENCE PROCUREMENT LAW FUNDAMENTALS

### Mandatory procurement clauses

13 Are there mandatory procurement clauses that must be included in a defence procurement contract or that will be read into the contract regardless of their actual inclusion?

Yes, all public procurement agreements must contain the following:

- the name or corporate name of the government contracting body;
- the nature of the procedure by which the agreement was awarded to the contractor;
- information regarding the authorisation of the budget granted to the corresponding government body to execute the agreement;
- information that proves the legal existence of the contractor;
- a description of the goods, assets or lease, subject matter of the public procurement agreement;
- a consideration price to be paid for the goods, assets or services rendered by the contractor;
- the terms of payment, including:
  - a statement that the price is fixed; or
  - a statement that the price is subject to adjustments, and the formula or condition(s) in which such adjustments will be made and calculated, expressly determining the indicator(s) or official means that will be used in such a formula; and
  - a percentage, number and dates or period of the exhibitions and amortisation of prepayments that are granted;
- the date or term, place and conditions of delivery;
- guarantees to be granted by the contractor;
- cases in which extensions may be granted;
- grounds for termination of the agreement;
- latent defects provisions;
- the general terms and conditions of the applicable contractual penalties;
- liabilities regarding the breach of intellectual property; and
- dispute resolution procedures.

If no dispute resolution procedure has been agreed and included in the corresponding public procurement agreement, all disputes will be resolved in the Mexican federal courts.

### Cost allocation

14 How are costs allocated between the contractor and government within a contract?

All costs arising from or regarding the public bidding process and in connection with the execution of the public procurement agreement are to be bear by the contractor.

### Disclosures

15 What disclosures must the contractor make regarding its cost and pricing?

The contractor must disclose the price per unit and the total price of the goods or services to be rendered. Also, if applicable, the contractor must disclose the way in which the final price is determined.

The contractor should also indicate if the price is fixed or variable. If it is variable, the contractor should indicate the formula by which an increase in the price will be calculated.

### Audits

16 How are audits of defence and security procurements conducted in this jurisdiction?

Pursuant to the Public Procurement Law, the Ministry of Public Affairs may verify, at any moment, that all public procurement agreements have been duly executed in accordance with the applicable laws. At the local level, the applicable laws may allow certain local governmental bodies to conduct such audits.

Moreover, the Ministry of Public Affairs may conduct visits and inspections of the government bodies that requested and executed the corresponding public procurement agreements, and may also request all related data and information from the involved officials and contractors.

The Ministry of Public affairs may also conduct product quality verifications.

Defence and security procurements are not exempted from such audits. However, defence and security procurements granted through a direct award, and not through a public bidding process, are required to be reported to the Ministry of Public Affairs by the corresponding government body, which is also required to justify why the procurement was not granted according to the traditional public bidding process.

### IP rights

17 Who gets the ownership rights to intellectual property created during performance of the contract? What licences are typically given and how?

Unless there is a specific prohibition or impediment, the ownership over all intellectual property created during performance of the contract will be granted to the contracting government body.

### Economic zones

18 Are there economic zones or other special programmes in this jurisdiction commonly utilised by foreign defence and security contractors for financial or other procurement related benefits?

During the previous federal administration (the presidency of Mr Enrique Peña Nieto, from the 1 December 2012 to 30 November 2018), Mexico implemented a special economic zones programme. These zones are designated geographical areas in which economic, tax and other administrative advantages would be granted to the private sector operating in them. They were designed as an instrument to boost economic development in underdeveloped regions. Each special economic zone has a niche, therefore only certain industrial or commercial activities can be developed in such regions, and only those activities will be subject to the advantages contemplated in the Federal Law of Special Economic Zones. If a special economic zone is declared in which defence and security-related goods or assets are to be manufactured or produced, then the manufacturer or producer installed in such zone may be subject to certain economic, tax and other administrative advantages.

Notwithstanding the aforementioned, the new Federal Administration recently announced the cancellation of special economic zones that were created during the previous administration. However, the Federal Law of Special Economic Zones is still in full force and effect, and, although it is unlikely, the creation of new special economic zones in the future may not yet be discarded.

**Forming legal entities**

19 Describe the process for forming legal entities, including joint ventures, in this jurisdiction.

Legal entities, such as corporations and companies, are incorporated pursuant to the provisions contained in the General Law of Business Corporations. Certain steps must be taken to incorporate a legal entity in Mexico, which are generally:

- obtaining the approval of the Ministry of Economy for the use of the desired corporate name;
- drafting the articles of incorporation (which must contain all information stated in the Business Corporation Law);
- formalising the articles of incorporation before a Mexican notary public;
- registering the newly formed entity's articles of incorporation in the corresponding Public Registry of Commerce; and
- registering the new entity with the Mexican Internal Revenue Service.

Other important information that must be contained in the articles of incorporation includes the company's attorneys-in-fact and their corporate authority, the appointment of the board of directors and managers, etc.

This process usually takes no longer than two to three weeks and its costs are relatively low.

**Access to government records**

20 Are there statutes or regulations enabling access to copies of government records? How does it work? Can one obtain versions of previous contracts?

In terms of the Federal Law of Transparency and Access to Public Government Information, all public entities must provide general or specific information, including that regarding their annual procurement programme with respect to the ongoing fiscal year, via the CompraNet website (the official website regarding government procurements) each year no later than 31 January.

Nonetheless, certain contracts (and related documentation) may be exempt from disclosure, as such information may be sensitive and pose a risk to national security.

**Supply chain management**

21 What are the rules regarding eligible suppliers and supply chain management and anti-counterfeit parts for defence and security procurements?

As stated in the Public Procurement Law, persons will not be eligible to execute a contract if:

- they share a personal or business interest with their employer, such as that which may provide personal benefits or advantages;
- they are employed or have a position or commission with the public service or legal entities that involved, without prior authorisation by the Public Service Ministry;
- they are a supplier that the ministry or legal entity that executed the contract has previously cancelled or rescinded a contract with;
- they were made ineligible by a resolution of the Public Service Ministry in terms of the Public Procurement Law;
- the suppliers are delayed in the delivery of the goods and supplies with respect to prior executed contracts;
- they have been declared in a bankruptcy process or any other similar process;
- they are suppliers or legal entities which file certain propositions in the same field of a good or service in a contracting procedure that may be related;
- they are suppliers or legal entities who pretend to participate in a contracting procedure and that are part of a holding corporation that has been or is currently involved in another contract;
- they are suppliers or legal entities that execute contracts with respect to matters regulated by the Public Procurement Law, without express faculties to use intellectual property rights;
- they use unduly provided privileged information;
- they contract advice, consulting services or any other support in terms of government contracts; or
- they are bidders who did not formalise the contract for unjustified causes.

With respect to supply-chain management, there are no general rules or regulations that establish how to proceed; a supply-chain agreement will be valid even if it is executed by and between the government and any other part. However, regarding anti-counterfeit parts, any contractor that commits fraud or acts in bad faith in any of the government procurement contracts will be subject to the fines and penalties established in the Public Procurement Law.

## INTERNATIONAL TRADE RULES

**Export controls**

22 What export controls limit international trade in defence and security articles? Who administers them?

In principle, the export of goods from Mexico is regulated by the Mexican Customs Law, the Mexican General Import and Export Duties Law and any other applicable law (national or international) depending on the tariff code in which the defence and security article is covered.

In this regard, on 25 January 2012, Mexico joined the Wassenaar Arrangement on Export Controls for Conventional Arms and Dual-Use Goods and Technologies, becoming the 41st state participant in the agreement. The Wassenaar Arrangement was established to contribute to regional and international security and stability by promoting transparency and greater responsibility in transfers of conventional arms and dual-use goods and technologies, to preventing destabilising accumulations. The aim is also to prevent terrorists from acquiring these items.

At the national level, on 16 June 2011, Mexico published in the Mexican Official Gazette the:

> *Agreement in which the export of conventional weapons, their parts and components, dual-use goods, software and technologies that could be diverted for the manufacture and proliferation of conventional arms and weapons of mass destruction are subject to a prior permission from the Ministry of Economy.*

On the other hand, on 30 January 2007, the 'Agreement that establishes the classification and codification of goods whose importation or exportation is subject to Regulation by the Secretary of National Defence' was published in the Mexican Official Gazette.

In this regard, the defence and security articles will be regulated depending on their tariff codes, and may require permission from the Ministry of Economy and National Defence to be exported.

Present information does not include nuclear material or use of pesticides, fertilisers and toxic substances.

**Domestic preferences**

23 | What domestic preferences are applied to defence and security procurements? Can a foreign contractor bid on a procurement directly?

Since all defence and security procurements are exempt from the traditional bidding process and may be granted via a direct award instead, there are no applicable domestic preferences.

**Favourable treatment**

24 | Are certain treaty partners treated more favourably?

No.

**Sanctions**

25 | Are there any boycotts, embargoes or other trade sanctions between this jurisdiction and others?

As part of the United Nations, Mexico agreed to comply with the decisions of its Security Council and, through its national policies, ensure that transfers of arms, dual-use goods and technology do not contribute to the development or enhancement of military capabilities that undermine these goals, and are not diverted to support such capabilities.

In this regard, on 29 November 2012 Mexico published in its official gazette the 'Agreement establishing measures to restrict the export or import of various goods to the countries, entities and persons indicated', by which Mexico restricts the export, among others, of defence and security articles to the countries established in the Agreement.

**Trade offsets**

26 | Are defence trade offsets part of this country's defence and security procurement regime? How are they administered?

Not applicable.

## ETHICS AND ANTI-CORRUPTION

**Private sector appointments**

27 | When and how may former government employees take up appointments in the private sector and vice versa?

The Government Employees' Responsibilities Federal Law provides that former government employees are subject to restrictions associated with their office or ministry. Former government employees must allow a specific period before they join a private or public sector employment that has significant dealings with the government or has any other restriction with respect to their job.

**Addressing corruption**

28 | How is domestic and foreign corruption addressed and what requirements are placed on contractors?

Several different approaches and measures address domestic and foreign corruption in public procurement. In all public procurement agreements, of which the total amount is above 5 million days of minimum wage (around 441 million Mexican pesos), or that may have certain impacts in the programmes of the contracting government body, individuals who are known as 'social witnesses' must participate. These individuals are in charge of supervising the procurement process to prevent and detect potential corruption or irregularities in the procurement process.

Also, as a means to prevent corruption, certain public procurement bidding may be executed through electronic means in accordance with applicable law.

To be eligible, contractors must register with the Contractors Sole Registry, in which they will have to disclose certain vital information of their own and their activities.

The Ministry of Public Affairs will be in charge of managing a government public procurement electronic system, which will contain all documentation in connection with all public procurement acts executed. All information must be kept for a period of at least three years.

In general, all domestic and foreign corruption is addressed and prevented by certain general provisions stated in the Federal Anti-Money Laundering Law, in the Criminal Code and in the Public Officials Liabilities Federal Law.

**Lobbyists**

29 | What are the registration requirements for lobbyists or commercial agents?

There are no specific rules of general application regarding the registration of lobbyists or commercial agents.

**Limitations on agents**

30 | Are there limitations on the use of agents or representatives that earn a commission on the transaction?

There are no specific rules of general application regarding the use of agents or representatives that earn a commission on the transaction.

## AVIATION

**Conversion of aircraft**

31 | How are aircraft converted from military to civil use, and vice versa?

According to current Mexican legislation, there are no provisions regarding the conversion of an aircraft from military to civil use or vice versa.

**Drones**

32 | What restrictions are there on manufacture and trade of unmanned aircraft systems or drones?

Pursuant to mandatory rule 'CO AV23/10 R4', issued by the Ministry of Communication and Transportation by virtue of the General Civil Aviation Directorate, regarding market remote-piloted aircraft (RPA), manufacturers must:

- install an automatic mechanism on an RPA preventing the pilot from flying the aircraft beyond the pilot's horizontal distance;
- install an automatic mechanism on an RPA preventing the pilot from flying the aircraft beyond a certain altitude;
- add or install a mechanism allowing the RPA automatic identification (only applicable to the 'heavy' RPA category); and
- type approval or type certificate issued by the aviation authority.

Further, RPA sellers must comply with the following as set forth in such mandatory rule:

- the RPA package must include information that alerts the RPA owner that registration of the RPA with the Ministry of Communication and Transportation through a specific website General Civil Aviation Directorate is necessary;
- the owner must comply with the requirements and technical limitations established on such mandatory rule; and
- every time an RPA with a maximum take-off weight of 250g is sold, the form found in the mandatory rule 'CO AV23/10 R4' must be completed and filed with the General Civil Aviation Directorate.

On 14 November 2019, the Ministry of Communication and Transportation published in the Official Gazette of the Federation a Mexican Official Standard that outlines the requirements for the manufacturing, commercialisation and operation of remote-piloted aircraft systems in Mexican airspace. The Mexican Official Standard resumes most of the obligations applicable for the operators, manufacturers and traders under the mandatory rule CO AV23/10 R4. and entered into effect on 3 January 2020.

## MISCELLANEOUS

### Employment law

**33 Which domestic labour and employment rules apply to foreign defence contractors?**

For every employer that has a source of employment in Mexican territory, the applicable law will be the Federal Labour Law. In accordance with such law, companies must employ at least 90 per cent of Mexican employees, and a maximum of 10 per cent of specialised foreign workers.

### Defence contract rules

**34 Are there any specific rules that contractors, foreign or domestic, are bound by in defence contracts?**

Contractors are bound by the legal framework outlined in the previous answers, and specifically by:

- article 134 of the Mexican Constitution which provides the general principles for public procurement in Mexico at the federal and state levels;
- the Law of Acquisitions, Leases and Services of the Public Sector (the Public Procurement Law), which together with its ruling (the Regulation of the Public Procurement Law) comprise the main legal framework under which all federal public procurement for defence and security matters are regulated, and detail the general constitutional principles.
- At the local level, procurement for security goods and equipment is regulated in the state's public procurement legal framework, all of which contain somewhat similar provisions to those contained in the Public Procurement Law and its ruling.

**35 Do contractors avail themselves of these rules when they perform work exclusively outside of the jurisdiction?**

Defence contracts are governed by the Mexican public procurement laws (excluding the place of performance of the corresponding works).

### Personal information

**36 Must directors, officers or employees of the contractor provide personal information or certify that they fulfil any particular requirements to contract with a government entity?**

As long as contractors do not breach any of the 14 disqualification causes established in the Public Procurement Law, which do not establish the necessary disclosure of personal information, they will not be disqualified to contract with the Mexican government. The 14 disqualification causes are:

1 A public officer who intervened in any stage in the hiring of a person which the officer has personal, family or business interest.
2 Individuals who hold a job or position in a governmental entity, or any entity in which the aforementioned individuals directly or indirectly participated or were involved in its administration, without the prior and specific authorisation of the Ministry of Public Services.
3 Those suppliers who have had more than one administrative termination of their contract by the convening government body, within a period of two calendar years from the notification of the first termination.
4 Those who are ineligible by a resolution of the Ministry of Public Services in terms of the Public Procurement Law.
5 The suppliers that delayed the delivery of goods and services subject to prior executed contracts with the government body.
6 Those who have been declared insolvent in a bankruptcy process or any other similar processes.
7 Entities that are looking to participate in a new public procurement procedure and that have provided or are providing, directly or through any subsidiary or related entity of the same corporate group, work related to the analysis, quality review or development of requirements, budgeting or any other activity related to the purpose of such new public procurement procedure.
8 Entities that submit proposals, in a single public procurement procedure, for the same good or service, and that are linked to another submitting entity to the same procedure, by partners or shareholders.
9 Individuals who, by themselves or through companies that are part of the same business group, intend to be hired to prepare reports, expert opinions and appraisals to be used to resolve discrepancies arising from contracts in which they are a party of.
10 Suppliers that execute and deliver agreements regulated under the Public Procurement Law, without the express authorisation to use intellectual property rights.
11 Those who hire advisory, consulting and support services from any type of person in the field of government contracting.
12 Bidders that did not formalise a contract for an unjustified cause.

Nevertheless, the contractor must disclose certain information regarding its shareholders and legal representatives when registering with the Contractors Sole Registry in order to be approved as a government contractor. The information to be provided is:

- the contractor's corporate name, nationality and address;
- its incorporation files and any amendments to its by-laws;
- a list of its current shareholders;
- names of its legal representatives and corresponding appointments;
- the contractor's expertise and experience;
- information regarding its technical and financial capacities; and
- the contractor's record in prior public biddings.

### Licensing requirements

**37 What registration or licensing requirements exist to operate in the defence and security sector in the jurisdiction?**

As any other contractor with the Mexican government, defence and security contractors can only be registered as approved contractors in the Contractors Sole Registry.

The above-mentioned requirement is applicable only to federal procurement processes. The registration or licensing requirements may vary at the local level and, therefore, we strongly suggest reviewing the specific local applicable law since each of the 32 Mexican federal states has a specific applicable law.

**Environmental legislation**

38 | What environmental statutes or regulations must contractors comply with?

Contractors are expected to comply with environmental statutes and regulations of general application established in the Mexican legal framework, including the Public Procurement Law, concerning the protection of the environment and sustainable development.

The legislation forming the environmental legal framework includes:

- the General Law of Ecological Balance and Environmental Protection;
- the Law of National Waters;
- the General Law of Sustainable Forestry Development;
- the General Law of Wildlife;
- the Law of Sustainable Rural Development;
- the General Law for the Prevention and Integral Management of Waste;
- the Law of Biosecurity of Genetically Modified Organisms;
- the Law of Organic Products;
- the General Law of Sustainable Fishing and Aquaculture;
- the Law of Promotion and Development of Bioenergy;
- the Federal Law of Environmental Responsibility;
- the General Law of Climate Change; and
- each law's own regulations and rulings.

Mexico is also a party to the following international agreements:

- the Convention on Indigenous and Tribal Peoples 1989;
- the North American Commission for Environmental Cooperation 1994; and
- the Kyoto Protocol to the United Nations Framework Convention on Climate Change 1992.

39 | Must companies meet environmental targets? What are these initiatives and what agency determines compliance?

Environmental targets should be met by companies during the performance of the procurement contract. The compliance with these laws is determined by the Ministry of Environment and Natural Resources (regulatory authority) and the Federal Prosecutor's Office for Environmental Protection (sanctioning authority).

40 | Do 'green' solutions have an advantage in procurements?

No, as all bidders must comply with the regulations contained in the Public Procurement Law and with the Mexican legal framework regarding the protection of the environment and sustainable development.

However, in the bidding process contractors must ensure they offer the best available conditions in terms of energy efficiency, responsible use of water, optimisation and sustainable use of resources, as well as environmental protection.

## UPDATE AND TRENDS

**Key developments of the past year**

41 | What were the key cases, decisions, judgments and policy and legislative developments of the past year?

On 27 May 2019, a decree creating the National Guard Law was issued. The National Guard is a new public security institution, of a civil, disciplined and professional nature, assigned as a decentralised administrative body of the Ministry of Security and Citizen Protection. The purpose of the National Guard is to carry out public security functions under the responsibility of the Federation and, if necessary, in accordance with the agreements entered into for such purpose and to temporarily collaborate in public security tasks with the states or municipalities.

On 9 July 2019, the decree forming the Asset Forfeiture National Law was issued. The decree permits the Mexican state to destroy property and assets related to the commission of certain crimes, set forth in article 22 of the Mexican Constitution.

On 19 November 2019, the decree forming the Federal Law of Republican Austerity was issued. Its purpose is to regulate the austerity measures applying to the exercising of federal public expenditure and to help ensure that the economic resources available are managed effectively, efficiently, economically, transparently and honestly.

**Coronavirus**

42 | What emergency legislation, relief programmes and other initiatives specific to your practice area has your state implemented to address the pandemic? Have any existing government programmes, laws or regulations been amended to address these concerns? What best practices are advisable for clients?

On 30 March 2020, the Federal government declared the epidemic of covid–19 as a health emergency due to force majeure. Since then, there have been numerous publications related to governmental measures against covid–19. Most of these decrees refer to suspension of terms and activities of different ministries, as well the authorisation to carry out certain activities or procedures, including public procurement procedures, at a distance using computer tools.

The following are the most important decrees related to defence and security public procurement:

- 30 March 2020 – an agreement by which the epidemic of covid–19 is declared a health emergency due to force majeure.
- 31 March 2020 – an agreement establishing extraordinary actions to address the health emergency generated by the SARS-CoV2 virus.
- 1 April 2020 – an agreement suspending terms in the Ministry of Economy and establishing administrative measures to contain the spread of the coronavirus covid-19.
- 1 April 2020 – an agreement by which the terms and activities of the Ministry of Governance are suspended, with the exclusions indicated therein.

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- 3 April 2020 – an agreement establishing extraordinary actions to be carried out for the acquisition and import of goods and services referred to in sections II and III of article two of the Decree declaring extraordinary actions in affected regions throughout the national territory in terms of general health to combat the serious disease of priority attention generated by the SARS-CoV2 virus (covid–19), published on 27 March 2020.
- 30 April 2020 – an agreement extending the suspension of the terms and activities of the Ministry of Governance until 30 May 2020, with the exclusions indicated therein.
- 7 May 2020 – an agreement by which the suspension of the administrative activities is extended, as well as the terms and conditions related to the procedures, administrative procedures and administrative resources, corresponding to the General Direction of Private Security, dependent on the Ministry of Security and Citizen Protection and the operation of the electronic counter.
- 29 May 2020 – an agreement by which the administrative activities are resumed and the suspension of terms and deadlines related to the procedures, administrative procedures and administrative appeals corresponding to the General Office of Private Security under the Ministry of Security and Citizen Protection is lifted and the operation of the electronic counter for the reception of the indicated procedures is continued.

We strongly advise clients remain up-to-date on the suspending and reestablishing of deadlines corresponding to procedures they are required to carry out before different government bodies in Mexico.

The above list is only applicable at the federal level. State governments are entitled to apply different measures to public procurements procedures.

# Norway

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## LEGAL FRAMEWORK

### Relevant legislation

1 | What statutes or regulations govern procurement of defence and security articles?

The following acts and regulations govern the procurement of defence and security articles in Norway:

- Public Procurement Act No. 73 of 17 June 2016; and
- Regulation No. 974 of 12 August 2016 on Public Procurement (RPP).

The above constitute the general legislation on civil public procurement. They apply to procurements by the armed forces and the Ministry of Defence, unless the category of procurement is exempt under the Regulation on Defence and Security Procurement or article 123 of the European Economic Area Agreement (EEA article 123).

**Regulation No. 1185 of 4 October 2013 on Defence and Security Procurement (FOSA)**

Regulation No. 1185 of 4 October 2013 on Defence and Security Procurement (FOSA) is Norway's implementation of the EU Defence Procurement Directive, and applies to the procurement of specific defence and security materiel, or construction work or services in direct relation to such, unless EEA article 123 provides for a defence and security exemption.

**Norwegian Defence Acquisition Regulations No. 1411 of 25 October 2013**

Parts I and II of the Norwegian Defence Acquisition Regulations No. 1411 of 25 October 2013 (DAR) apply to all defence-related procurement. Part III applies to defence procurement under the Public Procurement Act and Regulation. Part IV applies to procurement under FOSA. Part V applies to procurement that is entirely exempt from the procurement regulations under article 123 of the European Economic Area Agreement (EEA article 123).

These regulations are internal instructions for the Ministry of Defence and its agencies (see DAR section 1–2). They do not provide any rights to third parties and thus a breach of these rules cannot be relied on in court by a dissatisfied contractor.

**Regulation No. 2053 of 20 December 2018 on Organisations' work on Preventative Safety (Operations Security Regulations)**

This regulation applies where the procurement procedure requires a security classification.

**National Security Act No. 24 of 1 June 2018**

The National Security Act applies where the procurement procedure requires a security classification.

### Identification

2 | How are defence and security procurements identified as such and are they treated differently from civil procurements?

Section 1-3, paragraph 1 of FOSA defines defence and security procurements in accordance with article 2 of EU Directive 2009/81/EC.

The procedures vary according to the nature of the goods and services to be procured. If the goods are not classified, ordinary civil procurement law applies. Where the goods or services are highly sensitive, or their requirements or specifications are classified, the entire procurement procedure may be exempt from ordinary procurement rules under EEA article 123. In that case, only DAR Part V applies, and the Ministry of Defence will also generally require offset agreements.

### Conduct

3 | How are defence and security procurements typically conducted?

DAR section 7-3 requires the procuring authority to assess the nature of the procurement, and to assess which set of regulations applies.

All defence procurement must be based on a formal market study, which forms the basis for a need assessment with realistic requirements for materiel and services (DAR sections 7-1 and 6-1). As a main rule, all contracts are subject to competitive bidding and published on Doffin, the Norwegian national notification database for public procurement.

The procuring authority may select the procuring procedure, with due care shown to the need for competition and national security interests. Outside the RPP and FOSA, there is no requirement for prior publication of a contract notice. Depending on certain circumstances related to EEA threshold values and the type of procurement, the procuring authority may choose to conduct the procurement without competition through a single-source procurement, to engage in selective bidding, competitive dialogue or a negotiated procedure with or without prior publication of a contract notice.

Use of competitive dialogue or a negotiating procedure without prior publication of a contract notice is contingent on the fulfilment of the conditions in FOSA sections 5-2 and 5-3, respectively.

The procuring authority will evaluate offers, and then decide whether to accept an offer. Normally, the procuring authority imposes a grace period between the decision and the contract-signing to allow for any complaints concerning the procurement from competing contractors (see FOSA Chapter 14).

### Proposed changes

4 | Are there significant proposals pending to change the defence and security procurement process?

No.

**Information technology**

5 Are there different or additional procurement rules for information technology versus non-IT goods and services?

No, but certain forms of command and control systems and components technology, including software, may be liable for offset purchases as Norway prioritises such technology under offset obligations in EEA article 123.

**Relevant treaties**

6 Are most defence and security procurements conducted in accordance with the GPA or other treaty-based procurement rules, or does this jurisdiction commonly use the national security exemption to procure them?

Both the European Union and Norway are members of the World Trade Organization, and are consequently parties to the Agreement on Government Procurement (GPA). Directive 2009/81/EC does not govern arms trade with third countries which continues to be governed by the GPA.

Norway does use a national security exemption on occasion, so may deviate from Directive 2009/81/EC where the procurement has essential security interests and falls under EEA article 123, or warrants an exception in accordance with the Operations Security Regulation. Such exemptions require approval from the Ministry of Defence.

## DISPUTES AND RISK ALLOCATION

**Dispute resolution**

7 How are disputes between the government and defence contractor resolved?

The Norwegian Defence Acquisition Regulations No. 1411 of 25 October 2013 (DAR) section 9-10 prescribes that the procuring authority requires contracts in the defence and security sector to dictate Norwegian law as the governing law, with Oslo District Court as the governing venue.

8 To what extent is alternative dispute resolution used to resolve conflicts? What is typical for this jurisdiction?

Generally, disputes are resolved through negotiations, and, if this is unsuccessful, through the Oslo District Court (see Armed Forces of Norway Form 5052 – General Purchase Conditions section 15). These conditions are used in small and medium-sized contracts, whereas larger contracts may require supplementary or alternative contracts and terms. Normally, larger contracts are based on the same contract principles and conditions that are used in Form 5052.

Arbitration is rarely used in Norwegian defence contracts.

Although the relationship between a prime contractor and a subcontractor is usually considered an internal matter, the procuring authority may, in certain circumstances, such as classified information disclosure, require that the prime contractor include clauses on conflict resolution equivalent or similar to those as stipulated in DAR.

DAR section 9-10 allows for deviations, such as accepting another country's jurisdiction or laws, if the contract involves international aspects and the deviation is necessary owing to the nature of the negations and the safeguarding of Norwegian interests. Whether to deviate is a matter of a case-by-case assessment and, in general, a foreign contractor ought not to rely on a requirement to apply national laws when negotiating with the Norwegian government.

**Indemnification**

9 What limits exist on the government's ability to indemnify the contractor in this jurisdiction and must the contractor indemnify the government in a defence procurement?

The procuring authority is entitled to compensation for direct losses caused by delay or defect (see Armed Forces of Norway Form 5052 sections 6.6 and 7.7). The contractor is liable for indirect losses caused by his or her negligence. In larger contracts, the procuring authority may accept a limit on the contractor's liability for direct or indirect losses.

Form 5052 section 10.1 provides that the procuring authority must indemnify the contractor from any claim owing to the use of drawings, specifications or licences provided by the procuring authority. The contractor must, in turn, indemnify the procuring authority from any claim owing to patent infringement or other immaterial rights related to the completion of the agreement.

In accordance with Armed Forces of Norway Form 5055 – General Terms for Cost Control, the following costs are considered unallowable should they incur in any contract:

- penalties;
- fines and compensatory damages; or
- costs and legal fees for legal action or preparation of such.

Further, the standard procurement contract states that, in the event of default, the armed forces shall pay interest in accordance with Act No. 100 of 17 December 1976 Relating to Interest on Overdue Payments etc. (See Armed Forces of Norway Form 5052 section 5.2.) As such, the maximum interest rate is currently set at 8 per cent.

**Limits on liability**

10 Can the government agree to limit the contractor's liability under the contract? Are there limits to the contractor's potential recovery against the government for breach?

If the procurement is time-sensitive or otherwise warrants it, the procuring authority must contractually require the contractor to pay liquidated damages upon failure to meet any deadlines (DAR section 26-4). Liquidated damages shall incur at 0.001 per cent of the contract price per working day, related to the part of the delivery that is unusable owing to the delay. Normally, the maximum liability shall be set at 10 per cent of the price for the same part.

The procuring authority may also exempt the contractor from liquidated damages or accept an extension of time in the implementation and execution of the procurement. If the waiver exceeds 500,000 Norwegian kroner, the procuring authority must request prior approval from the Ministry of Defence (see Parts I and II of the Norwegian Defence Acquisition Regulations No. 1411 of 25 October 2013 (DAR) sections 5-5 and 5-9).

**Risk of non-payment**

11 Is there risk of non-payment when the government enters into a contract but does not ensure there are adequate funds to meet the contractual obligations?

The Norwegian government budgets future procurement through a long-term strategy. The strategy is updated on an annual basis and is valid for a seven-year period. The current plan – Future Acquisitions for the Norwegian Defence Sector 2021–24 – is available from the Norweigan government's website.

The risk of non-payment for contractual obligations, excluding contract disputes, is non-existent as the procuring authority evaluates budgetary limits before entering into a contract.

**Parent guarantee**

12 | Under what circumstances must a contractor provide a parent guarantee?

The contractor must have financial strength that is proportionate with the financial risks entailed by the contract in question. If the procuring entity has doubts concerning the contractor's financial ability, it may request adequate security of performance of the contract. The procuring authority calculates the need for security based on the perceived consequences for the defence sector, should the contractor incur financial problems.

In accordance with DAR section 18-6, paragraph 6, or section 36-2, such security could be in the form of a guarantee from a bank, financial institution or insurance company, or a parent guarantee. In the case of parent guarantees, the guarantee must be issued by the highest legal entity in the corporate group and reflect the contractor's obligations under the contract.

In larger contracts, the use of a performance guarantee is usually the norm and the guarantee used is often that of a parent guarantee.

The main rule in Norwegian defence procurement is payment upon delivery or the achievement of milestones. Under certain circumstances, the procuring authority may pay the contractor prior to fulfilment. In such situations, the contractor shall provide a surety for payments due before delivery (see DAR section 23-7). The surety shall cover the full amount of any outstanding payment.

## DEFENCE PROCUREMENT LAW FUNDAMENTALS

**Mandatory procurement clauses**

13 | Are there mandatory procurement clauses that must be included in a defence procurement contract or that will be read into the contract regardless of their actual inclusion?

The procuring authority must include a number of clauses in its contract, such as clauses on termination, damages, transparency and warranties. The exact wording and depth of such clauses fall under the discretion of the procuring authority.

**Cost allocation**

14 | How are costs allocated between the contractor and government within a contract?

The allocation of costs between the contractor and the government is dependent on the choice of the contract (see the Norwegian Defence Acquisition Regulations No. 1411 of 25 October 2013 (DAR) section 26-9, paragraph 1). The procuring authority may use the following contract types concerning aspects of the delivery and costs:

- cost contracts: the contractor is only obliged to deliver the goods or services if they receive payment of the relevant costs under the contract (see DAR section 19-2, paragraph 2b); or
- price contracts: the contractor is obliged to deliver the goods or services at an agreed price, regardless of the actual costs incurred (see DAR section 19-2, paragraph 2a).

**Disclosures**

15 | What disclosures must the contractor make regarding its cost and pricing?

The procuring authority will list the contractor's completion of the Armed Forces of Norway Form 5351 – Specification of Pricing Proposal as a qualification criterion where a cost analysis is required.

**Audits**

16 | How are audits of defence and security procurements conducted in this jurisdiction?

Normally, the procuring authority shall request the right to review the contractor's accounting in order to monitor their performance under the contract (see DAR section 27-2, paragraph 1).

Additionally, the procuring authority shall contractually require the contractor to supply specific information in a number of circumstances, for instance, where cost controls are required, where there is suspicion of economic irregularities or when the contractor is foreign. The procuring authority may also demand that the contractor include contract clauses with subcontractors belonging to the same company group as the contractor, or in whom the contractor has a controlling interest, or vice versa, allowing the procuring authority equivalent rights to information and to audit (see DAR section 27-4).

If the procurement has uncertain price calculations, or if the procuring authority conducts the procurement without competition, the procuring authority shall perform a cost control of the contractor's offer regardless of contract type, both before work commencement and during the fulfilment of the contract.

Additionally, cost control on accrued expenses and costs is required regardless of competition for all cost contracts (incentive, fixed or no compensation for general business risks, or cost-sharing) as well as price contracts with limited risk compensation or incentive.

Lastly, the procuring authority shall perform cost control on procurement from a foreign sole contractor.

The procuring authority conducts the cost control in accordance with Armed Forces of Norway Form 5055 – General Terms for Cost Control.

Upon confirming the correctness of its costs in Armed Forces of Norway Form 5351 – Specification on Pricing Proposal, the contractor shall give the procuring authority the right to audit the costs in accordance with Form 5055.

**IP rights**

17 | Who gets the ownership rights to intellectual property created during performance of the contract? What licences are typically given and how?

DAR section 24-3 obliges the procuring authority to consider the legal opportunity, wholly or partly, to acquire the intellectual property rights covered by the contract, including any right of use.

The main rule, in accordance with DAR section 24-4, is that the procuring authority shall acquire a non-exclusive licence to the IP rights, if this meets the needs of the armed forces and constitutes the most economically advantageous option. A non-exclusive licence shall include interface documentation and the rights of usage.

Under DAR section 24-5, the procuring authority shall acquire the IP rights or an exclusive licence if this is considered necessary or appears to be the most economically advantageous option, or there are significant security considerations. If the procuring authority is unable to acquire a wholly exclusive licence, it shall consider whether to partly acquire the rights, or enter into both exclusive and non-exclusive licence agreements (see DAR section 24-6).

If Norway has financed the research and development of a deliverable, the procuring authority is obliged to enter into a royalty agreement with the contractor, normally requiring 5 per cent of the sale price (see DAR section 24-10).

DAR section 24-7 states that the procuring authority must ensure that a contract concerning IP rights contains provisions concerning, among other things, the possibility of the procuring authority making available documentation related to the IP rights to the entire defence sector within Norway, and to other countries' armed forces should it

prove necessary; and a clause that if the deliverable is not fully developed, produced, industrialised or commercialised, the defence sector receives the IP rights necessary to recover their costs through a resale. This clause must stipulate that the transferred IP rights may be subject to completion, development, production, industrialisation or commercialisation by another contractor, or resold to cover the defence sector's share of the costs.

**Economic zones**

18 Are there economic zones or other special programmes in this jurisdiction commonly utilised by foreign defence and security contractors for financial or other procurement related benefits?

Not applicable.

**Forming legal entities**

19 Describe the process for forming legal entities, including joint ventures, in this jurisdiction.

**Limited liability company**

To form a limited liability company, the shareholders must compile and sign the following documentation:

- a memorandum of association;
- articles of association;
- confirmation from a bank, financial institution, attorney or auditor that the share capital has been paid. The share capital requirement for a limited liability company is 30,000 Norwegian kroner, while public limited liability companies have a requirement of 1 million Norwegian kroner; and
- a declaration of acceptance of assignment from an auditor, or minutes of a board meeting if the company has decided against using an auditor.

Following this process, the company registers in the Register of Business Enterprises with the documents enclosed. Registration may be done electronically and takes, in general, no more than one to five business days. Registration must be completed before the company commences commercial activities, and within three months after signing the memorandum of association at the latest.

**Partnerships**

Norwegian law recognises three forms of partnerships: a general partnership with joint liability, general partnership with several (proportionate) liability, and limited partnerships.

To form a partnership, the partners must sign and date a partnership agreement and register the partnership in the Register of Business Enterprises with the agreement enclosed, before the company commercially activates and within six months of signing the partnership agreement. The partnership's headquarters must be located within Norway, though its partners do not need to be resident there.

**Joint venture**

It is usual to form a joint venture by establishing a separate company. While several forms of incorporation are available, parties generally choose a limited liability company.

Another way to establish a joint venture is through a simple cooperation or joint venture agreement between the parties.

**Norwegian-registered foreign enterprises**

While Norway does not consider a Norwegian-registered foreign enterprise (NUF) to be a separate legal entity, foreign companies frequently use them owing to their practical nature.

When a foreign company wants to register a branch in Norway, the branch can register as a NUF. To form a NUF, or to conduct business within Norway in general, the foreign company must register in the Register of Business Enterprises. The foreign parent company is fully responsible for the activity of its branch owing to the lack of recognition of its separate legal status.

**Access to government records**

20 Are there statutes or regulations enabling access to copies of government records? How does it work? Can one obtain versions of previous contracts?

Anyone seeking access to information from Norwegian ministries is entitled to request any unclassified information, including previous contracts, under Act No. 16 of 19 May 2006 on the Freedom of Information. The responsible ministry receives any requests for information and performs a case-by-case review of whether to approve the request. This review also entails the assessment of whether to approve the request with or without redactions.

**Supply chain management**

21 What are the rules regarding eligible suppliers and supply chain management and anti-counterfeit parts for defence and security procurements?

There are no general rules concerning counterfeit parts, though the contractor must certify that the deliverables conform in all aspects to the contract requirements (see the Armed Forces Form 5357 – Certificate of Conformity).

The procuring authority often requires materiel and deliveries to be accompanied by relevant certificates of quality and specifications, such as allied quality assurance publications, which also allows the procuring authority to conduct inspections at the contractors' and subcontractors' place of production. The procuring authority may also require a certificate of origin to ensure that the deliverable is not from an embargoed country, among other things.

## INTERNATIONAL TRADE RULES

**Export controls**

22 What export controls limit international trade in defence and security articles? Who administers them?

The export of certain defence-related goods, technology and services, or services related to trade or assistance concerning the sale of such deliverables, or the development of another country's military capability, is conditional on acquiring a licence from the Ministry of Foreign Affairs in accordance with Regulation No. 718 of 19 June 2013 on the Export of Defence-related Products, Dual-use Items, Technology and Services, which only governs the export and import between Norway and other EEA countries.

The export of such products to the EEA is subject to general transfer licences covering specific product categories and recipients, global transfer licences covering specific defence-related product categories (and services) or recipients for a period of three years, and finally, individual transfer licences covering the export of a specific quantity or specific defence-related product to a recipient in one EEA state.

For countries other than those belonging to the EEA, the Ministry of Foreign Affairs distinguishes between the following categories:

- Group 1: the Nordic countries and members of NATO.
- Group 2: countries not belonging to Group 1 that the Ministry of Foreign Affairs have approved as recipients of arms.

- Group 3: countries not belonging to Group 1 or 2 and to which Norway does not sell weapons or ammunition, but which can receive other goods as listed in Annex I of Regulation 2009/428/EC.
- Group 4: countries that are located in an area with war, the threat of war, civil war or general political instability that warrants the deterrence of export of defence-related goods and services, or that is subject to sanctions by the United Nations, EU or the Organization for Security and Co-operation in Europe (OSCE). As a member of the UN, Norway is a state party to the UN Arms Trade Treaty.

For export to Groups 1 to 3 (above), the Ministry of Foreign Affairs may grant the following licences in accordance with their guidelines:

- Export licence: valid for one year and for a single export of goods.
- Service licence: valid for one year and for a single export of services.
- Technology transfer licence: valid for one year and for a single export of technology.
- Global export licence: valid for a maximum of three years and for one or several exports of one or several defence-related goods to one or several specific recipients outside of the EEA, within NATO or other countries of relations.
- Project licence: valid for one or several exports of defence-related goods, services or technology to one or several collaboration partners or subcontractors in conjunction with development projects where a state within Group 1 is the final end-user.

For Group 4, an export licence valid for one single export may be granted in certain situations.

As a member state of the EEA, Norway also adheres to the Council Common Position 2008/944/CFSP defining common rules governing control of exports of military technology and equipment, and has transposed its criteria listed in article 2 when assessing whether to grant a licence.

**Domestic preferences**

23 | What domestic preferences are applied to defence and security procurements? Can a foreign contractor bid on a procurement directly?

Norwegian defence procurement is generally not conducted with domestic preference, and the possibility of making direct bids will vary with the rules governing the procurement procedure.

In accordance with Regulation No. 1185 of 4 October 2013 on Defence and Security Procurement (FOSA) article 3-2 and DAR's preamble, all procurement shall as far as possible be based on competition, and the procuring authority shall not discriminate against a contractor owing to nationality or local affiliation. Parts I and II of the Norwegian Defence Acquisition Regulations No. 1411 of 25 October 2013 (DAR) section 34-2 allows the procuring authority to conduct the procurement without competition in certain specific circumstances, similar to the exemptions from competition under ordinary EEA procurement law.

Further, Norway may deviate from Directive 2009/81/EC where the procurement has essential security interests and falls under article 123 of the European Economic Area Agreement, or warrants exception in accordance with the Operations Security Regulation. Exemptions require approval from the Ministry of Defence.

The aforementioned exemptions may, under certain circumstances, result in the procuring authority allowing only Norwegian contractors to submit offers for the request of tender.

**Favourable treatment**

24 | Are certain treaty partners treated more favourably?

Certain countries enjoy the benefit of bilateral security agreements with Norway, which eases the exchange and certification of contractors with regard to classified information related to procurements. Members of the EEA also have the advantage of a common transfer licence arrangement.

**Sanctions**

25 | Are there any boycotts, embargoes or other trade sanctions between this jurisdiction and others?

Norway enforces mandatory UN and EU arms embargoes and sanctions.

Additionally, Norway enforces the embargo on Artsakh, also known as Nagorno–Karabakh, which remains internationally recognised as being part of Azerbaijan, through its membership of the OSCE.

**Trade offsets**

26 | Are defence trade offsets part of this country's defence and security procurement regime? How are they administered?

Offset agreements are required in the procurement of defence and security articles from foreign contractors. This also includes contractors based in Norway if they produce essential parts of the delivery abroad. Exceptions to this rule are procurements that are:

- conducted in accordance with the Regulation No. 974 of 12 August 2016 on Public Procurement;
- conducted in accordance with FOSA, where the contractor (and most of its subcontractors) are located within the EEA;
  - if the contractor is domiciled in the EEA, but one of its subcontractors is not and the value of the subcontract exceeds 50 million Norwegian kroner, said subcontractor shall be made a party to an offset agreement with the procuring authority; and
- conducted with a contract price below 50 million kroner, provided that the contract does not include future options or additional procurement that may exceed this threshold or the procuring authority expects that the contractor will enter into several contracts below 50 million Norwegian kroner over a period of five years.

The procuring authority manages trade offsets by enclosing the provisions contained in the Regulation for Industrial Co-operation related to Defence Acquisitions from Abroad to the request for tender. The foreign contractor compiles a proposal on the offset requirement and delivers it to the Ministry of Defence or Norwegian Defence Materiel Agency. The offset agreement is a precondition for accepting the contractor's tender. Consequently, the procuring authority conducts negotiations for the procurement contract, while the Ministry of Defence or Norwegian Defence Materiel Agency conducts simultaneous negotiations concerning the offset agreement.

## ETHICS AND ANTI-CORRUPTION

**Private sector appointments**

27 | When and how may former government employees take up appointments in the private sector and vice versa?

There is no mandatory waiting period for former government employees wanting to enter the private sector.

However, certain government employees have a duty to inform the Board of Quarantine, which is tasked with deciding whether the employee would have to undergo a waiting period before entering into the private sector or receive a temporary ban on their involvement in specific cases.

Norwegian Defence Acquisition Regulations No. 1411 of 25 October 2013 (DAR) section 2-5 prescribes that if the contractor's personnel have been employed by the Ministry of Defence or in the defence sector within the past two years, or are retired, they are prohibited from being involved in the contact between the contractor and the Norwegian defence. The contractor shall inform the procuring authority if they have hired or otherwise used such personnel.

There are no general restrictions on private-sector employees' appointment to public sector positions.

**Addressing corruption**

28 How is domestic and foreign corruption addressed and what requirements are placed on contractors?

Corruption within Norway is punishable by law and carries a maximum penalty of 10 years in prison (see the Norwegian Penal Code sections 387 and 388).

DAR section 3-2 dictates that in any procurement that exceeds the current national threshold value at the time of the request for tender's publication, the procuring authority must contractually require the contractor to warrant that it has measures or systems in place to prevent corruption or the abuse of influence. Such measures or systems may entail internal controls or ethical guidelines.

For procurements exceeding the aforementioned threshold value, DAR section 4-1 requires that the procuring authority issue to the contractor or attach to any request for tender the Ethical Statement for Suppliers to the Royal Norwegian Ministry of Defence with underlying agencies (DAR appendix 5).

The statement obliges the contractor to adhere to the ethical guidelines and not:

> *[ . . . ] to offer any gift, benefit or advantage to any employee or anyone else who is carrying out work for the MoD or underlying agencies, if the gift, benefit or advantage may be liable to affect their service duties. This rule applies regardless of whether the gift, benefit or advantage is offered directly, or through an intermediary.*

Failure to comply with these requirements may lead to rejection of the contractor's current and future offers to the Ministry of Defence or its underlying agencies.

**Lobbyists**

29 What are the registration requirements for lobbyists or commercial agents?

Lobbyists or commercial agents are not subject to any general registration requirements, though commercial agents who directly engage or provide assistance in the export of certain defence and security articles require an export licence from the Ministry of Foreign Affairs.

DAR section 7-4, paragraph 2 dictates that the procuring authority shall provide contractors, at the request for tender, with the guidelines on prudence, non-disclosure and conflict of interest (DAR appendix 3):

> *The name of any lobbyist acting on behalf of the supplier must be reported to the Defence sector. If a supplier fails to act with openness and strict adherence to good business practices and high ethical standards, this may undermine trust in the relationship between the supplier and the Defence sector, and potentially also the rating of the supplier's bid in the final decision process.*

**Limitations on agents**

30 Are there limitations on the use of agents or representatives that earn a commission on the transaction?

Norwegian law does not contain any limitations on the use of agents or representatives that earn a commission on transactions between a contractor and a procuring authority.

If the contract in question is between the procuring authority and an agent, the procuring authority may require disclosure of the commission or agreement between the agent and the contractor (see DAR section 17-3, paragraph 7).

If the contract falls under article 123 of the European Economic Area Agreement, the procuring authority may not enter into a contract with an agent (see DAR section 36-3).

## AVIATION

**Conversion of aircraft**

31 How are aircraft converted from military to civil use, and vice versa?

When converting military aircraft to civilian use, the process is subject to a case-by-case pre-conference review by the Civil Aviation Authority, which reviews the relevant documentation, with applicable procedures for registration of ownership, security and certification from the civil aircraft register to follow.

When a civilian aircraft is considered converted for military use, the armed forces perform a case-by-case assessment of the aircraft's military use and capabilities, and requirements concerning the aircraft's safety and airworthiness. Upon acceptance of the conversion, the armed forces notify the Civil Aviation Authority and the aircraft receives the appropriate marking and certification in the military aircraft register.

Deletion of the aircraft's certification in the civil aircraft register is a prerequisite for certification in the military aircraft register.

**Drones**

32 What restrictions are there on manufacture and trade of unmanned aircraft systems or drones?

There are none.

## MISCELLANEOUS

**Employment law**

33 Which domestic labour and employment rules apply to foreign defence contractors?

The Working Environment Act No. 62 of 17 June 2005 and Regulation No. 112 of 8 February 2008 on Wages and Working Conditions in Public Contracts will apply if the contractor is operating or performs work within Norway.

Contractors performing work within Norway on procurements exceeding 100,000 Norwegian kroner, excluding value-added tax, shall provide the contracting authority with a health, safety and environment (HSE) statement warranting that the contractor complies with all legal requirements pertaining to HSE (see Regulation No. 1185 of 4 October 2013 on Defence and Security Procurement (FOSA) sections 3-13 and 8-18).

The procuring authority shall contractually require the contractor to adhere to the national legislation related to wages and working conditions in the country where the contractor carries out work (Norwegian Defence Acquisition Regulations No. 1411 of 25 October 2013 (DAR) section 3-1). Further, the contractor shall adhere to the prohibition

against child, forced and slave labour, discrimination and the right to organise in accordance with the UN Convention on the Rights of the Child and ILO Conventions Nos. 29, 87, 98, 100, 105, 111, 138 and 182.

**Defence contract rules**

34 | Are there any specific rules that contractors, foreign or domestic, are bound by in defence contracts?

The Armed Forces of Norway Form 5052 – General Purchase Conditions are used in small and medium-sized contracts, whereas larger contracts may require supplementary or alternative contracts and terms. Normally, larger contracts are based on the same contract principles and conditions that are used in Form 5052.

Although the relationship between a prime contractor and a subcontractor is usually considered an internal matter, the procuring authority may, in certain circumstances, such as during a classified information disclosure, require that the prime contractor include clauses equivalent or similar to those as stipulated in the Parts I and II of the Norwegian Defence Acquisition Regulations No. 1411 of 25 October 2013 (DAR).

DAR section 9-10 prescribes that the procuring authority requires contracts in the defence and security sector to dictate Norwegian law as the governing law, with Oslo District Court as the governing venue. Arbitration is rarely used in Norwegian defence contracts. Section 9-10 allows for deviations from Form 5052 (eg, accepting governing law or venue of a country other than Norway if the contract involves international aspects and the deviation is necessary owing to the nature of the negations and the safeguarding of Norwegian interests).

The procuring authority is entitled to compensation for direct losses caused by delay or defect (see Form 5052 sections 6.6 and 7.7). The contractor is liable for indirect losses caused by his or her negligence. In larger contracts, the procuring authority may accept a limit on the contractor's liability for direct or indirect losses.

Form 5052 section 10.1 provides that the procuring authority must indemnify a contractor from any claim owing to the use of drawings, specifications or licences provided by the procuring authority. The contractor must, in turn, indemnify the procuring authority from any claim owing to patent infringement or other immaterial rights related to the completion of the agreement.

If the procurement is time-sensitive or otherwise warrants it, the procuring authority must contractually require the contractor to pay liquidated damages upon failure to meet any deadlines (DAR section 26-4). Liquidated damages shall incur at 0.001 per cent of the contract price per working day, related to the part of the delivery that is unusable owing to the delay. Normally, the maximum liability shall be set at 10 per cent of the price for the same part.

As a main rule, the procuring authority shall request the right to review the contractor's accounting in order to monitor their performance under the contract (see DAR section 27-2, paragraph 1). Additionally, the procuring authority shall contractually require the contractor to supply specific information in a number of circumstances, for instance, where cost controls are required, where there is suspicion of economic irregularities or when the contractor is foreign.

The main rule, in accordance with DAR section 24-4, is that the procuring authority shall acquire a non-exclusive licence to the IP rights, if this meets the needs of the armed forces and constitutes the most economically advantageous option. A non-exclusive licence shall include interface documentation and the rights of usage.

Under DAR section 24-5, the procuring authority shall seek to acquire the IP rights or a whole or partly exclusive licence if this is considered necessary or appears to be the most economically advantageous option, or there are significant security considerations. If Norway has financed the research and development of a deliverable, the procuring authority is obliged to enter into a royalty agreement with the contractor, normally requiring 5 per cent of the sale price (see DAR section 24-10).

There are no general rules concerning counterfeit parts, though the contractor must certify that the deliverables conform in all aspects to the contract requirements (see the Armed Forces Form 5357 – Certificate of Conformity).

35 | Do contractors avail themselves of these rules when they perform work exclusively outside of the jurisdiction?

The procuring authority shall contractually require the contractor to adhere to the national legislation related to wages and working conditions in the country where the contractor carries out work (DAR section 3-1). Further, the contractor shall adhere to the prohibition against child, forced and slave labour, discrimination and the right to organise in accordance with the UN Convention on the Rights of the Child and ILO Conventions Nos. 29, 87, 98, 100, 105, 111, 138 and 182.

**Personal information**

36 | Must directors, officers or employees of the contractor provide personal information or certify that they fulfil any particular requirements to contract with a government entity?

DAR section 4-1 mandates that the procuring authority issue to the contractor the Ethical Statement for Suppliers to the Royal Norwegian Ministry of Defence with underlying agencies. The procuring authority shall issue the statement (DAR appendix 5) to the contractor together with the request for tender or otherwise.

The statement places a duty on the contractor to inform the procuring authority if the contractor, its employees or associates have:

> *[ . . . ] been convicted by a final judgment of any offence concerning its professional conduct, such as, for example, infringement of existing legislation on the export of defence and/or security equipment [or] criminal acts of participation in a criminal organisation, corruption, fraud, money laundering, financing of terrorism or terrorist activities [or] been guilty of grave professional misconduct, such as, for example, a breach of obligations regarding security of information or security of supply during a previous contract.*

The contractor may see his or her current and future offers rejected by the Ministry of Defence or its underlying agencies, should he or she fail to comply with the information duties imposed by the statement.

**Licensing requirements**

37 | What registration or licensing requirements exist to operate in the defence and security sector in the jurisdiction?

The Directorate for Civil Protection and Emergency Planning requires contractors operating within Norway to adhere to the regulations concerning the production, storage and transport of materiel of a chemical, biological, explosive or otherwise dangerous nature. In that regard, the Directorate may perform inspections and require prior notification, certificates and permissions.

Regulation No. 718 of 19 June 2013 on the Export of Defence-related Products, Dual-use Items, Technology and Services governs the possibility for Norwegian companies to acquire certification to receive defence-related goods from other EEA countries operating under a general transfer licence. Such goods may include materiel used for production.

The certification is subject to a case-by-case review where, among other things, the department factors in the company's reliability and defence-related experience.

**Environmental legislation**

38 | What environmental statutes or regulations must contractors comply with?

Contractors that are transporting or storing deliverables or operating within Norway must comply with the environmental rules in Act No. 6 of 13 March 1981 Concerning Protection against Pollution and Concerning Waste, as well as any requirements imposed in the contract with the procuring authority.

39 | Must companies meet environmental targets? What are these initiatives and what agency determines compliance?

The procuring authority may impose environmental targets on contractors through the inclusion of environmental requirements in both contracts and framework agreements (see FOSA sections 8-3 and 8-16). If the procuring authority requires documentation that shows the contractors are adhering to certain environmental standards, the procuring authority should refer to the Eco-Management and Audit Scheme or other European or international standards.

40 | Do 'green' solutions have an advantage in procurements?

Green solutions do not have an outright advantage in procurements as such, but may have an advantage in the sense that the procuring authority is obliged to consider the life-cycle costs and environmental consequences of the procurement when it designs the requirements of the deliverable. As such, environmentally conscious contractors may be better able to meet these requirements depending on the desired deliverable in question.

If possible, the procuring authority should require the contractor to meet certain environmental criteria concerning the deliverable's performance or function. Additionally, the procuring authority may give green solutions an advantage in accordance with the applicable rules and regulations.

## UPDATE AND TRENDS

**Key developments of the past year**

41 | What were the key cases, decisions, judgments and policy and legislative developments of the past year?

There is a minor case decided by the Public Procurement Complaints Board regarding the procurement of vehicles for the Home Guard under Regulation No. 1185 of 4 October 2013 on Defence and Security Procurement (FOSA). The issue was whether the Norwegian Defence Materiel Agency had changed the interpretation of award criteria. After an assessment of the facts, the Board found that was not the case (KOFA–2018–362).

More importantly, the future structure of the armed forces was discussed by Norway's parliament in 2020. The government proposed a resolution on the acquisition of new main battle tanks for the Army during 2021, as well as the acquisition of new helicopters for the special forces by 2024.

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**Coronavirus**

42 | What emergency legislation, relief programmes and other initiatives specific to your practice area has your state implemented to address the pandemic? Have any existing government programmes, laws or regulations been amended to address these concerns? What best practices are advisable for clients?

The government has announced several initiatives regarding postponement of tax payments, general support for profitable companies before the pandemic which now have problems with liquidity, as well as support for specific sectors. However, none of these are relevant to the defence industry as such.

The government has periodically restricted the possibility of entering the country, imposing a 10 day quarantine period for entering personnel. This may create problems for maintenance and/or delivery contracts that require foreign personnel to be on-site in Norway and should be checked in advance. Such restrictions do not constitute force majeure events under Norwegian contract law and the parties need to make specific agreements as to which contractual consequences any quarantine issues may have.

# Poland

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## LEGAL FRAMEWORK

### Relevant legislation

1 What statutes or regulations govern procurement of defence and security articles?

Up until 2020, the procurement of defence and security articles in Poland was governed in principle by the Act of 29 January 2004 Public Procurement Law (PPL), which implements the EU Defence and Security Directive (2009/81/EC) into Polish law, and, in particular, Chapter 4a of the PPL. However, from 1 January 2021, the Act of 11 September 2019 Public Procurement Law (New PPL) will enter into force. The New PPL is an entirely new act with a different structure and terms aimed at improving the effectiveness and transparency of procurement procedures. Please note that further answers to the questionnaire will be based on the provisions of New PPL.

In the case of the procurement of arms, munitions or war materiel referred to in article 346 of the Treaty on the Functioning of the European Union (TFEU), if the essential interests of national security so require, the New PPL does not apply. Instead, the Decision of the Minister of National Defence No. 367/MON of 14 September 2015 shall be used. This decision regulates the principles and procedures of awarding contracts to which the provisions of the New PPL do not apply. The decision is supplemented by a number of additional regulations on planning, preparation, justification and approval procedures of defence procurement to which the Decision No. 367/MON applies.

The use of the said exemption from the New PPL rules may require the application of the Act on Certain Agreements Concluded in Connection with Contracts Essential for National Security of 26 June 2014 (the Offset Act). The Act sets out the rules for concluding agreements in connection with the performance of contracts related to the production of trade in arms, munitions and war materiel, commonly called offset contracts.

The public procurement rules do not apply to the procurement of defence and security articles in the situations described in article 13 of the New PPL, being:

- where the procurement is subject to a special procedure under an international agreement;
- in cases of government-to-government procurement if Poland is one party of a procurement; and
- in the event of contracts provided for intelligence or counter-intelligence activities.

General principles derived from the TFEU also apply to such procurements, including the principles of equal treatment, non-discrimination, transparency, proportionality and mutual recognition.

### Identification

2 How are defence and security procurements identified as such and are they treated differently from civil procurements?

A procurement by a Polish contracting authority falls within the scope of the New PPL when the contract has a value equal to or greater than EU financial thresholds for goods and services and for works (from 1 January 2020 for goods and services €428,000 and for works €5,350,000), and if the procurement covers:

- the supply of military equipment, including any parts, components, subassemblies or software thereof;
- the supply of sensitive equipment, including any parts, components, subassemblies or software thereof;
- works, supplies and services directly related to the security of the facilities at the disposal of entities performing contracts in the fields of defence and security, or related to the equipment referred above and any and all parts, components, and subassemblies of the life cycle of that product or service; and
- works and services for specifically military purposes or sensitive works and sensitive services.

Please note that the New PPL raised the threshold for works – from €30,000 to €5,350,000 – above which the contracting authority is obliged to apply the New PPL.

The procurement will be advertised in the Official Journal of the European Union (OJEU).

The key differences between procurements carried out under the specific defence rules (in comparison to civil procurement) are:

- the mechanisms put in place to protect sensitive information and to ensure defence and security interests are protected (eg, restriction of the range of contractors authorised to obtain classified information);
- a broader catalogue of the circumstances justifying the exclusion of economic operators from the procurement procedure;
- the power of the contracting authority to restrict the involvement of subcontractors in certain situations;
- the limitation of the number of contract award procedures which may be applied (this only applies to procedures for awarding contracts in which an initial qualification of contractors is possible (eg, restricted tender or negotiated procedure with prior publication));
- a wider range of tender assessment criteria (other than standard criteria such as viability, security of supply, interoperability, and operational characteristics indicated in terms of reference);
- additional rights for the contracting authority to reject an offer or cancel the procedure; and
- differences in the content of contract notices or terms of reference.

Decision 367/MON (applicable if the application of the provisions of the New PPL is excluded because of the existence of a fundamental security interest state) imposes more stringent requirements regarding procurement. It limits the scope of procurement procedures to just three:

- negotiations with one supplier;
- negotiations with several suppliers;
- exceptionally negotiated procedure with prior publication.

In addition, the Decision does not provide the mechanism for appealing the decisions of the contracting entity to the National Appeals Chamber. This Chamber can only consider procurement disputes regulated by the New PPL. In the case of procurement under the Decision 367/MON, contractors can only file claims in civil courts.

**Conduct**

3 | How are defence and security procurements typically conducted?

The procurement of standard defence and security products is usually conducted as public procurement regulated by the New PPL. The strategic procurement, or any other procurement that is related with protecting the essential security interests of the state, is typically conducted on the basis of Decision 367/MON or a government-to-government arrangement (eg, contracting with the US government based on a foreign military sales programme).

Under the New PPL there are two procedures available for all defence and security procurements:

- restricted procedure; or
- negotiated procedure with the publication of a contract notice.

In addition, there are four more procedures that may be applied in certain cases:

- competitive dialogue;
- negotiated procedure without the publication of a contract notice;
- single-source procurement; or
- electronic auction.

Most procurement procedures involve a pre-qualification process, as part of which bidders must demonstrate their financial stability and technical capability, including experience in similar contracts. The way that the procurement proceeds depends on whether the authority has chosen a procedure that permits them to negotiate the contract and requirements with the bidders.

The negotiations phase is usually limited, with many of the contract terms being identified as non-negotiable. The evaluation process is undertaken on the basis of transparent award criteria, which are provided to bidders in advance in the tender documents. Once the winning bidder is selected, there is relatively little scope for further negotiation.

Decision 367/MON provides that the procurement procedure may be performed in the model of negotiations with one or several suppliers and, in exceptional cases, if it is not possible to define a closed catalogue of potential contractors, in a negotiated procedure with prior publication.

**Proposed changes**

4 | Are there significant proposals pending to change the defence and security procurement process?

The current PPL will be in force until the end of 2020 and on 1 January 2021, it will be replaced by the New PPL.

The PPL currently in force has been amended dozens of times during recent years and several of these amendments have been very extensive. The result of this is that it has now been deemed to be too complicated for an average contractor, hence the rewritten PPL.

The major changes in the New PPL include:

- solutions introducing better tender procedure preparation;
- a new principle of public procurement law – the principle of efficiency;
- introduction of procedural simplifications, in particular for contracts below the EU thresholds;
- better balance between the position of contracting authorities and contractors;
- greater transparency of tender procedures;
- introduction of an out-of-court dispute resolution mechanism; and
- changes to public procurement agreements, including regulation of the valorisation of contracts.

The above changes will have an impact on all procurement procedures, including defence procurement.

**Information technology**

5 | Are there different or additional procurement rules for information technology versus non-IT goods and services?

There are no specific or additional rules that relate to IT procurement.

**Relevant treaties**

6 | Are most defence and security procurements conducted in accordance with the GPA or other treaty-based procurement rules, or does this jurisdiction commonly use the national security exemption to procure them?

The majority of defence and security procurements in Poland are conducted in accordance with the Agreement on Government Procurement, EU treaties or relevant EU directives. The number of contracts awarded based on the national security exemptions is limited, but the value of these contracts is usually substantial.

## DISPUTES AND RISK ALLOCATION

**Dispute resolution**

7 | How are disputes between the government and defence contractor resolved?

The Act of 11 September 2019 Public Procurement Law (New PPL) provides a legal remedies framework which may be used by the contractors who have, or who had, an interest in winning a contract or have suffered, or may suffer, damage due to the contracting entity's violation of the provisions of the New PPL. Disputes between the contracting authority and a contractor are resolved by the National Appeals Chamber (NAC) in Warsaw as a state entity (quasi-court) specialising in such disputes. Disputes are resolved very quickly – usually within 14 days of submitting an appeal and usually after 1 hearing.

Disputes are resolved by the NAC in accordance with the dispute procedure regulated mainly by the New PPL and partially by the Polish Civil Procedure Code. The ruling issued by the NAC may be appealed to the Regional Court in Warsaw, which acts as a public procurement court. The judgment of the Regional Court in Warsaw may be contested by way of a cassation appeal filed with the Supreme Court.

The NAC has the power to resolve disputes related to the procedure of awarding public contracts while other disputes regarding, for example, the public contract performance, are resolved by common courts.

In most of the procurement proceedings conducted on the basis of exemption from the New PPL (eg, where Decision of the Minister of National Defence No. 367/MON of 14 September 2015 applies), the disputes are resolved by the common state courts. In practice, it means that the dispute may last a very long time and may be completed many

months after the contract was awarded to a competitor. This is a significant difference in comparison to procurement based on the New PPL.

8 To what extent is alternative dispute resolution used to resolve conflicts? What is typical for this jurisdiction?

The New PPL introduces entirely new provisions concerning formal alternative dispute resolution used to resolve conflicts between a contracting authority and a contractor. This regulation is considered by the legislator as necessary to regulate at the statutory level due to the lack of settlements in public procurement matters in practice.

The mediation (or another amicable dispute resolution method) is started with each party submitting a request for mediation with the Court of Arbitration at the General Counsel to the Republic of Poland, a selected mediator, or the person affecting another amicable dispute resolution method.

It should be noted that mediation is mandatory in certain cases. If the estimated value of the contract is determined as equal to or greater than the zloty equivalent of €10,000,000 for supplies or services and of €20,000,000 for works, and the value of the subject of the dispute exceeds 100,000 zloty, the court will refer the parties to mediation or another amicable dispute resolution method at the Court of Arbitration at the General Counsel to the Republic of Poland, unless the parties have already indicated a choice of mediator or other person affecting another amicable dispute resolution method.

The legislation indicates that, as a rule, mediation should be conducted by the Court of Arbitration. The mediations conducted by this court will be resolved on the basis of the rules of this Court of Arbitration.

**Indemnification**

9 What limits exist on the government's ability to indemnify the contractor in this jurisdiction and must the contractor indemnify the government in a defence procurement?

There are no specific rules governing liability under a defence procurement contract.

During the contract performance phase, the contractual liability of the parties is governed by the contract and the general rules of Polish civil law. The New PPL does not modify these principles, except on cooperation with subcontractors in construction works contracts.

There are no statutory or legal obligations on a contractor to indemnify the government, although contractual indemnities may result from negotiation (subject to a negotiated procedure being undertaken).

The New PPL does not regulate the liability of the awarding entity for breach of law during the award procedure. It only provides that in the event of cancellation of the procurement procedure for reasons attributable to the contracting authority, contractors who have submitted valid tenders shall be entitled to claim reimbursement of the reasonable costs of participating in the procedure, in particular the costs of preparing the tender.

**Limits on liability**

10 Can the government agree to limit the contractor's liability under the contract? Are there limits to the contractor's potential recovery against the government for breach?

The contracting authority can agree to limit the contractor's liability under the contract. However, the usual policy of awarding entities is to not accept a limit unless it is reasonable or is common market practice. It is common practice in Poland that a contracting entity's liability towards contractors is limited to the amount of the contract value.

The contract award procedure used by the contracting authority will determine the extent to which the limitation of liability is negotiable.

However, the New PPL introduces a list of prohibited contractual provisions on the basis of which certain kinds of contractor liability are excluded. The proposed provisions that a contract may not envisage are:

- contractor's liability for delay, unless it is justified by the circumstances or the scope of procurement;
- the imposition of contractual penalties on the contractor that are not directly or indirectly linked to the subject of the contract or proper performance thereof; and
- the contractor's liability for the circumstances for which the sole liability rests with the contracting authority.

Public contracts usually include provisions on the payment of liquidated damages. According to the civil code, the result of introducing such a clause is the elimination of further liability by the payment of an amount stipulated in advance in a contract. However, the public contract usually explicitly outlines the possibility of claiming damages for the amount exceeding the amount of the contractually stipulated liquidated damages.

**Risk of non-payment**

11 Is there risk of non-payment when the government enters into a contract but does not ensure there are adequate funds to meet the contractual obligations?

In theory, there is a risk of non-payment, as with all customers. However, according to the Act on Public Finances, the awarding entities can only undertake obligations that are within its budget. Therefore, in practice, the practical risk of non-payment for an undisputed, valid invoice by the awarding entity is very low. Additionally, major defence procurements are conducted in line with the Polish Armed Forces development programmes. These programmes are financed from a special Armed Forces modernisation fund or a state budget. Currently, purchases of equipment by the Ministry of Defence for defence needs is carried out on the basis of the updated Plan for Technical Modernisation of the Polish Armed Forces for the years 2021–2035. Under this Plan, the ministry is entitled to conclude multi-year contracts with flexible budgets. The ministry assumes that 524 billion zloty will be spent over 2021 to 2035.

**Parent guarantee**

12 Under what circumstances must a contractor provide a parent guarantee?

The contracting authority should specify in its initial tender documentation its requirements concerning the guarantees to be provided by the contractor. Under the New PPL, there is no obligation to provide a parent guarantee. The contracting entity may require a security of performance of the contract. This is customary for large contracts. The procurement regulations contain a list of forms in which security of performance of the contract should be provided. These include, primarily, bank guarantees and insurance guarantees (performance bonds).

The submission of a performance bond is only mandatory in offset agreements.

## DEFENCE PROCUREMENT LAW FUNDAMENTALS

**Mandatory procurement clauses**

13 Are there mandatory procurement clauses that must be included in a defence procurement contract or that will be read into the contract regardless of their actual inclusion?

There are mandatory clauses that must be included in a defence procurement contract on the basis of the Act of 29 January 2004 Public Procurement Law (PPL). Moreover, the Act of 11 September 2019 Public

Procurement Law (New PPL) extends the list of obligatory clauses which should be introduced to the contract (eg, indexation clause in the event of changes in the prices of materials or costs linked to the performance of the contract if the works contract or the service contract was concluded for a period longer than 12 months).

There are also numerous provisions of the Polish Civil Code and other legal acts that will apply regardless of their inclusion in a defence procurement contract. The most important are mandatory provisions that cannot be modified by the parties in a contract (eg, the scope of the public contract, termination and duration). Other provisions (non-mandatory) stem from, mainly, the Polish Civil Code (regarding payments, liability, warranty etc) and will be applicable unless otherwise agreed by the parties.

**Cost allocation**

14 | How are costs allocated between the contractor and government within a contract?

There is no allocation of costs in public contracts. The consideration due to the contractor is indicated in a contract, usually as a fixed price for all contractual consideration. All costs incurred or estimated by the contractor plus an agreed profit rate would need to be included in the price. The only exception is indexation clause introduced pursuant to New PPL. On the basis of this clause, a contracting authority is obliged to modify remuneration in the event of changes in the prices of materials or costs linked to the performance of the contract, if the works or service contract was concluded for a period of longer than 12 months.

**Disclosures**

15 | What disclosures must the contractor make regarding its cost and pricing?

The contractor may be required to disclose the cost and pricing information in the case of complex procurements (typically in the form of a spreadsheet indicating the elements of the price and their calculation).

Additionally, in case there is concern that the offered price is abnormally low or doubts are raised by the contracting authority as to the possibility of performing the subject of the contract in accordance with the requirements, the awarding entity has a right to require more detailed information regarding cost and pricing. In the case of works contracts or service contracts, the contracting authority is obliged to request such explanations regarding abnormally low prices.

**Audits**

16 | How are audits of defence and security procurements conducted in this jurisdiction?

Audits of defence and security procurements are conducted by:

- the Armament Inspectorate – the Inspectorate regularly conducts audits by internal audit and control units;
- the Supreme Audit Office – temporarily, from the perspective of general compliance with the law and in particular with the Act on Public Finances; and
- the Ministry of Defence's Office of Anticorruption Procedures and the Public Procurement Office, during the stage of procurement proceedings.

If the procurement is financed from EU funds there might be additional audit undertaken related to the spending of EU funds.

**IP rights**

17 | Who gets the ownership rights to intellectual property created during performance of the contract? What licences are typically given and how?

In the description of the subject of a contract, the contracting authority may provide for the necessity of transferring intellectual property rights or granting a licence.

The usual policy on the ownership of IP arising under public contracts is that IP that was created before the signing of the contract will normally vest with the contractor generating the IP, in exchange for which the awarding entity will expect to have the right to disclose and use the IP for the contracting authorities' purposes (licence). However, the awarding entities will expect that any IP that has been created by the contractor exclusively for the awarding entity in/during performance of the contract to be transferred to the awarding entity.

**Economic zones**

18 | Are there economic zones or other special programmes in this jurisdiction commonly utilised by foreign defence and security contractors for financial or other procurement related benefits?

There are no economic zones or programmes dedicated exclusively to defence contractors in Poland. In general, economic zones or similar special programmes exist in Poland for the benefit of entrepreneurs. Defence contractors may not only benefit from undertaking economic activity in economic zones, but also in areas where there are a lot of companies active in specific sectors; sometimes they are grouped in clusters, such as the Aviation Valley Association in south Poland.

**Forming legal entities**

19 | Describe the process for forming legal entities, including joint ventures, in this jurisdiction.

There are various types of legal entities that may be formed in Poland, including limited liability companies, general partnerships, limited liability partnerships, limited partnerships, limited joint stock partnerships, and joint stock companies. Business activities may also be conducted in the form of individual business activity, a civil partnership (under a contract) or by a branch office of a foreign company.

**Joint ventures**

Joint ventures can be corporate or commercial.

A corporate joint venture would involve the joint venture's parties setting up a new legal entity (likely, a limited liability company registered in Poland), which would be an independent legal entity able to contract in its own right where the joint venture parties are the shareholders. It is relatively straightforward and inexpensive to establish a company (the required share capital for a limited liability company is 5,000 zloty).

The parties must file a motion together with respective attachments (eg, articles of association and so on) at registry court and pay the applicable filing fee. The company will gain its legal personality upon its registration in the National Court Register. The joint venture's parties would also likely agree in a shareholders' agreement the roles and responsibilities of each shareholder and their respective obligations to invest capital and resources into the company.

A commercial joint venture does not involve any separate legal entity, and the parties contractually agree each party's roles and responsibilities based on various types of agreements such as cooperation agreements, consortium agreements and agreements on a common understanding.

In public procurement, the most popular type of joint venture is a commercial consortium based on a consortium agreement.

**Access to government records**

20 | Are there statutes or regulations enabling access to copies of government records? How does it work? Can one obtain versions of previous contracts?

Under the Access to Public Information Act 2001, there is a general right for the public to access information held by public bodies. As the Ministry of Defence is a public body, on the face of it this right would extend to contracts and records held by the ministry, allowing anyone to request documents related to both the procurement and the contract performance phase.

The New PPL also provides the possibility to access to the procedure record and its annexes. This record is public and made available upon request. Annexes to the procedure record (such as tenders) are available after the selection of the most advantageous tender or cancellation of the procedure.

However, Polish law indicates a few exemptions from disclosure of information related to the contract award procedure which covers primarily classified information at the levels of restricted, confidential, secret and top secret, and information that is regarded as a business secret of the contractor. In such cases, a contractor is entitled to request information of a technical, technological, organisational or other nature, which is of economic value, not be disclosed by that contracting entity.

The proceedings conducted under Decision 367/MON, which are aimed at securing the essential security interests of the state, are commonly set at the 'restricted' level. Therefore, public access to documents under these proceedings is limited.

**Supply chain management**

21 | What are the rules regarding eligible suppliers and supply chain management and anti-counterfeit parts for defence and security procurements?

Subject to limited exceptions, the New PPL obliges an authority to reject tenders from bidders who have been convicted of certain serious offences. They also give the contracting authority discretion to exclude bidders on other grounds, such as insolvency or gross professional misconduct. The rules expressly permit contracting authorities to consider the same exclusion grounds for sub-contractors, as well as giving them broad rights, for example, to require a supplier to disclose all sub-contracts or to flow down obligations regarding information security. In case of a procurement based on Decision of the Minister of National Defence No. 367/MON of 14 September 2015, the awarding entity may also limit the use of subcontractors or may require specific conditions to be met by subcontractors.

Under the New PPL, contracts for defence and security may be applied for by operators established in one of the member states of the European Union or the European Economic Area, or a state with which the European Union or the Republic of Poland has entered into an international agreement concerning these contracts. The contracting authority may specify in the contract notice that a contract for defence and security may also be applied for by economic operators from states other than those listed above.

In defence and security procurements, the contracting entities may influence the management of the supply chain of the contractor. Despite general permission for contractors to use subcontractors under the PPL, the contracting entity has the right to:

- limit the scope of the contract which may be subcontracted;
- request the contractor to specify in his or her offer which part or parts of the contract it intends to subcontract to fulfil the subcontracting requirement;
- request the contractor to subcontract a share of the contract in a non-discriminatory manner; or
- to refuse to consent to a subcontract with a third party if that party does not comply with the conditions for participation or if there are grounds for exclusion.

## INTERNATIONAL TRADE RULES

**Export controls**

22 | What export controls limit international trade in defence and security articles? Who administers them?

The Polish legislation implements EU regulations regarding export controls such as Council Regulation No. 428/2009 of 5 May 2009. The strategic goods (including dual-use items) captured by the regulation are known as 'controlled goods' as trading in them is permitted if, where appropriate, authorisation is obtained.

On the basis of Act of 29 November 2000 on International Trade in Goods, Technologies and Services of Strategic Importance for National Security and for the Maintenance of International Peace and Security, entrepreneurs are obliged to obtain a permit for the export of goods of strategic importance.

The EU has adopted the Council Common Position 2008/944/CFSP defining common rules governing the control of exports of military technology and equipment (the Common Position) and an accompanying list of military equipment covered by such a Common Position (the Common Military List) in the EU. The Common Position and Common Military List have been implemented by Poland into its own national legislation.

**Domestic preferences**

23 | What domestic preferences are applied to defence and security procurements? Can a foreign contractor bid on a procurement directly?

If the Act of 11 September 2019 Public Procurement Law (New PPL) applies, there is no scope for domestic preferences. Foreign contractors can bid on procurement directly without any local partner or without any local presence.

However, where article 346 of Treaty on the Functioning of the European Union (TFEU) is relied upon in order to exclude the application of the New PPL, defence procurement proceedings are conducted according to Decision 367/MON. The contracting entity may then request that the prime contractor be a domestic company if it can be demonstrated that the essential security interests of the state justify it. Furthermore, on the basis of Decision 367/MON the contracting entity may demand from the foreign contractor additional obligations such as offset obligations or the establishment of production or maintenance capacity in Poland.

The result is that domestic contractors may be given a more favourable position in comparison with foreign contractors.

**Favourable treatment**

24 | Are certain treaty partners treated more favourably?

Only member states of the European Union and signatories of the Agreement on Government Procurement or a free-trade agreement with Poland are able to benefit from the full protection of the New PPL. Contractors from other countries may be less favourably treated, including facing total exclusion from bidding in procurement proceedings.

**Sanctions**

25 | Are there any boycotts, embargoes or other trade sanctions between this jurisdiction and others?

Poland complies with all EU-implemented embargoes and (financial) sanctions that are imposed by the United Nations or the EU. All of these embargoes and sanctions are implemented through EU regulations, which have direct legal effect in each member state. Poland complies also with the economic and trade sanctions imposed by organisations such as the Organization for Security and Cooperation in Europe and the North Atlantic Treaty Organization.

**Trade offsets**

26 | Are defence trade offsets part of this country's defence and security procurement regime? How are they administered?

Defence trade offsets are part of Poland's defence and security procurement regime. However, the use of offsets is limited to specific cases. They may be required only if both the procurement itself and the related offset are justified by the existence of an essential security interest of the state. Offset requirements apply only to foreign contractors so they can be used as a form of domestic preferential treatment.

The Offset Act is the governing regulation regarding offset agreements and was harmonised with the EU approach to offsets. The requirement for an offset can be justified on the basis of article 346 TFEU, if it is necessary for the protection of the essential security interests of the state.

Offsets are not performed in public procurement proceedings under the New PPL. They are admissible only in proceedings governed by Decision 367/MON or in other procurements that are exempted from the New PPL (eg, G2G agreements). Offsets are negotiated by the Ministry of Defence. Signing an offset contract occurs after a procedure that consists of supplying the contractor with offset assumptions drafted by the ministry and a submission by the foreign contractor of an offset offer that responds to the assumptions.

## ETHICS AND ANTI-CORRUPTION

**Private sector appointments**

27 | When and how may former government employees take up appointments in the private sector and vice versa?

The employment of former government employees in the private sector and vice versa is subject to restrictions stipulated in:

- the Act of 11 September 2019 Public Procurement Law (New PPL)
- the decision of the Minister of National Defence No. 367/MON of 14 September 2015;
- the Act of 21 August 1997 regarding Limitation of Conducting Business by Persons Exercising Public Functions; and
- the Act of 11 September 2003 on Professional Military Service.

Both the New PPL as well as Decision 367/MON state that an economic operator that was involved in the preparation of a given contract award procedure, or whose employee was involved in the preparation of such a procedure, must be excluded from such a proceeding. Under the New PPL, the exclusion is not mandatory if the distortion of competition caused can be remedied by another method than excluding the operator from participating in a procedure.

According to the Act regarding Limitation of Conducting Business by Persons Exercising Public Functions, governmental employees specified in this Act may not be employed or perform other activities for an entrepreneur within one year from the date of cessation of their position or function, if they participated in the issuance of a decision in individual cases concerning that entrepreneur.

Under the Professional Military Service Act, members of Poland's armed forces cannot be employed nor undertake employment on the basis of another title in businesses conducting activity in the production or trade of defence goods if, during three years prior to the date of his or her dismissal from professional military service, he or she participated in a procurement procedure concerning products, supplies, works and services, or took part in the performance of a contract, related to such business.

**Addressing corruption**

28 | How is domestic and foreign corruption addressed and what requirements are placed on contractors?

Polish law criminalises domestic and foreign corruption practices. Moreover, the New PPL provides for sanctions for contractors who (or whose management or supervisory board members) have been sentenced for corruption by a final judgment. Such contractors must be excluded from the procurement proceedings.

Also, on the basis of Decision 367/MON at the stage of a contract's signing, the contractor is obliged to sign a clause under which the contractor will pay liquidated damages in the amount of 5 per cent of the gross value of the contract in the event of corruption within the procurement involving the contractor or its representatives.

**Lobbyists**

29 | What are the registration requirements for lobbyists or commercial agents?

The Lobbying Act 2005 requires that anyone active in the business of lobbying should be registered with the register of entities conducting lobbying activities held by the minister relevant for administrative affairs.

The rules of professional lobbying activity in the Sejm and Senate are set out in the Sejm's and Senate's regulations. Persons performing intermediation services in executing contracts concerning military equipment need to possess the relevant licence in accordance with the Act of 13 July 2019 on Conducting the Business of Manufacture and Sale of Explosives, Weapons, Ammunition and Technology for the Military or Police.

**Limitations on agents**

30 | Are there limitations on the use of agents or representatives that earn a commission on the transaction?

Polish law does not provide for such limitations.

## AVIATION

**Conversion of aircraft**

31 | How are aircraft converted from military to civil use, and vice versa?

Civil aircraft may not fly in Europe unless they comply with the airworthiness regime established pursuant to Regulation (EC) 2018/1139 or, if they fall within Annex I of the Regulation, are approved by individual member states.

Regulation 2018/1139 requires a type of certification process in accordance with certification specifications promulgated by the European Aviation Safety Agency (EASA). Annex I permits EU member states to approve ex-military aircraft, unless EASA has adopted a design standard for the type in question. Moreover, there are separate registers for military and civil aircraft at the national level of

legislation. The implementation of the registers of civil aircraft tasks results from the Aviation Law 2002 and the Regulation of the Minister of Transport, Construction and Maritime Economy of 6 June 2013 on the register of civil aircraft and signs and inscriptions on aircraft entered in that register.

The register for military aircraft is maintained by the Ministry of Defence and is mainly based on the regulation adopted in Order No. 3/MON of the Ministry of Defence dated 11 February 2004 on the keeping of a register of military aircraft. The order contains provisions that suggest that an aircraft cannot be included in both registers at the same time. For example, to include an aircraft in the military register, the application should be accompanied by a certificate of removal from a foreign aircraft register where the previous user was not from the Armed Forces. Until a military aircraft is removed from the military register, it cannot be entered into another aircraft register.

**Drones**

32 | What restrictions are there on manufacture and trade of unmanned aircraft systems or drones?

The manufacturing and trade of unmanned aircraft systems (UAS) or drones for the military purposes requires a licence issued in accordance with the Act of 13 June 2019 on conducting business activity within the scope of manufacturing and trade in explosives, weapons, ammunition and products and technology for military or police purposes.

The manufacturing and trade of UAS or drones for other purposes is currently in the process of harmonising the EU regulations. On 11 June 2019, two EU regulations on drones were published to harmonise the law in the EU in this field: the Commission Delegated Regulation (EU) 2019/945 of 12 March 2019 and Commission Implementing Regulation (EU) 2019/947 of 24 May 2019.

From 31 December 2020, the registration of drone operators, who use equipment equal to or greater than 250 grams, or less than 250 grams if the drone is equipped with a sensor capable of collecting data, will be mandatory. On the basis of these new regulations, drone manufacturing and trading will be subject to a number of exploitation requirements and will require qualification within one of the categories proposed by the EU.

## MISCELLANEOUS

**Employment law**

33 | Which domestic labour and employment rules apply to foreign defence contractors?

There are no specific statutory employment rules that apply exclusively to foreign defence contractors. If the work is to be performed by a Polish worker or in Poland, the employment contract with the foreign contractor cannot be less favourable to the employee than the rules stipulated in Polish labour law. The choice of a foreign law may therefore, only result in the implementation of more favourable obligations (eg, longer holiday periods). Foreign contractors should also consider tax and insurance-related consequences in relation to the performance of work by employees in Poland.

**Defence contract rules**

34 | Are there any specific rules that contractors, foreign or domestic, are bound by in defence contracts?

The answers above provide the details of the laws, regulations and decisions applicable to the defence contracting authorities and contractors, most notably the New PPL, Decision 367/MON and the Act on Certain Agreements Concluded in Connection with Contracts Essential for National Security of 26 June 2014 (the Offset Act). Apart from that, there are other mandatory provisions of Polish law with respect to defence contracts provided by acts such as the Industrial Property Law dated 30 June 2000, the Act on Copyright and Related Rights of 4 February 1994 or other legislation governing supervision of military equipment or assessment of conformity of goods.

35 | Do contractors avail themselves of these rules when they perform work exclusively outside of the jurisdiction?

If a contractor provides goods, services or works to a Polish awarding entity, the regulations detailed above will apply generally to all activities of the contractor related to the performance of the contract. If the work is performed outside of Poland, Polish rules will apply only to the delivery of the results of these works to a Polish awarding entity unless the contract provides otherwise. A Polish awarding entity may, for instance, request the right to audit the production units of the contractor located abroad.

**Personal information**

36 | Must directors, officers or employees of the contractor provide personal information or certify that they fulfil any particular requirements to contract with a government entity?

Companies will be asked to provide information about their management and supervisory board members as part of the pre-qualification process, and will usually be required to provide the official certificates certifying that management and supervisory board members have not been convicted of certain offences. In addition, the name, place of residence and the information from the criminal records of these persons must be disclosed to the contracting authority. On the basis of this information, the contracting authority makes a decision concerning a contractor's potential exclusion.

**Licensing requirements**

37 | What registration or licensing requirements exist to operate in the defence and security sector in the jurisdiction?

The Act of 13 June 2019 on conducting business activity within the scope of manufacturing and trade in explosives, weapons, ammunition and products and technology for military or police purposes provides for specific licensing requirements to operate in the defence and security sector in Poland. These requirements relate to various areas of business activity. For example, one of the criteria is that two members of the management board of the company need to be citizens of Poland or an EU or European Economic Area member state. The licensing authority is the Minister of Internal Affairs.

In addition, a contractor may be obliged to meet additional procurement requirements such as obtaining a necessary licence to operate in the defence and security sector issued by the country of the contractor's residence. The contracting authority publishes specific conditions in the procurement documentation (typically in terms of reference). The defence contractor may be also required to meet other procurement conditions, such as military quality control systems.

**Environmental legislation**

38 | What environmental statutes or regulations must contractors comply with?

Contractors producing or supplying goods and services or importing them into Poland will face different environmental legislation depending on their operations, product or service. The most important act in this area is the Polish Environmental Law. Contractors could face regulations

encompassing, among other things, air emissions, water discharges, water pollution, noise and waste disposal, and face responsibility for electrical waste and electronic equipment and restrictions on hazardous substances in such equipment. Applicable requirements may also incorporate energy efficiency, carbon emissions and energy consumption.

In some circumstances, there are exemptions, derogations or exemptions from environmental legislation for defence and military operations. One of them is derogation in respect to military aircraft from Regulation (EC) No. 2018/1139 of 4 July 2018 on common rules in the field of civil aviation and establishing the European Union Aviation Safety Agency.

### 39 | Must companies meet environmental targets? What are these initiatives and what agency determines compliance?

The companies may need to meet environmental targets under respective environmental legislation. The contractors may be required to meet environmental targets if their activity has a negative impact on the environment. These requirements are the most important for manufacturers. However, in general, any activity that influences the environment may require relevant environmental permits. In Poland, the authorities conducting inspections and issuing permits are, in particular, the Ministry of Environment and local government administration bodies.

### 40 | Do 'green' solutions have an advantage in procurements?

The contracting authorities may include in the procurements 'environmental' parameters such as life-cycle costs of a product or non-price environmental criteria for the evaluation of tenders. If such a requirement is included in the terms of reference then the contractor offering products compatible with such requirement may obtain an advantage. The use of the environmental parameters is recommended by the government however it is not obligatory.

## UPDATE AND TRENDS

**Key developments of the past year**

### 41 | What were the key cases, decisions, judgments and policy and legislative developments of the past year?

2020 is referred to as the year of the pandemic. As a result, the Polish government was focused on the health crisis and limiting economic damages. The main goals of the Armaments Inspectorate were a modification of the timetables for the implementation of the contracts and awarding new contracts regarding national defence industry entities. In the course of 2020, the Ministry of Defence concluded agreements with Polish and foreign entities regarding the purchase of military equipment, such as the multi-purpose aircraft F–35A Lightning II and artillery command vehicles using KTO Rosomak chassis.

Meanwhile, both contracting authorities and contractors were preparing for the Act of 11 September 2019 Public Procurement Law (the New PPL) entering into force on 1 January 2021.

One of the most important documents in the fields of defence and security was the new Technical Modernisation Plan for the period 2021–2035, also covering the year 2020, signed by Ministry of Defence in 2019. The plan envisages modernisation expenditure will total 524 billion zloty. The most important programmes included in the plan are:

- Harpia – the acquisition of 32 fifth-generation multi-role combat aircraft;
- Narew – short-range air defence systems;
- Cyber.mil.pl – modern cryptographic and IT hardware, expenditure is to be contained in an amount of 3 billion zloty;
- Wisła – medium-range air defence systems;
- Gryf – tactical unmanned aerial vehicles;
- Ważka – micro unmanned aerial vehicles;
- Płomykówka – maritime patrol aircraft;
- Miecznik – coastal defence vessels;
- Orka – submarines;
- Regina – Krab howitzer squadron fire module elements;
- Rak – self-propelled mortars based on the Rosomak armoured personnel carrier;
- Homar – long-range rocket artillery;
- Pustelnik – light anti-tank guided missile launchers;
- Borsuk – infantry fighting vehicles; and
- Mustang - high-mobility passenger/cargo vehicles.

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**Coronavirus**

### 42 | What emergency legislation, relief programmes and other initiatives specific to your practice area has your state implemented to address the pandemic? Have any existing government programmes, laws or regulations been amended to address these concerns? What best practices are advisable for clients?

Numerous acts and regulations have been implemented during the pandemic. The most important acts issued to counteract the covid-19 virus are commonly called 'Anti-Crisis Shields'. The legislator adopted five Anti-Crisis Shields so far and will adopt another to support and regulate the activity of different branches of the economy. In the area of public procurement law, the most notable changes included:

- the obligation of parties to inform each other about the impact of covid-19 on the contract execution process;
- the obligation to amend public procurement contracts (in consultation with the contractor) in the event that circumstances around covid-19 affect the proper performance of that contract;
- a prohibition on deducting contractual penalties under certain circumstances;
- the obligation to pay remunerations in instalments or to make advance payments;
- a reduction to the limit of performance bonds to 5 per cent of the total price quoted in the offer (currently 10 per cent); and
- right to return the performance bond after completion of the part of the order.

Some of these changes applies also to the offset contract that has been signed and are in the execution stage.

# South Korea

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## LEGAL FRAMEWORK

### Relevant legislation

1 | What statutes or regulations govern procurement of defence and security articles?

The primary legislation governing defence and security procurement in Korea is the Defence Acquisition Program Act (DAP Act). The statute is further implemented by the Enforcement Decree and Enforcement Rules thereof. For matters not stipulated in the DAP Act, the Act on Contracts to Which the State is a Party (ACSP) generally applies along with the Enforcement Decree and Enforcement Rules thereof.

The Defence Acquisition Program Administration (DAPA), an executive agency of the Ministry of National Defence, has detailed administrative rules, such as the Defence Acquisition Program Management Regulation (DAPMR), Guidelines for Evaluation of Weapon System Proposals, and Offset Program Guidelines.

The Act on Development and Support of the Defence Industry and the Act on Promotion of Innovation of Science Technology for National Defence have been newly enacted as offshoots of the DAP Act. The former concerns the development of and support for the defence industry, while the latter concerns the development of science technology and acquisition of weapons systems for national defence.

### Identification

2 | How are defence and security procurements identified as such and are they treated differently from civil procurements?

Among the articles owned and controlled by the government and the Ministry of Defence, security procurement and civil procurement are distinguished by the identity of the procurer and the nature of the articles being procured. DAPA is the main procurer of defence and security articles. The army, navy or air force is each able to directly procure articles to a total value of up to 30 million won per year. By contrast, civil procurement (ie, procuring articles that are generally not used for defence nor security) is carried out by the Public Procurement Service.

The procurement of items classed as 'weapons systems' is exclusively conducted by DAPA. In addition, DAPA oversees the purchase of certain munitions necessary for operations, training and security, including the items closely related to weapons systems; the items procured in conjunction with equipment for efficient maintenance and management of the equipment; the items which are subject to special security considerations; and the items which have been imported from other countries, to name a few.

However, recent amendments in law have allowed the Public Procurement Service to participate in the procurement of certain defence and security articles. However, in order to enable DAPA to focus on defence force improvement projects, the Public Procurement Service is only in charge of purchasing munitions unrelated to weapons systems.

### Conduct

3 | How are defence and security procurements typically conducted?

Defence and security procurements consist of defence force improvement projects and military forces management projects. Procurements for the improvement of defence capacities are the most general procurement of defence and security articles.

Procurements for the improvement of defence capacities is carried out according to the following procedure:

- requests are submitted from each armed force;
- a decision of the joint chiefs of staff is made;
- prior research is carried out;
- a project strategy is established;
- alignment of the project strategy with the Mid-Term National Defence Plan, which is a five-year plan that specifies the annual projects and financing arrangements for implementing the overall defence policy and strategy;
- budgeting;
- a bidding announcement is made; and
- the contract is concluded.

### Proposed changes

4 | Are there significant proposals pending to change the defence and security procurement process?

The National Assembly is considering to make the following changes to the defence and security procurement process:

- redefining the scope of 'defence projects';
- converting the concept of 'offset program' to 'industrial cooperation' with a renewed focus on exports of defence and security articles;
- monitoring the employment of former public officials in the defence industry;
- authorising the chairman of the joint chiefs of staff to form testing and evaluation plans for weapons systems and technologies;
- requiring the minister in charge of DAPA to monitor the use of counterfeit and obsolete equipment;
- requiring, by statute, that suppliers and bidders submit cost estimates and imposing criminal sanctions for any misrepresentations or forgeries;
- changing the term 'munitions sales agency' (ie, a broker or an agent that acts on behalf of a foreign contractor) into 'defence program agency', and requiring a defence program agency to be registered;
- expanding the scope of application for integrity pledges;
- inserting agency provisions into the DAP Act;
- requiring DAPA to designate an agency to oversee the standardisation and management of munitions inventories;

- revoking a contract if the contractor is found to engage in the illegal acquisition, use or disclosure of technologies, or leaks or negligently discloses military secrets;
- expediting the procedure for approving exports of munitions;
- providing an end-user certificate to individuals who intend to import munitions for research and development;
- providing preferential treatment to articles made from domestically produced materials; and
- revoking the registration of a munitions sales agency that allows a third party to operate its business under the agency's own name or which transfers or lends its registration certificate to a third party.

**Information technology**

5 Are there different or additional procurement rules for information technology versus non-IT goods and services?

Generally, heightened security and interoperability are demanded when procuring IT goods and services. However, frequently the underlying software of IT equipment is inseparable from the hardware, which makes it difficult to treat them differently.

**Relevant treaties**

6 Are most defence and security procurements conducted in accordance with the GPA or other treaty-based procurement rules, or does this jurisdiction commonly use the national security exemption to procure them?

Korea is a party to the Government Procurement Agreement within the framework of the World Trade Organization. However, this agreement does not apply when significant national security interests are at stake in connection with defence procurements. As a general principle, defence and security articles manufactured domestically in Korea are preferred over those manufactured overseas. Only those articles that are not available domestically are purchased overseas.

Korea has entered into free trade agreements with Association of Southeast Asian Nations, Australia, Canada, Central America, Chile, China, Colombia, the European Free Trade Association, the European Union, India, New Zealand, Peru, Singapore, Turkey, the United States and Vietnam. There are procurement provisions in these agreements carving out national security exemptions.

## DISPUTES AND RISK ALLOCATION

**Dispute resolution**

7 How are disputes between the government and defence contractor resolved?

In principle, a dispute between the government and a defence contractor related to a bidding and procurement contract would be resolved by litigation.

In addition, where the value of the procurement exceeds a certain amount (ie, 3 billion won for a construction project, 150 million won for a commodity contract, and 150 million won for a service contract), parties may opt to use the appeal process under the Act on Contracts to Which the State is a Party (ACSP) or the mediation process provided by the State Contract Dispute Mediation Committee. With respect to penalties for delays, the Defence Acquisition Program Administration (DAPA) provides an internal examination procedure with the support of external experts. A defence contractor may directly file a lawsuit in court without having exhausted available alternative dispute resolution processes. However, in practice alternative dispute resolution processes are infrequently used.

If a contractor has engaged in unfair bidding, misstated costs or has breached their contract, the government may restrict the contractor's eligibility to participate in future biddings by way of an administrative appeal or administrative litigation.

8 To what extent is alternative dispute resolution used to resolve conflicts? What is typical for this jurisdiction?

The DAPA resolves disputes related to procurements of weapon systems through litigation or arbitration. In the case of domestic procurements, the parties generally resolve disputes through litigation. In the case of overseas procurements, it is common to resolve disputes through arbitration. However, in many cases disputes on international procurement do not often turn to alternative dispute resolution procedures; court litigation is the norm.

**Indemnification**

9 What limits exist on the government's ability to indemnify the contractor in this jurisdiction and must the contractor indemnify the government in a defence procurement?

There is no particular limitation on the scope of the government's liability toward a defence contractor. The ordinary rules of contractual breach determine the scope of the government's and contractor's liabilities, subject to any particular provisions on the calculation of damages.

**Limits on liability**

10 Can the government agree to limit the contractor's liability under the contract? Are there limits to the contractor's potential recovery against the government for breach?

As a general principle, government contracts must comply with all relevant laws and regulations, and contracting officers generally have very little discretion when executing the contracts.

However, certain enforcement decrees limit the extent of a contractor's liability or of their potential recoveries against the government.

For example, the Enforcement Decree of the Defence Acquisition Program Act prescribes that contracts relating to test products for research and development purposes or to the first mass production of weapon systems designated as 'defence material' must limit the amount of liquidated damages to 10 per cent of the contract price. The Enforcement Decree of the Act on Contracts to Which the State is a Party similarly prescribes that the liquidated damages in contracts subject to this legislation must not exceed 30 per cent of the contract price.

The DAPA's general terms and conditions for overseas procurements limit the maximum amount of a delay penalty to 10 per cent of the contract price.

**Risk of non-payment**

11 Is there risk of non-payment when the government enters into a contract but does not ensure there are adequate funds to meet the contractual obligations?

There is little risk that the Korean government will not meet its payment obligations under a procurement contract. The government is required to secure the full budget in advance, before engaging in the procurement of defence and security articles.

**Parent guarantee**

12 | Under what circumstances must a contractor provide a parent guarantee?

No parent guarantee is required. Instead, the contractor is directly required to pay a performance bond to cover the risk of possible damages. In overseas procurement, for example, the contractor is required to pay a performance bond equivalent to at least 10 per cent of the contract price within 30 days after opening a letter of credit. The performance bond must be paid in cash or by an irrevocable standby letter of credit.

## DEFENCE PROCUREMENT LAW FUNDAMENTALS

**Mandatory procurement clauses**

13 | Are there mandatory procurement clauses that must be included in a defence procurement contract or that will be read into the contract regardless of their actual inclusion?

The Defence Acquisition Program Administration (DAPA) prescribes the mandatory terms and conditions of procurement contracts.

One mandatory condition is the selection of the Korean law as the governing law for overseas procurements and conformity with the Act on Contracts to Which the State is a Party (ACSP). It is also important that DAPA or a contracting officer execute a procurement contract using the general terms and conditions and the contract form, as prescribed by the administrative rules in existence.

The procurement contract must also expressly stipulate the purpose, price, time period for performance, performance bond, risks and delay penalty.

**Cost allocation**

14 | How are costs allocated between the contractor and government within a contract?

While the allocation of costs is generally negotiable, the common practice is that the contractor bears the costs of execution. The DAPA's general terms and conditions stipulate that the contractor shall be responsible for:

- the administrative costs, bank charges and other related expenses (such as postal charges) incurred in performing its contractual obligations;
- the costs in obtaining government approval for exports; and
- delivery costs.

**Disclosures**

15 | What disclosures must the contractor make regarding its cost and pricing?

The contractor must make the following disclosures when bidding for a 'weapons system' procurement contract:

- the total price;
- sub-system prices;
- parts prices and cost factors;
- cost accounting standards and the exchange rate used to convert the contract price from US dollars to Korean won;
- detailed quotation prices for each component;
- proposed prices based on the work breakdown structure; and
- annual operation and maintenance costs.

**Audits**

16 | How are audits of defence and security procurements conducted in this jurisdiction?

In Korea, audits of defence and security procurements are conducted by the Board of Audit and Inspection. The Board audits DAPA and each armed force involved in a procurement. Where appropriate, the Board also engages administrative agencies to conduct daily audits known as 'prior consulting'.

The DAPA conducts audits of its own too. Its special inspector general for defence acquisition examines each stage of the procurement procedure. The DAPA's auditor's office or its ombudsman, established pursuant to the DAP Act, inspect allegations of misconduct or complaints related to the procurement of defence and security articles.

**IP rights**

17 | Who gets the ownership rights to intellectual property created during performance of the contract? What licences are typically given and how?

In a 'weapons system' procurement contract, the seller, in principle, retains the intellectual property rights in the same manner as in contracts for the purchase of general goods. However, the seller may choose to transfer technology to the government using a defence offset agreement. In such cases, the relevant technology, equipment and tools are transferred free of charge, and the government receives ownership or a license to use the technology, equipment and tools.

On the other hand, licensing agreements may be concluded with respect to IP rights. For example, the government may obtain a licence to use the technical data and software provided by the contractor within the scope of the purpose of the contract.

The Act on Promotion of Innovation of Science Technology for National Defence states that IP rights arising from national defence research and development projects conducted under contracts or agreements executed by the state with companies, universities and research institutes, etc may be shared between the state and the research and development institute, or other participating institutes, subject to such contracts or agreements, and that a licence may be granted to the relevant companies, universities or research institutes to state-owned IP rights. The act will be implemented on 1 April 2021.

**Economic zones**

18 | Are there economic zones or other special programmes in this jurisdiction commonly utilised by foreign defence and security contractors for financial or other procurement related benefits?

The Korean government provides free trade zones or free economic zones to foreign defence and security contractors. These zones grant tax cuts and financial support to foreign entities domiciled in them. However, only a few foreign contractors have moved into these zones to date.

**Forming legal entities**

19 | Describe the process for forming legal entities, including joint ventures, in this jurisdiction.

A company is formed in accordance with the mandatory procedures stipulated in the Korean commercial law. The procedure for establishing a company by a foreigner is generally identical to that used by a Korean citizen. Additional requirements for foreign nationals include submitting a foreign investment notification and registering the company as

a foreign-invested enterprise with the Ministry of Trade, Industry and Energy. This notification is also required for joint ventures between a foreign investor and a domestic investor.

A foreign national who intends to acquire shares or newly issued shares in a company that operates as a defence contractor must obtain permission in advance from the Minister of Trade, Industry and Energy. Violating this obligation is punishable by imprisonment of no more than one year or a fine not exceeding 10 million won.

**Access to government records**

20 | Are there statutes or regulations enabling access to copies of government records? How does it work? Can one obtain versions of previous contracts?

Public access to government records is permitted under the Public Records Management Act and the ACSP. The records are prepared, integrated, used and maintained by the DAPA, which records every defence procurement under progress from their beginning to end. Bidding announcements, progress and results are available for viewing on the Defence E-Procurement System website, although access to competitors' bids is not permitted.

**Supply chain management**

21 | What are the rules regarding eligible suppliers and supply chain management and anti-counterfeit parts for defence and security procurements?

Contractors participating in bidding must register as 'procurement contractors', in accordance with the Guidelines on Procurement Contractor Registration Information Management. The DAPA manages suppliers and supply chains using an integrated management system.

Brokers or agents acting on behalf of a foreign contractor must register as munitions sales agents, and report brokerage fees they receive from foreign companies to the DAPA, which enables the DAPA to effectively manage the supply chain.

To protect against counterfeit parts, the government works with the Korea Customs Service to verify original manufacturer's certification documents at every stage of delivery inspection. In the case of domestic procurements, an integrated test report management system is in place to prevent tampering with test reports. Contractors in domestic procurements are also required to check the authenticity of the test reports on products supplied by subcontractors.

## INTERNATIONAL TRADE RULES

**Export controls**

22 | What export controls limit international trade in defence and security articles? Who administers them?

The Defence Acquisition Program Administration (DAPA) is the agency responsible for administering the exporting of defence and security articles. All exporters must file a report with the DAPA and obtain approval for each export transaction.

DAPA is cooperating with private companies to establish the Defence Export Promotion Centre, which aims to increase exports of Korean defence and security articles.

**Domestic preferences**

23 | What domestic preferences are applied to defence and security procurements? Can a foreign contractor bid on a procurement directly?

Preference is given to defence and security articles manufactured in Korea. Procurement of foreign articles is pursued only when similar domestic articles are not available.

However, foreign contractors may enter bids for the procurement of certain defence articles with low relevance to national security.

**Favourable treatment**

24 | Are certain treaty partners treated more favourably?

In principle, the Korean government does not treat any country more favourably than others regarding the purchase of defence and security articles from foreign contractors.

**Sanctions**

25 | Are there any boycotts, embargoes or other trade sanctions between this jurisdiction and others?

In accordance with the United Nations Security Council resolutions, the Korean government does not engage in any defence-related transactions with North Korea. The Korean government has also banned exports of weapons to countries that are under arms embargoes, or countries designated as violating international peace and security.

Furthermore, the Minister of Trade, Industry and Energy has the discretion to prohibit exports or imports if there are justifiable reasons (eg, war, natural disaster) in Korea or in the partner country, or if the partner country refuses to recognise the rights and authority of Korea under international law.

**Trade offsets**

26 | Are defence trade offsets part of this country's defence and security procurement regime? How are they administered?

The Korean government promotes defence trade offsets when purchasing defence articles of more than US$10 million from overseas, in order to secure the technology necessary for defence improvement projects, logistics support capability for weapon systems that are to be procured, and the maintenance of the contracting partner's weapon systems. The Korean government may also conduct defence trade offsets for the purpose of participating in the development and production of weapon systems, or facilitating the export of domestic defence articles to foreign countries.

However, legislation is currently pending before the National Assembly that will replace offset programs with projects of 'industrial cooperation' for the purpose of promoting exports of Korea's defence and security articles.

## ETHICS AND ANTI-CORRUPTION

**Private sector appointments**

27 | When and how may former government employees take up appointments in the private sector and vice versa?

The Public Service Ethics Act prohibits government employees from working in the private sector under certain circumstances for three years following the termination of their public service.

The three-year prohibition applies to government officials of grade four or higher and to military officers of equivalent rank (that is a colonel in the army, air or marine forces, and captain in the navy) who

seek employment with a defence contractor or a commercial private company with annual sales exceeding 10 billion won and a capital scale exceeding 1 billion won. However, an exemption may be granted if there is sufficient 'screening' of the employee from the work performed under the government (including the Korean armed forces) during the five years prior to retirement and the work currently being performed.

In addition, after the three-year prohibition has lapsed, former government employees are prohibited from engaging in the same duties as they performed during their time in public office, and this rule applies equally to former military officers.

There are no specific regulations restricting a person in the private sector from taking a government appointment.

**Addressing corruption**

28 How is domestic and foreign corruption addressed and what requirements are placed on contractors?

Domestic and foreign corruption is addressed by the Criminal Code, the Act on the Aggravated Punishment of Specific Crimes, and the Act on the Aggravated Punishment of Specific Economic Crimes. These laws punish:

- a person abusing their position or authority or violating laws to benefit themselves or any third party in connection with their duties;
- the act of causing damage to public institutions by expropriating public funds, or in acquiring, managing or disposing of public property, or in concluding and performing a contract to which a public institution is a party, in violation of laws and regulations; and
- the act of forcing, recommending, suggesting or inducing the execution or concealment of any of the aforementioned acts.

Bribery to foreign officials is punished under the Act on Combating Bribery of Foreign Officials in International Business Transactions.

Furthermore, defence contractors, their subcontractors, and munitions sales agent (a Korean term for commercial agents working in the defence sector) are required to submit integrity pledges and to fully comply with them. If violated, they will be restricted from future bidding for up to five years.

In principle, bribery of domestic officials is punishable under the condition of reciprocity. However, the Improper Solicitation and Graft Act (commonly called the Kim Young-ran Act) punishes public officials who demand, accept or promise to accept anything valued at 1 million won (per single occasion) or 3 million won (per year) or more, regardless of whether it is connected with their duties.

**Lobbyists**

29 What are the registration requirements for lobbyists or commercial agents?

Except for lawyers, no one is allowed to lobby the government, public institutions or public officials on behalf of others for commercial purposes. There is no separate lobbyist registration system.

A commercial agent who works in the defence sector is defined as a 'munitions sales agent' in Korea. A munitions sales agent must be registered with the Defence Acquisition Program Administration (DAPA) in advance by submitting his or her:

- resumes of the representative and officers;
- employment information such as numbers and names of employees; and
- integrity pledge.

Acting as a munitions sales agent without being registered is illegal. Any person who violates this rule is punished by imprisonment of maximum 1 year and/or fines of up to 10 million won. A munitions sales agent who has been sentenced to imprisonment may not register as an agent for five years following the completion of his or her sentence. Similarly, an agent whose registration of a munitions sales agency business is cancelled by the minister of DAPA may not register again for two years.

**Limitations on agents**

30 Are there limitations on the use of agents or representatives that earn a commission on the transaction?

As a general rule, a foreign contractor involved in a procurement exceeding US$2 million is required to deal directly with DAPA, rather than through a munitions sales agent. However, if the DAPA determines that the foreign company requires the use of a munitions sales agent, then submission of the application via the munitions sales agent is permitted.

As discussed above, a munitions sales agent must register with the DAPA in advance.

## AVIATION

**Conversion of aircraft**

31 How are aircraft converted from military to civil use, and vice versa?

For the purposes of research and development, civilian to military mutual technology transfers, technical cooperation and standardisation of specifications, the Korean government encourages the spin-on, spin-off and the dual use of civilian and military aircraft technology. The government may give preference to the purchasing of defence articles developed by civilian-military technical cooperation projects. Such a procurement contract may proceed on a negotiated basis in lieu of competitive bidding.

In the case of transferring defence technology to the private sector, the head of the central administrative agency concerned classifies technologies as military or non-military, prepares a list of technologies that can be mutually transferred, chooses technology transfer projects, and makes relevant technologies available to the private sector.

**Drones**

32 What restrictions are there on manufacture and trade of unmanned aircraft systems or drones?

Drones and unmanned aircraft systems are subject to the rules found in the Aviation Act, which reflect the standards and methods adopted by the Convention on International Civil Aviation and Annexes thereto.

The manufacturing and sale of unmanned aircraft is permitted, but the design, manufacturing and maintenance of their physical frames must comply with the certification and airworthiness requirements of aircraft generally. If the weight of the aircraft (excluding fuel) is between 12 and 150 kilogrammes, pilot certificate, owner notification and display of the notification number are required; aircraft weighing less than 12 kilogrammes are exempt. The Act on the Promotion of Utilization of Drones is the general legislation addressing the drone industry and certification in Korea.

Unmanned military aircraft are required to obtain airworthiness certificate issued by the Defence Acquisition Program Administration (DAPA) or by the armed forces under the Military Aircraft Airworthiness Certification Act.

The Act on the Promotion of Utilization of Drones addresses establishing a foundation for, and government support of, a drone industry (eg, financing for startups, provision of outcomes from drone-related research and development, and provision of testing equipment and facilities, etc). The Act also requires the government to relax some requirements for obtaining safety certifications and so on, designate

advanced drone technologies and support relevant industries (eg, fast-track safety certifications applicable to drones that use the designated advanced technologies).

## MISCELLANEOUS

### Employment law

33 Which domestic labour and employment rules apply to foreign defence contractors?

Foreign defence contractors must comply with the mandatory labour and employment rules of the place where the employee routinely provides his or her service (eg, Korea), even if the contract's governing law, as chosen by the parties, is a different jurisdiction.

### Defence contract rules

34 Are there any specific rules that contractors, foreign or domestic, are bound by in defence contracts?

The Defence Acquisition Program Act (DAP Act) prescribes the procedures for domestic and overseas procurement. The details are further expanded upon in the Defence Acquisition Program Management Regulation (DAPMR). The Defence Acquisition Program Administration (DAPA) has established standardised special terms and conditions to be used in the case of domestic procurement. Unless there is a special reason, domestic procurement contracts are generally entered into using such terms and conditions. The DAPA has also established general terms and conditions for foreign procurements, and negotiates with foreign contractors based on such terms and conditions.

35 Do contractors avail themselves of these rules when they perform work exclusively outside of the jurisdiction?

Procurement contracts between the Korean government and a foreign contractor must comply with the provisions concerning the formation of procurement contracts under the DAP Act, the Act on Contracts to Which the State is a Party (ACSP) and other relevant legislation. These laws will apply even where the contractor performs work exclusively outside of Korea.

### Personal information

36 Must directors, officers or employees of the contractor provide personal information or certify that they fulfil any particular requirements to contract with a government entity?

Personal information of directors, officers or employees of the contractor are not required, and there is no particular requirement to satisfy other than the submission of integrity pledges. However, a contractor must register as an overseas source in the Defence E-Procurement System to participate directly in the procurement bidding. To register, a registration application, notarised security pledge and business registration certificate must be submitted.

In cases of registering a domestic branch or a domestic munitions sales agent of a foreign company, the registree submits a domestic business registration certificate, a corporate registry, security measurement results (ie, background checks conducted by Korean intelligence agencies) an integrity pledge and an agency agreement signed by the foreign company.

Furthermore, a civilian, regardless of his or her nationality, who needs to enter facilities or properties of the DAPA or a military unit in connection with the execution of a defence procurement contract for more than one month, may be required to provide personal information for a background check.

### Licensing requirements

37 What registration or licensing requirements exist to operate in the defence and security sector in the jurisdiction?

To register as an overseas source, a foreign company must apply for registration in the Defence E-Procurement System. The application must include a notarised security pledge, a business licence or business registration certification in the foreign jurisdiction, a manufacturer's certificate or a supplier's certificate to confirm the type of industry the registree is involved in, and the employment certificate of the signatory of the procurement contract. Upon the submission of all those required documents, a registration certificate is issued to the foreign company and it will be eligible to participate in procurement bidding in Korea.

If a Korean branch, or a Korean munitions sales agent, of a foreign company wishes to participate in procurement bidding, it must register in the Korean Comprehensive E-Procurement System and the Defence E-Procurement System.

### Environmental legislation

38 What environmental statutes or regulations must contractors comply with?

Contractors operating in Korea must comply with the following environmental laws and regulations, whether they are domestic or foreign entities:

- the Framework Act on Environmental Policy;
- the Natural Environment Conservation Act;
- the Environmental Health Act;
- the Clean Air Conservation Act;
- the Soil Environment Conservation Act;
- the Marine Environment Management Act;
- the Occupational Safety and Health Act;
- the Chemicals Control Act;
- the Nuclear Safety Act;
- the Water Environment Conservation Act;
- the Malodour Prevention Act;
- the Environmental Impact Assessment Act;
- the Environmental Dispute Adjustment Act; and
- the Wastes Control Act.

39 Must companies meet environmental targets? What are these initiatives and what agency determines compliance?

Companies exporting products to Korea or operating within the territory of Korea must comply with environmental standards prescribed by the Korean government. Environmental standards are established primarily by the Ministry of Environment, which has the authority to investigate breaches of these standards and may file criminal complaints with the prosecution service.

The Ministry of Oceans and Fisheries has the authority to investigate marine pollution.

Hazardous substances that not only affect the environment, but also the working environment of employees, are addressed by the Ministry of Employment and Labour.

40 Do 'green' solutions have an advantage in procurements?

'Green solutions' provide an advantage in procurements, moreover, they have now become legal requirements in many government purchases of products.

The Act on the Promotion of Purchase of Green Products requires that the national government, government entities, local governments and public institutions purchase products, where available, that

minimise emissions of greenhouse gases and pollutants by saving and using energy and resources efficiently.

In addition, the Environmental Technology and Industry Support Act requires that certain products be certified as 'eco-friendly' by the Ministry of Environment or by the Ministry of Trade, Industry and Energy in order to be eligible for purchase by the government. In the case of domestic procurement, eligibility to participate in bidding can be restricted based on whether a defence article to be procured is certified as an environmentally friendly product or an environmentally friendly technology by the Ministry of Environment.

## UPDATE AND TRENDS

### Key developments of the past year

41 What were the key cases, decisions, judgments and policy and legislative developments of the past year?

The National Assembly recently enacted the Act on Promotion of Innovation of Science Technology for National Defence as a way to integrate the new technologies of the Fourth Industrial Revolution into the defence industry, as well as to promote the continuous and systematic innovation, research and development related to science and technology for national defence. Accordingly, previous provisions regarding research and development have been removed from the Defence Acquisition Program Act (DAP Act).

Also, the National Assembly enacted the Act on Development and Support of the Defence Industry as independent legislation with the aim of laying a foundation for developing the defence industry and strengthening its competitiveness around the world. Accordingly, the previous provisions regarding plans and financing for promotion of the national defence industry, and financial support, etc have been removed from the DAP Act.

### Coronavirus

42 What emergency legislation, relief programmes and other initiatives specific to your practice area has your state implemented to address the pandemic? Have any existing government programmes, laws or regulations been amended to address these concerns? What best practices are advisable for clients?

In response to covid–19, the Korean government has implemented strict policies on disease prevention and social distancing. The government has amended the Infectious Disease Control and Prevention Act to address questions of stockpiling and management of medicines and medical equipment, tracking the spread of infections, access to and disclosure of information on movement, and enhancing the enforcement capacity of government officials.

In addition, the government has established a central headquarters to address the economic issues arising from the covid–19 pandemic. The government has distributed emergency funds to support exporters and the aviation, shipping and other key industries; and it has provided employment subsidies.

The Korean government has temporarily lowered the mandatory share of private investment in National Research and Development Projects from 35 per cent to 20 per cent, which will be applied during the duration of the covid–19 crisis.

In the national defence industry, the government has modified many procedures to reduce face-to-face contacts where possible. For example, a defence contractor was previously required to conduct on-site inspections when renewing a quality management certificate from the Defence Agency for Technology and Quality. However, an examination in writing and any other procedure which does not involve physical contact is now acceptable.

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## LEGAL FRAMEWORK

### Relevant legislation

1 What statutes or regulations govern procurement of defence and security articles?

The primary procurement legislation in Sweden regarding defence and security articles consists of the Defence and Security Procurement Act and the Government Procurement Act.

This legislation is based on European Union directives and is a part of the harmonisation process within the Union. More specific laws regarding the procurement of defence and security articles are based on Directive 2009/81/EC of the European Parliament and of the Council of 13 July 2009 (the Defence Procurement Directive). The purpose of the Defence and Security Procurement Directive is to provide a regulatory framework that is more flexible and better adapted to the continuations and needs of the procurement of defence and security articles. Meanwhile, the general legislation regarding public procurements is based on Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 (the Procurement Directive).

Since 1994, Swedish procurement legislation has been based on EU directives and several updates have been made since then. In 2008, previous national procurement legislation was replaced by the first Government Procurement Act (2007:1092).

On 26 February 2014, new EU directives on public procurement were adopted by Sweden, and as a result, a new Government Procurement Act entered into force on 1 January 2017. However, the 2007 Government Procurement Act largely still applies to procurements initiated before 2017.

The Defence and Security Procurement Act was introduced into Swedish legislation on 1 November 2011, in the light of the Defence Procurement Directive. This Directive created a special regulation for the procurement of defence and security articles. The introduction of the rules was intended to strengthen the European defence industry and facilitate harmonisation of the EU's internal market of defence equipment.

Over the years, parts of the Defence and Security Procurement Act have undergone changes. The latest changes, which came into force in 2019, are summarised below:

- The definition of 'security classified' was changed due to the creation of a new security law. The definition has been supplemented with a reference to the Security Protection Act containing provisions on the protection of classified information.
- To ensure that the information in advertisements of procurements is reliable, all procurements must be advertised in registered advertising databases, including those that, in accordance with the provisions of EU procurement directives, must be advertised through the European Commission Publications Office and its advertising database.
- References to the 'Terrorism Framework Decision' in laws have been replaced by references to the EU Counter-terrorism Directive 2017/541. And
- Amendments due to the designation of municipalities at the regional level being changed from 'county council' to 'region'.

### Identification

2 How are defence and security procurements identified as such and are they treated differently from civil procurements?

Defence and security procurement is defined as the procurement of the following articles, infrastructural projects and consultancy services:

- military equipment, including parts adherent to the equipment, components, and parts of components;
- equipment of a sensitive nature, including parts adherent to the equipment, components, and parts of components;
- construction contracts, goods and services that are directly related to the equipment in the above bullet points, during the article's entire period of use; or
- construction contracts and services specially intended for a military purpose or construction contracts and services of a sensitive nature.

The main difference between defence and security procurements and civil procurements is the applicable legislation. The Defence and Security Procurement Act and the Government Procurement Act are similar and coherent regarding regulations and structure, but there are some crucial differences. The Defence and Security Procurement Act contains regulations concerning security of supply and information security that are not contained in the Government Procurement Act, but does not contain regulations about competitive bidding and, unlike the Government Procurement Act, it does not contain restrictions regarding when negotiated procurement and selective bidding processes can be considered as acceptable methods of procurement. Even so, the general rule is that procurements should be executed through competitive bidding and published in the EU's Tenders Electronic Daily, an electronic publication in which all procurements within the EU are announced.

Regarding defence and security procurement, regulation concerning subcontractors is far more extensive than it is regarding civil procurement. For example, the contracting authority or entity may require a supplier to use subcontractors in defence and security procurement. The tenderer must, under certain conditions, advertise such a subcontract. A contracting authority or entity may reject a subcontractor selected by the tenderer.

There are some exceptions to the Defence and Security Procurement Act. On example is article 346 of the Treaty on the Functioning of the European Union (TFEU), which gives member states the right to exempt certain defence procurements to protect essential national security interests. The Defence and Security Procurement Act

states that intergovernmental agreements and procurements with the areas of underwater warfare, combat aircraft and critical parts of command infrastructure (eg, sensors, telecommunications and cryptography) are exempt from the regulations regarding competitive bidding, as are contracts awarded to research and development co-operation programmes between two or more European Economic Area (EEA) member states that aim to develop a new product.

**Conduct**

3 | How are defence and security procurements typically conducted?

The Swedish Armed Forces and the Swedish Defence Material Administration (FMV) follow a strategy regarding the supply of materiel. The strategy's main pillars are as follows:

- the needs of the Swedish Armed Forces should guide the supply of materiel;
- the supply should be cost-effective from a lifespan perspective and strive for enhanced security of supply;
- the supply should be guided by clear and mindful choices, taking cost, efficiency and discretion into consideration;
- the supply should make efficient use of existing materiel, with consideration of market prospects, and should be coordinated with the formation of new military units;
- international cooperation should be the main alternative regarding development, procurement and maintenance, and international cooperation regarding materiel should be maximised;
- the supply should be conducted in accordance with Swedish Armed Forces' research and development of technology;
- the number of weapon systems should be reduced through enhanced coordination of the systems;
- increased cost efficiency must be sought by reducing the FMV's own operations and giving suppliers greater commitments instead; and
- the supply of equipment shall be managed by a joint authority integrated equipment manager.

Both the FMV and the Swedish Armed Forces make defence and security procurements. Since the first of January 2019, the Armed Forces have had the opportunity to procure security and defence equipment itself regarding storage, servicing and workshops, as well as for maintaining existing weapon systems. However, the FMV is responsible for the majority of the defence and security procurements carried out in Sweden, which is why only the FMV will be referred to as the contracting authority from now on.

There are several methods available for the procuring entity, allowing for various different circumstances.

**Selective bidding**

During selective bidding, all suppliers are welcome to show an interest in a procurement, but only a selected number of suppliers will be invited to bid. The selection of the suppliers must be conducted according to the foundational principles of public procurements.

**Negotiated procurement**

A negotiated procurement is when the procuring entity invites a selected number of suppliers to negotiate for bids in accordance with the specifications advertised for that specific procurement.

'Negotiated procurement without foregoing advertising' is accepted under special circumstances, such as:

- when there has been a failed procurement where no bids were received;
- procurement of goods of proprietary nature, which can be obtained only from the proprietary source; and
- when the procurement consists of a supplementary order adherent to a previously conducted procurement.

There is extensive legislation regarding when this alternative procuring method is acceptable and is not an illegal direct contracting procedure.

**Dialogue of a competitive nature**

Competitive dialogue is used when procuring highly specialised types of goods and consulting services, where the procurement cannot be conducted through selective bidding or negotiated procurement. If this process is used, information regarding the goods or service must be included in the advertisement for the procurement. The purpose of the dialogue is to identify and decide how the needs of the procuring entity can best be provided for. Suppliers are requested to submit their final bids after the dialogue has concluded.

**Direct contracting**

Direct contracting is most commonly used when the contractual value is below the set monetary limit. The limit for defence and security procurements is currently 1,142,723 Swedish krona. The monetary limit is not limited to a specific contract, but to all contracts of the same kind procured during one financial year. Direct contracting can also be used if the contract's value exceeds the monetary limit under certain circumstances, provided, however, that the rules for approving negotiated procurement without foregoing advertising are complied with. This requires extraordinary reasons (eg, the opportunity to a very profitable contract or exceptional urgency. If extraordinary reasons exist, such procurements are evaluated on a case-by-case basis).

The advertising (when applicable) and submission of bids is followed by the evaluation of bids and the selection of the winner. The contract cannot be awarded for a period of 10 days following this, to enable time for reconsideration if it is requested. This period is called a 'standstill period' and is applicable in all cases. After the standstill period, the contract can be awarded and signed. The administrative court may request a decision to award a contract be reconsidered. With regard to FMV's procurement within FMV, it is always the administrative court in Stockholm that applies.

**Proposed changes**

4 | Are there significant proposals pending to change the defence and security procurement process?

The Defence Procurement Directive dates from 2009 and the European Commission has now concluded that it has had a limited effect. In connection with the proposed establishment of the European Defence Fund (EDF), during 2021 the European Commission will carry out an EU-wide review of the Directive's effects. As the Defence and Security Procurement Act is based on EU directives, changes in relevant EU directives will affect the act.

EU member states would be allowed to use the EDF to fund joint defence investments and research projects (research and development is exempt from the Defence and Security Procurement Act), and to procure 'capabilities' (ie, everything that contributes to the performance of a certain task (eg, equipment, knowledge, technology and planning)).

Another factor that may affect the defence and security procurement process is the upcoming review of the Swedish strategy regarding supply of materiel. The review will be a government inquiry that will present a strategy for the Swedish military's need for materiel and related research, technological development and services in peace, crisis and war. This inquiry must be finalised no later than 4 May 2022, and shall, among other things, clarify Sweden's essential security interests, which may affect the exemptions to the Defence and Security Procurement Act.

**Information technology**

5 | Are there different or additional procurement rules for information technology versus non-IT goods and services?

There are no exceptions regarding information technology in the Swedish legislation.

However, the security recommendations for public procurement linked to the expansion of fifth-generation mobile networks (5G) will be tightened. In January 2020, EU member states, with the support of the European Commission and the European Union Cyber Security Agency (ENISA), published a toolbox of measures designed to effectively manage risks to 5G networks in a coordinated manner. ENISA's toolbox contains recommended measures to reduce identified risks, for example by requiring risk analyses and the taking of protective measures prior to the procurement of a contractor or equipment. These recommendations are not binding upon member states.

**Relevant treaties**

6 | Are most defence and security procurements conducted in accordance with the GPA or other treaty-based procurement rules, or does this jurisdiction commonly use the national security exemption to procure them?

The Swedish legislation is a part of the harmonisation process within the European Union. The EU directives, which Sweden's national legislation on defence and security procurement is based on, were revised in accordance with the Agreement on Government Procurement as the EU is a member of the World Trade Organization (WTO). The individual EU member states are also WTO members in their own rights.

## DISPUTES AND RISK ALLOCATION

**Dispute resolution**

7 | How are disputes between the government and defence contractor resolved?

The standard form contract of the Swedish Defence Material Administration (FMV) provides that disputes regarding the application and interpretation of the contract should be settled in the district court of Stockholm. When it comes to contracts of higher contractual values, the most common dispute resolution method is arbitration in accordance with the rules of the Arbitration Institute of the Stockholm Chamber of Commerce (SCC). An arbitral tribunal is usually composed of three arbitrators, unless parties in the individual case agree on a sole arbitrator, and the seat of arbitration shall be Stockholm, Sweden. If the arbitration tribunal consists of three arbitrators, the parties each choose one arbitrator and these arbitrators jointly select a chairperson. If there is to be a sole arbitrator to settle the dispute, the parties must agree that there should be a sole arbitrator and who it should be. There is no clear definition of what is regarded as 'contracts of higher contractual values', however, the concept refers to the nature of the contract rather than its contractual value. Factors that may indicate that it is a contact of higher contractual value are, among other things, whether the product or service is to be procured is of a sensitive nature, requires development, and will cost a significant price.

The FMV has a long tradition of using arbitration as its main method of dispute resolution. When the FMV took over procurements from the Swedish Armed Forces in 2013, it continued to use arbitration and its cases were heard at Stockholm's district court. The Swedish Armed Forces have since regained responsibility for procurement and they are keeping their old method of resolving disputes (ie, disputes are heard at Stockholm's district court).

8 | To what extent is alternative dispute resolution used to resolve conflicts? What is typical for this jurisdiction?

For smaller contracts, it is more common to use the regular dispute resolution alternative provided in the FMV's standard form contract. The predominant dispute resolution mechanism in larger contracts is arbitration in accordance with the rules of the SCC's Arbitration Institute. There is no clear definition of what is to be regarded as 'small contracts' or 'larger contracts'. These concepts refer to the nature of the contract rather than the contractual volume. Factors that may indicate a small contract are, among other things, the product or service to be procured is a standard product or service, development is not required and the cost is insignificant. When it comes to larger contracts, factors such as whether the product or service is to be procured is of a sensitive nature, requires development or comes at a significant price are crucial.

A contractor may not stop or postpone executing its obligations pursuant to procurement agreement on the grounds that arbitration proceedings have been applied for or are in progress.

**Indemnification**

9 | What limits exist on the government's ability to indemnify the contractor in this jurisdiction and must the contractor indemnify the government in a defence procurement?

Under Swedish contract law, the FMV, like any other counterparty, has to indemnify the contractor for direct losses arising from a breach of contract by the FMV, provided that the direct losses are reasonably and foreseeably caused by the breach. This also applies to contractors, which have to indemnify the FMV for breaches caused by contractors' actions. The FMV's standard form contract contains language to the effect that the FMV or contractor only becomes accountable for indirect losses if the FMV or the contractor was grossly negligent.

**Limits on liability**

10 | Can the government agree to limit the contractor's liability under the contract? Are there limits to the contractor's potential recovery against the government for breach?

The limitations on a contractor's and the government's liabilities vary depending on the value of the contract. For smaller procurements, the FMV's standard form contract is used which it provides that liability is limited to 5 million Swedish krona and applies to both parties. When it comes to larger procurements, an open-ended limitation of liability is standard practice. The FMV has traditionally only used open-ended liability limitations but is now willing to negotiate liability level caps with counterparties. There is no clear definition of what is to be regarded as 'smaller procurement' or a 'larger procurement'. These concepts are aimed at the nature of the contract rather than the procurement volume. Factors that may indicate a smaller procurement are, among other things, the product or service to be procured is a standard product or service, no development is required and the price is insignificant. When it comes to larger procurements, factors such as whether the product or service is of a sensitive nature, requires development and comes at a significant price, are crucial.

**Risk of non-payment**

11 | Is there risk of non-payment when the government enters into a contract but does not ensure there are adequate funds to meet the contractual obligations?

All procurements conducted by the FMV are based on a pre-decided procurement plan that is approved by the Swedish parliament. The procurement plan consists of specific procurement projects, each of

which have set budgets. This means that there are always sufficient funds for a desired procurement. The FMV may not enter into a legally binding procurement contract if adequate funds to meet the contractual obligations are not ensured.

**Parent guarantee**

12 | Under what circumstances must a contractor provide a parent guarantee?

For larger contracts, a parent guarantee is typically required. These types of contracts often require a performance guarantee for the execution of the contract as well. For smaller contracts and smaller suppliers, a bank guarantee from a reputable bank is often sufficient.

## DEFENCE PROCUREMENT LAW FUNDAMENTALS

**Mandatory procurement clauses**

13 | Are there mandatory procurement clauses that must be included in a defence procurement contract or that will be read into the contract regardless of their actual inclusion?

There are no mandatory clauses that must be included in a defence procurement contract, but some clauses are almost always included. For example, the FMV always requires that Swedish law is applicable. The FMV's right to cancel a contract due to anticipated breach of contract is also always included. Furthermore, the FMV has the right to fully or partly assign contracts to another Swedish government agency.

Swedish contractual legislation contains a fundamental principle of good faith. This principle forms part of all Swedish contractual law. There are also specific clauses that can be read into contracts – for example, compliance with ethical standards and good practice, including in the areas of environment, human rights, working conditions, anti-corruption, anti-discrimination, and diversity.

In the procurement document, a distinction is made between criteria that must be fulfilled and criteria that are non-mandatory. The criteria can concern economic status, technology features, etc.

**Cost allocation**

14 | How are costs allocated between the contractor and government within a contract?

A fixed price for the procured article or services is included within the contract. New negotiations must be conducted if the price is to be altered.

In development contracts, which have been quite rare in Sweden during the last decade, there is usually a mix of elements of open-book or cost-plus pricing. The actual allocation of costs between the FMV and the contractor under these development contracts depends on the language of the individual contract.

**Disclosures**

15 | What disclosures must the contractor make regarding its cost and pricing?

This depends on how the FMV has decided to procure articles or contract a procurement. The two main ways to follow up on a contractor's costs and pricings are managed through open-book or earned value management (EVM) processes.

In a fixed-price contract, the contractor must account for its costs according to EVM. EVM is a project management technique for measuring project performance and progress in an objective manner that uses data that has emerged during the project to make projections, such as whether the supplier will keep to the agreed timeframe and final price.

**Audits**

16 | How are audits of defence and security procurements conducted in this jurisdiction?

Audits are conducted by the FMV or a reputable accountant firm (ie, chartered accountants and their assistants) of the FMV's choice. Furthermore, the FMV has the right to call in experts to assist in performing audits.

It is the contractor's responsibility to provide FMV with full insight into its operations. Regarding transparency with subcontractors, FMV has the same right to transparency in the operations as if the work had been performed by the contractor. This presupposes that the subcontractor's work is not of an insignificant nature. Furthermore, the FMV has the right to place its own personal or expert hired by FMV with the subcontractor.

**IP rights**

17 | Who gets the ownership rights to intellectual property created during performance of the contract? What licences are typically given and how?

In the past, intellectual property rights have vested in principle with the contractors to whom the FMV have granted certain rights. However, the current trend is for the FMV to request more extensive rights over the IP, and therefore these clauses have to be carefully drafted.

FMV's general terms stipulate that the client shall have a timely and geographically unlimited right to, for its own part and for the authorities within the Ministry of Defence's area of activity needs, including participation in international efforts or other intergovernmental collaborations – without special compensation and without prejudice to intellectual property rights – to freely use, and allow others to use, documentation that is created by the supplier or its subcontractors when performing the contract. The right of use also includes documentation that has been produced in another context to the extent that it is necessary to use the product or services in accordance with the objectives and purpose of the contract.

**Economic zones**

18 | Are there economic zones or other special programmes in this jurisdiction commonly utilised by foreign defence and security contractors for financial or other procurement related benefits?

Not applicable.

**Forming legal entities**

19 | Describe the process for forming legal entities, including joint ventures, in this jurisdiction.

**Limited companies**

A limited company must:

- establish a memorandum of association and articles of association;
- subscribe and pay for shares;
- apply for a certificate from a Swedish bank that states that the share capital has been paid in;
- sign the memorandum of association; and
- register the company at the Swedish Companies Registration Office.

A public limited company requires share capital of 500,000 Swedish krona and a private limited company requires share capital of 25,000 Swedish krona.

### Trading companies

To establish a trading company, there must be an agreement to jointly conduct business. The partnership must be registered at the Swedish Companies Registration Office.

### Partnerships

A partnership consists of an agreement to jointly conduct business without the intention to establish a limited company or a trading company. The parties can be either individuals or legal persons.

### Joint ventures

There are three different types of joint ventures that can be established. A contractual joint venture (or non-corporate joint venture) consists of an agreement between two or more companies to conduct business through collaboration. (Note that the joint venture agreement can constitute a partnership agreement.) A partnership joint venture is when two or more companies decide to form a trading company, and a corporate joint venture is when a new limited company is established between the parties. The two latter forms are conducted according to the Companies Act and Partnership and Non-registered Partnership Act.

### Licensing

In order to conduct business in the defence and security sector, a licence is required from the Swedish National Authority called the Inspectorate of Strategic Products (ISP). Criteria regarding the quantity of non-Swedish ownership can be attached to the licence. The ISP can also require that the president of the company a certain number of members of its board must be Swedish citizens and be resident in Sweden. The ISP sets such requirements on a case-by-case basis.

### Access to government records

20 Are there statutes or regulations enabling access to copies of government records? How does it work? Can one obtain versions of previous contracts?

The Swedish jurisdiction recognises the principle of public access to public records. The principle gives both Swedish citizens and foreigners the right to apply for copies of government records that are not classified. Applications are handed to the authority of interest and a confidentiality assessment is conducted. The same rules apply to previous contracts.

The principle of public access to information regarding tenders is expressed in the Public Access and Secrecy Act. The law stipulates that information relating to an ongoing tender may not be requested from anyone other than the natural person or legal person that submitted the tender, nor before a decision to award the contract to a tenderer is made. Until that time, details about the tender cannot be made public and are held in absolute secrecy. However, after the absolute secrecy is lifted some details still cannot be released (mainly concerning information about a tenderers' business or operating conditions) if it can be assumed that the tenderer would suffer damage if the information was to be disclosed.

A contracting authority is not bound by a tenderer requesting confidentiality but is of great importance when assessing whether the tenderer may suffer damage if the information is disclosed and therefore whether confidentiality applies to information in a tender.

### Supply chain management

21 What are the rules regarding eligible suppliers and supply chain management and anti-counterfeit parts for defence and security procurements?

Every supplier that has the legal right within its own jurisdiction to deliver the article of the procurement in question may be included in the procurement process. Swedish legislation also contains a strict non-discrimination principle and a principle of equal treatment. These principles give foreign suppliers the same rights as Swedish national suppliers to take part in the procurement processes.

Regarding subcontractors, the main rule is that the supplier has the right to choose its own subcontractors, with some restrictions. The procuring entity may require that parts of the contract are undertaken by a subcontractor. There may also be requirements regarding the process in which the subcontractors are chosen. For example, the supplier may be required to observe the principles of non-discrimination and equal treatment. The procuring entity has the ability, under certain circumstances, to dismiss a subcontractor chosen by the supplier.

There is no procurement legislation that specifically regulates against the use of counterfeit parts. The most applicable regulations concern intellectual property. Clauses regarding intellectual property feature in procurement contracts.

## INTERNATIONAL TRADE RULES

### Export controls

22 What export controls limit international trade in defence and security articles? Who administers them?

There are regulations regarding manufacturing and supplying defence articles. These regulations can be found in the Military Equipment Act of 1992.

The Inspectorate of Strategic Products (ISP) administrates control and compliance of defence material and dual-use products. The ISP has provided the following guidelines regarding export in defence and security articles:

*A licence to export defence material, or other cooperation arrangements with someone abroad regarding defence equipment, should be permitted only if such exports or cooperation is*

- *considered necessary to meet Swedish defence needs;*
- *otherwise desirable in terms of security policy;*
- *not in conflict with Sweden's international obligations; and*
- *not in conflict with the principles and objectives of Swedish foreign policy.*

The ISP also handles targeted sanctions, including trade restrictions. These sanctions may be based on a decision from the United Nations, the European Union or the Organization for Security and Co-operation in Europe (OSCE) to take collective sanction measures. In addition, Sweden also adheres the 2008 EU Common Position on arms export controls and is a signatory of the UN Arms Trade Treaty.

In 2018, export controls on defence material were tightened. This is the result of a public inquiry that has sharpened Sweden's national political guidelines, which have been given a stricter view of exports of defence material to non-democratic states. The tightened legislation has, for example, led to a democracy criterion being introduced in the Military Equipment Act.

**Domestic preferences**

23 | What domestic preferences are applied to defence and security procurements? Can a foreign contractor bid on a procurement directly?

There are no restrictions in Swedish legislation regarding foreign contractors. On the contrary, the legislation includes a non-discrimination principle and a principle of equal treatment. Every supplier who has the legal right within its own jurisdiction to deliver the article of the procurement in question may not be excluded from the procurement process. However, Sweden has recognised essential security interests within the areas of underwater warfare and combat aircraft, integrity-critical parts of the command area, such as sensors, telecommunications and cryptography, and desires to maintain a national industrial capacity within these areas.

**Favourable treatment**

24 | Are certain treaty partners treated more favourably?

Generally, Sweden is a promoter of free trade, and has approached trade positively and without restrictions regarding the suppliers' nationality. However, there are rules regarding cooperation within the EU. In the procurement legislation, there are regulations regarding reciprocal acknowledgement for certificates that are issued in another member state of the EU or in another country within the European Economic Area (EEA). There are also some generally issued permissions to export defence and security articles within the EU, where the exporting entity does not need to apply for permission from the ISP.

When it comes to buying defence and security articles from the United States, this can be done through a Foreign Military Sales acquisition. This method has had a positive reaction from the Swedish government and been used on several occasions.

In general, Sweden is interested in international cooperation but rarely enters into a development project without another funding state. In these occasions, there are some countries that Sweden prefers to cooperate with, such as Finland. In December 2020, the Swedish government has decided to authorize the Swedish Defence Material Administration (FMV) to negotiate and enter into international agreements with Finland regarding common procurement of defence material and services. The objective from the Swedish government is to procure larger quantities of defence material and services together with Finland and thereby create cost efficiency among other things.

**Sanctions**

25 | Are there any boycotts, embargoes or other trade sanctions between this jurisdiction and others?

Sweden adheres to the following boycotts, embargoes and other trade sanctions provided by the UN, EU or the OSCE regarding defence and security articles.

**UN weapon embargoes**

- Afghanistan (listed entities);
- the Central African Republic;
- North Korea;
- the Democratic Republic of the Congo;
- Iraq;
- Yemen;
- Lebanon;
- Liberia;
- Libya;
- Somalia;
- Sudan; and
- South Sudan.

**EU weapon embargoes**

In addition to the following, the EU implements all weapon embargoes decided by the UN Security Council.

Legally binding

- Belarus (including equipment used for internal repression);
- Burma/Myanmar (including equipment used for internal repression);
- Iran (including equipment used for internal repression);
- Libya (including equipment used for internal repression);
- Russia;
- Sudan;
- South Sudan;
- Venezuela (including equipment used for internal repression); and
- Zimbabwe (including equipment used for internal repression).

Politically binding

- China (Council declaration).

Other agreements

- Egypt (including equipment used for internal repression) (Council conclusions); and
- Syria (Council declaration).

Sweden is also party to the OSCE weapon embargo on Nagorno-Karabash, which affects both Armenia and Azerbaijan.

**Trade offsets**

26 | Are defence trade offsets part of this country's defence and security procurement regime? How are they administered?

The main concern is that trade offset is to be abolished within the EU as it is not considered to be compatible with the foundational purposes of the EU. Within the EU, there is only one exception in which trade offset may be used, which is when an offset is required to protect a member states' substantial security. Outside EU and EEA trade, trade offset is still an available option. However, in general, Sweden does not use trade offset as a requirement for procuring articles from a supplier outside the EU.

## ETHICS AND ANTI-CORRUPTION

**Private sector appointments**

27 | When and how may former government employees take up appointments in the private sector and vice versa?

There are no general regulations regarding mandatory garden leave in the Swedish jurisdiction. A government inquiry has been looking into the issue of 'revolving doors' on a generic basis between the public and private sectors. As a result, the Restrictions on the Transfer of Ministers and State Secretaries to Other than State Activities Act has been added.

This legislation introduced a 'restrictions deferred period' and a 'subject restriction'. The 'restrictions deferred period' means that the minister or state secretary may not start a new assignment, employment or business activity for up to 12 months after being terminated from their public service position. 'Subject restriction' means that the individual beginning a new assignment, employment or business activity may not deal with specified issues for a period of up to 12 months after their departure from public service.

**Addressing corruption**

28 How is domestic and foreign corruption addressed and what requirements are placed on contractors?

The legislation provides a non-optional rule that states that if a supplier is found guilty of corruption, the supplier must be excluded from the procurement. If the supplier is a legal person, the supplier is considered guilty of corruption if a representative of the supplier is found so. If there are well-grounded reasons to presume that a supplier is guilty of corruption, the procuring entity may require that the supplier offer evidence to disprove the presumption.

Both the passive and the active sides of corruption are punishable. This means that it is a criminal offence both to receive and to offer a bribe. Bribery can be committed by an employee or a contractor. The crime is committed if he or she, for his or her own part or for someone else, receives, accepts a promise of or requests an improper benefit for the performance of their employment or assignment. Criminality also applies if the act was committed before the employee or contractor received his or her position and after it has ceased. The offering of a bribe is committed if someone leaves, promises, or offers an improper benefit to an employee or contractor for the performance of his or her employment or assignment.

The Swedish Defence Material Administration (FMV) provides an extensive code of ethics concerning bribery to its employees. These consist of guidelines concerning suppliers offering to pay for meals and travel expenses or provide loans, etc. Corruption is considered a crime according to the Swedish Penal Code. The FMV's terms and conditions require compliance with anti-corruption regulations and maintain ethical standards from tenderers. FMV has corresponding requirements through, among other things, policies and FMV's status as an authority.

**Lobbyists**

29 What are the registration requirements for lobbyists or commercial agents?

There are no requirements regarding registration for lobbyists or commercial agents. Concerning licensing from the ISP, agents that only sell to the Swedish government, or to suppliers that have permission to manufacture, were previously excepted. Since 2018, agents that sell to the Swedish government or to suppliers and have permission to manufacture are required to have a manufacturing licence and a brokering licence.

**Limitations on agents**

30 Are there limitations on the use of agents or representatives that earn a commission on the transaction?

There are no such limitations in the Swedish jurisdiction.

## AVIATION

**Conversion of aircraft**

31 How are aircraft converted from military to civil use, and vice versa?

All aircraft in Sweden require certification that proves that the aircraft is safe to use. Aircraft are typically only certified for either civil or military use, but there are no restrictions regarding running the two certification processes parallel to each other. In this case, the aircraft will enjoy both certifications and can be put to for both civil and military use. To convert an aircraft from military to civil use, or vice versa, a new certification process is needed if the aircraft does not have both certificates. There are also two different registers for the two types of aircraft, in which individual aircraft are to be registered.

**Drones**

32 What restrictions are there on manufacture and trade of unmanned aircraft systems or drones?

There are no specific rules concerning unmanned aircraft systems or drones. These products are subject to the same rules as all other controlled products. The Inspectorate of Strategic Products (ISP) issues licences according to the specific types of articles that can be manufactured or supplied.

## MISCELLANEOUS

**Employment law**

33 Which domestic labour and employment rules apply to foreign defence contractors?

If the suppliers' employees are working in Sweden, Swedish labour law is applied. It is prohibited to use child labour abroad, and to import goods manufactured by child labour to Sweden. If a sufficient amount of working hours are executed, a permanent establishment might be considered established. The necessary conditions regarding this are to be found in the Swedish Income Tax Act. These conditions may vary according to taxation treaties.

**Defence contract rules**

34 Are there any specific rules that contractors, foreign or domestic, are bound by in defence contracts?

There are clauses that are included in most of the contracts concerning defence procurements. For example, the Swedish Defence Material Administration (FMV) always requires that Swedish law is applicable. The right for the FMV to cancel a contract due to an anticipated breach of contract is also always included.

Swedish contractual legislation contains a fundamental principle of good faith. This principle impregnates the corpus of Swedish contract law. There are also specific clauses that can be read into a contract regarding compliance with ethical standards and good practice (eg, the areas of environment, human rights, working conditions, anti-corruption, anti-discrimination and diversity).

35 Do contractors avail themselves of these rules when they perform work exclusively outside of the jurisdiction?

This depends on the subject of the contract. For example, the prohibition against child labour applies even if the work is performed outside the Swedish jurisdiction. The choice of applicable law is another example that is still applicable outside Sweden.

**Personal information**

36 Must directors, officers or employees of the contractor provide personal information or certify that they fulfil any particular requirements to contract with a government entity?

There are some situations when a supplier, and its representatives, may be required to provide information regarding certain circumstances. Swedish legislation requires a supplier that is found guilty of corruption, organised crime, money laundering or terrorist offences is excluded from procurements. If the supplier is a legal person, the supplier is considered guilty of corruption if a representative for the supplier is found so. If there are well-grounded reasons to presume that the supplier is guilty of corruption, the procuring entity may require that the supplier offer evidence to disprove the suspicion. The same

principles apply to less severe situations, where the procuring entity may exclude the supplier (eg, bankruptcy and faults in the exercising of their profession).

**Licensing requirements**

37 | What registration or licensing requirements exist to operate in the defence and security sector in the jurisdiction?

To be able to manufacture and distribute security and defence articles, two licences are required from the Inspectorate of Strategic Products (ISP): a manufacturing licence and a brokering licence.

Criteria limited the amount of non-Swedish ownership of a company may be attached to these licences, and the ISP may also require the company's president and a certain number of the board members to be Swedish citizens and be resident in Sweden.

**Environmental legislation**

38 | What environmental statutes or regulations must contractors comply with?

The Swedish defence sector authorities have jointly developed 'The Defence Sector's Criteria Document – Chemical Substances, Chemical Products and Articles'. In this document, the suppliers can find environmental requirements and how they may apply to procurements.

For some contracts, the FMV requires that the supplier establish an environmental plan describing how environmental measures will be taken in the course of a project. The plan describes how environmental work or management will be applied in the supplier's commitment to the FMV, and what measures will be taken to ensure and confirm that legal requirements, internal requirements and the FMV's environmental requirements are met.

For some contracts, the FMV will require that a supplier produces a 'recycling manual' for the system in question. The aim of this manual is to provide all the information needed to dispose of the system in a way that minimises effects on people's health and the environment.

In the implementation of projects and the development of products on behalf of the FMV, environmental legislation, such as the Swedish Environmental Code and the European Community Regulation on chemicals and their safe use (EC) 1907/2006, is followed.

39 | Must companies meet environmental targets? What are these initiatives and what agency determines compliance?

The industries operating in Sweden play a large role in meeting Swedish environmental targets, and the targets set up by the European Union and the United Nations. There are specific rules and regulations that must be complied with to run a business in Sweden. These rules can be found in the Environmental Code. The legislation consists of both general environmental goals and more specific rules regarding conducting business that possibly has a negative effect on the environment. The authorities conducting controls and making decisions according to the Environmental Code are the government, county administrations, municipalities, and regional environmental courts, the Environmental Court of Appeal and the Supreme Court of Sweden.

40 | Do 'green' solutions have an advantage in procurements?

'Green' solutions do not have advantages in procurements. However, the Swedish National Agency for Public Procurement emphasises that procurement is an important instrument for achieving socio-political aims, such as environmental goals. A contracting authority has, according to the National Agency for Public Procurement, a great opportunity to set far-reaching requirements for what is to be procured.

Due to these circumstances, the FMV may set up extensive environmental requirements for a procurement, which the supplier must be able to meet. The FMV works to set well-balanced and relevant environmental requirements for its suppliers in order to reduce the authority's indirect environmental impact in procurements. When the FMV draws attention to the fact that there is a need for environmental requirements within a work, it works to produce requirements and proposals on how the supplier can report requirements.

## UPDATE AND TRENDS

**Key developments of the past year**

41 | What were the key cases, decisions, judgments and policy and legislative developments of the past year?

The Swedish defence procurement process is probably one of the most stable and transparent procurement systems in the world. Furthermore, the trend for Swedish defence acquisitions is also increasing, as the Swedish defence budget is set to see a significant increase, even by international standards, over the coming five years (2021-2025). The Swedish defence forces are setting up several new regiments, which have to be staffed and equipped with new infrastructure and defence materiel. We also project that Sweden will engage in joint procurements, at higher levels, with Finland.

The Transatlantic Link continues to be important for Swedish security and defence interests. There is reason to assume that President Biden's administration will foster a deepening of the already ongoing defence and security cooperation regarding procurement and development between Sweden and the United States.

On 1 April 2019, the new Security Protection Act came into force in Sweden. The act sets contemporary requirements for what public and private activities need to do to protect information that is important regarding Sweden's security.

In 2019, the EU adopted Regulation (EU) 2019/452 to examination foreign direct investment (FDI) in the EU that created a legal framework for member states to examine FDI within the EU in the interests of security or public order. Due to this, a new act with supplementary provisions to the EU regulation entered into force on 1 December 2020 in Sweden. The Inspectorate of Strategic Products (ISP) has been commissioned to be the contact point for such investigations and has been empowered to collect certain information from foreign companies intended to invest in Sweden prior to their investment being made, if there is a risk that the transaction may affect Swedish security activities.

**Coronavirus**

42 | What emergency legislation, relief programmes and other initiatives specific to your practice area has your state implemented to address the pandemic? Have any existing government programmes, laws or regulations been amended to address these concerns? What best practices are advisable for clients?

In Sweden, several general measures have been put in place to mitigate the effects of the coronavirus pandemic (eg, revenue support, short-term layoffs of employees and various types of tax relief for companies). The main measure that applies to the defence industry, is an exemption to the limitations on state support in the Treaty on the Functioning of the European Union that has enabled several states to assist defence companies manage deficits.

Also, due to the pandemic, companies should review their ability to invoke force majeure clauses. The possibility of invoking such clauses depends on how specific clauses within agreements are formulated, but it is not always obvious how a force majeure clause can be interpreted

and whether it can be applied to the pandemic. Swedish legislation lacks provisions on force majeure. Due to this, there have been recent discussions among the Swedish legal scholars within jurisprudence about other grounds to allow responsibilities to be discharged in the event of a breach of contract due to the pandemic. Among other things, it has been discussed whether the control responsibility that is expressed in the Sale of Goods Act and United Nations Convention on Contracts for the International Sale of Goods can be applied by analogy. In practice, the control responsibility means that the buyer is entitled to damages in the event of the seller's delay if the seller cannot show that the delay is due to an obstacle beyond his control and which the seller could not be expected to have taken into account at purchase and consequences could not be avoided or overcome. It has also been discussed whether it might be relevant to adjust agreements that have been unduly burdensome to one of the parties due to pandemic with reference to the Contracts Act. However, the legal situation is still unclear.

Considering this, our advice is for defence industry companies to review their agreements and act in a timely fashion, and for all future agreements to include pandemic relief in force majeure clauses.

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## LEGAL FRAMEWORK

### Relevant legislation

1 | What statutes or regulations govern procurement of defence and security articles?

Procurement of defence and sensitive security equipment and services by contracting authorities in the United Kingdom is governed by the Defence and Security Public Contracts Regulations 2011 (DSPCR). Domestic and pre-Brexit EU case law is also influential in interpreting the applicable laws. The Single Source Contract Regulations 2014 (SSCRs) apply when the Ministry of Defence (MoD) awards qualifying defence contracts with a value of over £5 million without any competition. They are intended to ensure value for money is achieved even in the absence of competition.

### Identification

2 | How are defence and security procurements identified as such and are they treated differently from civil procurements?

Procurement by a UK contracting authority (such as the MoD) falls within the scope of the DSPCR when the contract has a value above the financial threshold (£378,660 for goods and services or £4,733,252 for works) and is for:

- military equipment and directly related goods, services, work and works;
- sensitive equipment (ie, equipment for security purposes involving, requiring or containing classified information), and directly related goods, services, work and works;
- work, works and services for a specific military purpose; or
- sensitive work or works and sensitive services.

From January 2021, procurements will be advertised by way of the UK Government's Find a Tender Service as a procurement under the DSPCR.

The key difference for procurements carried out under the specific defence rules are the mechanisms put in place to protect sensitive information and to ensure defence and security interests are protected. For example, there are specific provisions that are intended to protect sensitive information throughout the supply chain, to ensure security of supply and to give the courts flexibility to consider defence and security interests when considering remedies.

Where a procurement falls outside the scope of the DSPCR, it will be governed by the usual civil procurement rules, with a lower threshold of about £122,976 for goods and services contracts procured by Central Government departments (or £189,330 for sub-Central authorities) and the same threshold for works contracts.

### Conduct

3 | How are defence and security procurements typically conducted?

There are three different procurement procedures under the DSPCR and five different procedures under the normal civil rules.

Where the rules are triggered, a formal procurement process is initiated by the publication of a Contract Notice in the UK Government's Find a Tender Service (FTS). Most procurement procedures involve a pre-qualification process, as part of which bidders must demonstrate their financial stability and technical capability, including experience in similar contracts. The way that the procurement proceeds depends on whether the authority has chosen a procedure that permits them to discuss the contract and requirements with the bidders (negotiated procedure with advert, competitive dialogue procedure or, under the civil rules only, an innovation partnership) or not (restricted procedure or, under the civil rules only, the open procedure). It is increasingly common for negotiations on a contract to be limited, with many of the contract terms being identified as non-negotiable.

The evaluation process is undertaken on the basis of transparent award criteria and weightings, which are provided to bidders in advance in the tender documents. Once the winning bidder is selected, there is relatively little scope for further negotiation. Although, in practice, some negotiation is common.

### Proposed changes

4 | Are there significant proposals pending to change the defence and security procurement process?

Certain consequential amendments were made to the DSPCR following the UK's exit from the European Union in January 2020. As a free trade agreement was made between the UK and EU following the end of the transition period on 31 December 2020, the DSPCR will likely be amended (potentially substantially) in the near future.

### Information technology

5 | Are there different or additional procurement rules for information technology versus non-IT goods and services?

There are no specific or additional rules that relate to IT procurement. Most IT procurement will be undertaken under the civil rules and, in many instances, this is done through centralised framework agreements awarded by the Crown Commercial Service.

**Relevant treaties**

6 Are most defence and security procurements conducted in accordance with the GPA or other treaty-based procurement rules, or does this jurisdiction commonly use the national security exemption to procure them?

The majority of defence and security procurements have been conducted in accordance with the Agreement on Government Procurement (GPA) or European Union treaties, but a minority of contracts are still awarded in the context of national security and other exemptions. The MoD published a five-year review of the application of the DSPCR in December 2016. It shows that 25 per cent of its contracts were considered exempt from the normal requirement to compete openly, mostly due to the national security exemption contained in article 346 of the Treaty on the Functioning of the European Union, but that there were also other exemptions (eg, an exemption relating to government-to-government sales). It also shows that since the introduction of the DSPCR there has been a decline in reliance on these exemptions – from 55 per cent to 25 per cent.

## DISPUTES AND RISK ALLOCATION

**Dispute resolution**

7 How are disputes between the government and defence contractor resolved?

Disputes between the government and a defence contractor regarding matters of contract performance will be resolved in accordance with the dispute resolution procedure contained in the contract. It is common for a defence contract to incorporate DEFCON 530 (DEFCONs are Ministry of Defence (MoD) defence conditions), which provides for disputes to be resolved by way of confidential arbitration in accordance with the Arbitration Act 1996.

For disputes regarding matters of contract award, how disputes are resolved will depend on which legislative regime the procurement process falls under. Where the Defence and Security Public Contracts Regulations 2011 (DSPCR) applies, there is a formal process under which suppliers may apply to the court to review the actions of the contracting authority during the procurement process, and the remedies available (which differ depending on whether the contract has been entered into or not).

Where the Single Source Contract Regulations 2014 (SSCRs) apply, either of the disputing parties may request that the Single Source Regulations Office (SSRO) makes a binding determination in certain circumstances. This determination will take precedence over any contractual dispute resolution procedure.

8 To what extent is alternative dispute resolution used to resolve conflicts? What is typical for this jurisdiction?

DEFCON 530 requires the disputing parties to attempt, in good faith, to resolve disputes that may include alternative dispute resolution (ADR) procedures, before commencing arbitration. The most appropriate form of ADR will depend on the size and nature of the dispute but the most common form remains mediation. ADR will remain available once the arbitration is under way.

ADR is also available to parties in disputes concerning a contract award. Under the DSPCR, before proceedings can be commenced, the challenger must provide the contracting authority with details of its claim and its intention to start proceedings, which provides an opportunity for the parties to try to resolve the dispute. However, owing to the short time limits for pursuing a procurement claim (typically 30 days from the date the supplier knew or ought to have known of the grounds giving rise to the breach), time is extremely limited for the parties to engage in any formal ADR process at this stage. ADR will be available to the parties as a parallel confidential process during any litigation.

**Indemnification**

9 What limits exist on the government's ability to indemnify the contractor in this jurisdiction and must the contractor indemnify the government in a defence procurement?

The legal limits on the government's ability to indemnify a contractor apply to any business-to-business contract; they are not specific to defence-related agreements. These limitations mainly stem from the Unfair Contract Terms Act 1977, which makes certain terms excluding or limiting liability ineffective or subject to reasonableness. There may also be public policy reasons for an indemnity not to be valid; for example, the government cannot indemnify a contractor for civil or criminal penalties incurred by the contractor if the contractor intentionally and knowingly committed the act giving rise to the penalty.

The MoD also has a commercial policy on when it can give indemnities. This policy says the MoD can offer a limited range of indemnities for specific risks, but that the MoD should not offer indemnities outside of this unless there are exceptional circumstances.

There are no statutory or legal obligations on a contractor to indemnify the government. Indemnities that are given by the contractor result from negotiation, although indemnities included in the initial draft contract issued by the government may not be negotiable depending on which contract award procedure is used.

If the government does request indemnities from the contractor, these are likely to focus on some of the following issues:

- third-party claims for loss or damage to property, or personal injury or death;
- damage to government property;
- product liability claims;
- infringement of a third party's intellectual property; and
- breach of confidentiality.

Some DEFCONs contain indemnities relating to these issues.

**Limits on liability**

10 Can the government agree to limit the contractor's liability under the contract? Are there limits to the contractor's potential recovery against the government for breach?

In principle, the government can agree to limit the contractor's liability under the contract. However, the MoD's policy is to not accept a limit unless it represents value for money. The contract award procedure used by the government will determine the extent to which this position is negotiable.

For certain heads of loss not restricted by statute, the government can limit its own liability under contract. This is unusual but would limit the contractor's potential to recover against the government for breach.

**Risk of non-payment**

11 Is there risk of non-payment when the government enters into a contract but does not ensure there are adequate funds to meet the contractual obligations?

There is a risk of non-payment, as with all customers. However, the MoD's policy, even if the MoD procures under the DSPCR, is to comply with regulation 113 of the Public Contracts Regulations 2015, which requires public sector buyers to pay prime contractors (Tier 1 suppliers) undisputed, valid invoices within 30 days. Generally, the risk of non-payment for an undisputed, valid invoice by the MoD is perceived to be very low.

**Parent guarantee**

12 | Under what circumstances must a contractor provide a parent guarantee?

The government should specify in its initial tender documentation whether it may require a parent company guarantee (PCG). If it is not specified in that documentation, the government should not, in theory, be able to ask for one later in the contract-award process. The government will assess a bidder's financial position during the qualification stage and determine whether it believes the company has the economic and financial capacity to deliver and perform the contract. If it does not believe that this is the case (eg, if a bidder is a special purpose vehicle set up specifically for a contract) then when the successful bidder is chosen, the government will determine whether a PCG is required. The MoD's standard-form PCG is set out in DEFFORM 24.

## DEFENCE PROCUREMENT LAW FUNDAMENTALS

**Mandatory procurement clauses**

13 | Are there mandatory procurement clauses that must be included in a defence procurement contract or that will be read into the contract regardless of their actual inclusion?

There are no mandatory clauses that must be included in a defence procurement contract, and no clauses that will be implied specifically within defence procurement contracts.

However, the Ministry of Defence (MoD) will typically seek to include certain standard clauses in its contracts. Primarily, these are the Ministry of Defence defence conditions (DEFCONs), although the MoD does use other standard forms of contract in certain circumstances. If a particular DEFCON is relevant to the subject matter of a contract, the MoD will typically seek to include that DEFCON.

**Cost allocation**

14 | How are costs allocated between the contractor and government within a contract?

Where the Single Source Contract Regulations 2014 (SSCRs) do not apply, allocation of costs under a contract will be contained in a commercial agreement between the parties, with a fixed or firm price being the most common. Gainshare, painshare or value for money reviews are common in long-term contracts to avoid excessive profits or losses occurring.

Where the SSCRs apply, one of the specified pricing models set out in the SSCRs must be used. These pricing methods are:

- fixed price;
- firm price;
- cost plus;
- estimate-based fee;
- target cost incentive fee; and
- volume-driven pricing.

All of these pricing mechanisms are based on the contract price being the allowable costs incurred or estimated by the contractor plus an agreed profit rate. To be allowable, costs must be appropriate, attributable to the contract and reasonable. This will be assessed by reference to the statutory guidance on allowable costs (published by the Single Source Regulations Office (SSRO) as regulator).

**Disclosures**

15 | What disclosures must the contractor make regarding its cost and pricing?

Where the SSCRs do not apply the cost and pricing information that the contractor must disclose to the MoD is a commercial agreement between the parties. The MoD will often negotiate open-book contractual obligations into its higher value contracts.

Under SSCRs, there are statutory reporting requirements where the contractor is required to report on the costs that it will incur or has incurred in performing the contract. Particularly relevant to contract cost and pricing is the 'contract pricing statement', which is settled on contract signature and sets out the cost information on which the price is agreed. Other reports are also required to be delivered regularly throughout the term of the contract (and at the end) that provide information on the costs actually incurred as the contract progresses.

**Audits**

16 | How are audits of defence and security procurements conducted in this jurisdiction?

Where the SSCRs do not apply, the MoD will not have a statutory audit right but will be reliant on the open book or audit contractual provisions negotiated into the contract.

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Under the SSCRs, there are statutory requirements to keep records in relation to the contract, and the MoD has the right to examine these records.

The MoD's audit right can be exercised at any time, though the MoD guidance sets out when this is likely to be exercised in practice.

**IP rights**

17 | Who gets the ownership rights to intellectual property created during performance of the contract? What licences are typically given and how?

The MoD's policy on the ownership of intellectual property arising under its contracts is that intellectual property will normally vest with the contractor generating the intellectual property, in exchange for which the MoD will expect the right to disclose, use and have used the intellectual property for UK government purposes (including security and civil defence).

This is achieved through the inclusion of intellectual property-related DEFCONs in the contract. These DEFCONs are currently under review – the MoD intends to replace them with a single intellectual property DEFCON, although this new DEFCON would still align with MoD's policy on intellectual property ownership.

MoD policy does specify certain scenarios when it expects that it should own the new intellectual property created by the contractor but, in such cases, the MoD will not unreasonably prevent the contractor from using the skills and expertise developed in carrying out the work without charge for its internal business purposes.

**Economic zones**

18 Are there economic zones or other special programmes in this jurisdiction commonly utilised by foreign defence and security contractors for financial or other procurement related benefits?

We are not aware of any such economic zones or programmes in the UK.

**Forming legal entities**

19 Describe the process for forming legal entities, including joint ventures, in this jurisdiction.

A joint venture could either be a corporate or commercial joint venture.

A corporate joint venture would involve the joint venture parties setting up a new legal entity (likely, a limited company registered in England and Wales), which would be an independent legal entity able to contract in its own right, and which is liable for its own debts. It is relatively straightforward and inexpensive to establish a company: the parties must file a Form IN01 and articles of association at Companies House and pay the applicable filing fee. The company is brought into existence when Companies House issues the certificate of incorporation. The shareholders (joint venture parties) would also likely agree in a shareholders' agreement the roles and responsibilities of each shareholder and their respective obligations to invest capital and resources into the company.

A commercial joint venture does not involve any separate legal entity, and the parties contractually agree each party's roles and responsibilities.

**Access to government records**

20 Are there statutes or regulations enabling access to copies of government records? How does it work? Can one obtain versions of previous contracts?

Under the Freedom of Information Act 2000, there is a general right for the public to access information held by public bodies. As the MoD is a public body, on the face of it this right would extend to contracts and records held by the MoD allowing people to request these documents.

There are exemptions from disclosure under the Act (whether they apply depends on the context):

- for 'information provided in confidence', where disclosure of the information to the public would constitute a legally actionable breach of confidence; and
- under 'commercial interests' subject to a public interest test for information that constitutes a trade secret or where disclosure would prejudice the commercial interests of any person.

MoD policy is to consult with companies when disclosure of information supplied by or related to them is being considered under the Act. Should the MoD decide to disclose information against the wishes of the company, it will notify the company of the decision prior to disclosure.

**Supply chain management**

21 What are the rules regarding eligible suppliers and supply chain management and anti-counterfeit parts for defence and security procurements?

Subject to limited exceptions, the defence procurement rules oblige an authority to reject tenders from bidders who have been convicted of certain serious offences (such as bribery, corruption and fraud). They also give the authority discretion to exclude bidders on other grounds, such as insolvency or gross professional misconduct. The rules expressly permit authorities to consider the same exclusion grounds for sub-contractors, as well as giving them broad rights, for example, to require a supplier to openly compete some of the sub-contracts or to flow down obligations regarding information security.

If the MoD has specific concerns around the robustness of the supply chain (eg, supplier fragility or lack of competition) then it will negotiate contractual provisions with the contractor giving it certain controls or involvement in the supply chain strategy. Detailed quality assurance requirements will also be included in a contract and will cover fraudulent and counterfeit material.

## INTERNATIONAL TRADE RULES

**Export controls**

22 What export controls limit international trade in defence and security articles? Who administers them?

The Trade etc in Dual-Use Items and Firearms etc (Amendment) (EU Exit) Regulations 2019 retains and transposes the EU Dual-Use Regulation 428/2009 into national UK legislation following the end of the transition period on 1 January 2021.

The fundamental UK legislation implementing export controls is the Export Control Act 2002. The Act provides authority for the United Kingdom's government to extend the export controls set forth in the Act through secondary legislation. The main piece of secondary legislation under the Act is Export Control Order 2008, which controls the trade and exports of listed military and dual-use items (ie, goods, software and technology that can be used for both civilian and military applications).

The military and dual-use items captured by the Order are known as 'controlled goods' as trading in them is permitted as long as, where appropriate, a licence has been obtained. Licences are administered by the UK Export Control Joint Unit within the Department for International Trade (DIT). The UK's HM Revenue & Customs is responsible for enforcing the legislation.

**Domestic preferences**

23 What domestic preferences are applied to defence and security procurements? Can a foreign contractor bid on a procurement directly?

If the Defence and Security Public Contracts Regulations 2011 (DSPCR) applies, there is no scope for domestic preferences. However, where article 346 of the Treaty on the Functioning of the European Union (TFEU) has been relied upon to disapply the DSPCR, contracts were commonly awarded to national suppliers.

Within the MoD, the use of article 346 to justify the awarding of a contract without competition required specific approval levels.

**Favourable treatment**

24 Are certain treaty partners treated more favourably?

Only member states of the European Union or signatories of the GPA are able to benefit from the full protection of the DSPCR.

**Sanctions**

25 Are there any boycotts, embargoes or other trade sanctions between this jurisdiction and others?

The UK implements embargoes and (financial) sanctions imposed by the United Nations and may also implement autonomous embargoes and sanctions. All of these embargoes and sanctions are implemented through sanctions regulations, which are based on the Sanctions and Anti-Money Laundering Act 2018. The specific sanctions regulation provides for the enforcement of, and penalties for, breaches of the UK

embargoes and sanctions and for the provision and use of information relating to the operation of those sanctions.

Embargoes and sanctions, depending on their type and ultimate aim, are targeted at individuals, entities, sectors or countries. The current arms-related and financial sanctions can be found on the UK government website. The Department for International Trade (DIT) implements and enforces trade sanctions and other trade restrictions, whereby it is overseen by the Secretary of State for International Trade. Financial sanctions are implemented and enforced by the Office of Financial Sanctions Implementation (OFSI) which is part of the HM Treasury.

**Trade offsets**

26 | Are defence trade offsets part of this country's defence and security procurement regime? How are they administered?

The Ministry of Defence does not use offsets in its defence and security procurement.

## ETHICS AND ANTI-CORRUPTION

**Private sector appointments**

27 | When and how may former government employees take up appointments in the private sector and vice versa?

Civil servants, including those employed by the Ministry of Defence (MoD), wishing to take up an appointment in the private sector are bound by the Business Appointment Rules (the Rules).

For most civil servants, the Rules are triggered in certain circumstances, such as when an individual has been involved in developing a policy affecting their prospective employer, has had official dealings with their prospective employer or has had access to commercially sensitive information regarding competitors of their prospective employer. In these circumstances, the individual must apply for approval from the relevant department before accepting any new appointment for up to two years after the individual leaves the civil service. Approval can be given unconditionally, or can be subject to specific restrictions.

Separate and more onerous obligations apply to senior civil servants (permanent secretaries, SCS3-level employees and equivalents) under the Rules. Similar provisions apply to members of the armed forces, intelligence agencies and the diplomatic service.

These Rules do not have legislative force but, as regulations issued by the Minister for the Civil Service, they are binding on both the government and its employees.

Private sector employees are not subject to any specific regulations governing the commencement of employment by the government. They may, however, be subject to specific restrictions detailed in their employment contracts and should be mindful of any potential conflict of interest.

**Addressing corruption**

28 | How is domestic and foreign corruption addressed and what requirements are placed on contractors?

The Bribery Act 2010 criminalises domestic and overseas bribery in the private and public sectors. It also provides for the corporate offence of failing to prevent bribery.

Giving, offering or agreeing to give a bribe is an offence, as is accepting, asking for or agreeing to accept a bribe. The bribe may be anything of value, whether monetary or otherwise, provided it is intended to influence or reward improper behaviour where the recipient performs public or business functions and is subject to a duty of trust or good faith. When the recipient is a foreign public official, the impropriety requirement does not apply.

Commercial organisations are strictly liable for any primary bribery offences (except receipt of a bribe) committed by anyone performing services on behalf of the organisation. This almost invariably includes employees, agents, intermediaries and other service providers. The organisation has a defence if it has 'adequate procedures' in place to prevent bribery. The Ministry of Justice has issued guidance on what is 'adequate', identifying six principles of bribery prevention:

- risk assessment;
- proportionate procedures;
- due diligence;
- communication and training;
- top-level commitment; and
- monitoring and review.

Prosecution of bribery offences is handled by the Director of Public Prosecutions or the Serious Fraud Office.

**Lobbyists**

29 | What are the registration requirements for lobbyists or commercial agents?

The Transparency of Lobbying, Non-Party Campaigning and Trade Union Administration Act 2014 requires that anyone in the business of consultant lobbying be registered with the Registrar of Consultant Lobbyists. Consultant lobbying includes any personal oral or written communication to a Minister of the Crown or permanent secretary relating to any contract or other agreement or the exercise of any other function of the government. Such a business must then record details of the company and its directors, of any code of conduct that it adopts and, on a quarterly basis, the names of any entities on whose behalf it has actually submitted any communications.

**Limitations on agents**

30 | Are there limitations on the use of agents or representatives that earn a commission on the transaction?

Public sector procurement in the UK is based on free and open competition designed to achieve value for money for the taxpayer, with a high level of transparency of the procurement process and tender terms. Part of the objective is to discourage the perceived benefit of using intermediaries to liaise with government procurement officials and thereby put a given supplier at an advantage. As a result, it is uncommon to use success-fee-based agents and intermediaries as in certain other markets, although some suppliers do use external assistance to help them understand the procurement process. However, there is no general prohibition on the use of agents or on their levels of remuneration, although individual tenders may include specific disclosure requirements.

Registration may be required where the agent's activity falls within the requirements of the Transparency of Lobbying, Non-Party Campaigning and Trade Union Administration Act 2014. The 2014 Act requires anyone in the business of consultant lobbying to register with the Registrar of Consultant Lobbyists. Consultant lobbying includes any personal oral or written communication to a Minister of the Crown or permanent secretary relating to any contract or other agreement or the exercise of any other function of the government. Such a business must then record details of the company and its directors, of any code of conduct that it adopts and, on a quarterly basis, the names of any entities on whose behalf it has actually submitted any communications.

A supplier who appoints an agent within the terms of the Commercial Agents' (Council Directive) Regulations 1993 to develop its presence in a given market may be obliged to pay additional compensation on termination. Otherwise, the 1993 Regulations do not prescribe maximum or minimum levels of remuneration.

## AVIATION

### Conversion of aircraft

31 How are aircraft converted from military to civil use, and vice versa?

Civil aircraft may not fly in Europe unless they comply with the airworthiness regime established pursuant to Regulation (EC) 2018/1139 or, if they fall within Annex I thereto, are approved by individual member states. Regulation 2018/1139 requires a type of certification process in accordance with certification specifications promulgated by the European Aviation Safety Agency (EASA). Annex I permits member states to approve ex-military aircraft unless EASA has adopted a design standard for the type in question. Most military aircraft are designed in accordance with a certification basis that is very different from the civil requirements, so the process of civil certification is often prohibitive. In that event, the Civil Aviation Authority may issue a 'permit to fly' if satisfied that the aircraft is fit to fly with regard to its overall design, construction and maintenance. Ordinarily, such aircraft are unable to conduct commercial air transport operations or to fly outside the United Kingdom. Details governing operations are contained in CAP632 and maintenance standards in BCAR Chapters A8–23 and A8–25, all available from the Civil Aviation Authority.

From 1 January 2021, when the transition period for the UK's departure from the European Union comes to an end, applicable EU law and regulation becomes part of UK law. Regulation 2018/1139 was amended by the Operation of Air Services (Amendment etc) (EU Exit) Regulations 2018 to allow the regime to continue to function and to confer EASA's functions under the regime upon the Civil Aviation Authority from this date.

The UK Military Aviation Authority regulates the certification and maintenance of military aircraft. Since 2010, military processes have been more closely based on the civil airworthiness philosophy than previously, but this is documented and administered separately from the civil process. Accordingly, a similar process is necessary if someone wishes to convert a civilian aircraft for military purposes, whereby the original certification has to be revalidated in accordance with military standards.

### Drones

32 What restrictions are there on manufacture and trade of unmanned aircraft systems or drones?

In September 2018, the new Basic Regulation (EU) 2018/1139 of 4 July 2018 came into force which enabled EASA to assume greater control over the manufacturing and operating of light unmanned aircraft systems (UAS). Hitherto, in Europe, EASA regulation over UAS had been limited to those over 150kg. Those under 150kg were subject to regulation by member states. The Basic Regulation confers powers on the European Commission to adopt implementing and delegated regulations, in accordance with the Essential Requirements at Annex IX to the Basic Regulation, for design, production, operation and maintenance of UAS. These regulations may provide that UAS are not subject to the normal provisions on conventional certification and the role of EASA.

Commission Implementing Regulation (EU) 2019/947 and Delegated Regulation (EU) 2019/945 were published in June 2019, and further amended during 2020. These Regulations establish three categories of UAS operation: open, specific and certified. They concentrate on the details applicable to the open and specific categories. The process for the certified category is expected to borrow heavily from existing manned aircraft standards. The Implementing Regulation contains rules and procedures for the operation of unmanned aircraft including an Annex on UAS operations in the "open" and "specific" categories. The Delegated Regulation prescribes product criteria for UAS for open category use, limits marketing of UAS that do not meet those criteria and governs third-country operators of UAS. Both regulations came into force on 1 July 2019, however, while the Delegated Regulation applies from that date, the Implementing Regulation was initially not to be applied until 1 July 2020. However, as a result of the covid-19 pandemic, application of the Implementing Regulation was postponed until 31 December 2020.

From 1 January 2021, when the transition period for the UK's departure from the EU ends, applicable EU law and regulation became part of UK law. These include the Delegated and Implementing Regulations governing UAS. Regulation 2018/1139 has been amended to allow the regime to continue to function and confer EASA's functions upon the Civil Aviation Authority.

In the UK, most requirements of the Air Navigation Order are disapplied for UAS under 25kg, in favour of the operational rules contained in the Implementing Regulation. Recent changes, on matters such as registration and competency, are compliant with the EU UAS regulations. Additional changes were made to align the UK small UAS regime with the open category of the Implementing Regulation.

UAS specially designed or modified for military use always require a licence for export from the UK. Likewise, a licence is required for export of dual-use UAS as defined in EU and UK regulations. Dual-use UAS include certain UAS designed for beyond line of sight operations with high endurance, with a range over 300km or with autonomous flight control and navigation capability. The general export control regime is supplemented by country-specific measures, such as those in force in relation to Iran.

## MISCELLANEOUS

### Employment law

33 Which domestic labour and employment rules apply to foreign defence contractors?

There are no specific statutory or common law employment rules that apply exclusively to foreign defence contractors, and the parties can choose the governing law that applies to the employment contract. However, regardless of the parties' choice of governing law, certain mandatory laws will apply if the employee habitually works in England or Wales to the extent that they give greater protection than the governing law of the employment contract. These mandatory laws include (but are not limited to):

- the right not to be unfairly dismissed (provided that the employee has two years of service);
- protection from discrimination and from suffering detriments or being dismissed for whistle-blowing (from day one of employment);
- rights to the national minimum wage, a minimum amount of paid holiday and a statutory redundancy payment, where applicable;
- certain maternity and parental rights; and
- rules relating to working hours.

### Defence contract rules

34 Are there any specific rules that contractors, foreign or domestic, are bound by in defence contracts?

The answers above provide the detail of the laws, regulations and policies applicable to the Ministry of Defence (MoD) and defence contractors, most notably the Defence and Security Public Contracts Regulations 2011 (DSPCR) and the Single Source Contract Regulations 2014.

35 Do contractors avail themselves of these rules when they perform work exclusively outside of the jurisdiction?

If a contractor provides goods or services to the UK government, the laws, regulations and policies detailed above will apply even if the work is performed outside the UK.

**Personal information**

36 | Must directors, officers or employees of the contractor provide personal information or certify that they fulfil any particular requirements to contract with a government entity?

Companies will be asked to provide information about their directors and certain other employees as part of the pre-qualification questionnaire process, and will usually be required to sign a 'Statement Relating to Good Standing' certifying that directors and certain other personnel have not been convicted of certain offences.

An awarded contract (or security aspects letter) may require directors or employees to submit to security clearance – so employees' personal information would need to be provided to the MoD in that scenario so that relevant checks could be carried out.

**Licensing requirements**

37 | What registration or licensing requirements exist to operate in the defence and security sector in the jurisdiction?

There are no specific licensing or registration requirements to operate in the defence and security sector in the United Kingdom.

The MoD may impose security requirements, but this is done by treating projects on a case-by-case basis and stipulating particular requirements depending on the nature of the particular project and its degree of sensitivity. Those requirements will typically be included in a security aspects letter that will bind the contractor upon contract award.

**Environmental legislation**

38 | What environmental statutes or regulations must contractors comply with?

Contractors producing or supplying goods and services in, or importing them into, the UK will face different environmental legislation depending on their operations, product or service. Contractors could face regulations encompassing, inter alia, air emissions, water discharges, water pollution, noise and waste disposal, and face responsibility for electrical waste and electronic equipment and restrictions on hazardous substances in such equipment. Applicable requirements may also cover energy efficiency, carbon emissions and energy consumption targets and reporting obligations (eg, the Energy Savings and Opportunity Scheme and the Streamlined Energy and Carbon Reporting Regime). Contractors involved with nuclear substances are subject to a separate or additional set of environmental obligations as well as strict nuclear waste disposal restrictions. Finally, in some circumstances, there are exemptions, derogations or disapplications from environmental legislation for defence and military operations.

39 | Must companies meet environmental targets? What are these initiatives and what agency determines compliance?

There are several areas to consider. First, general targets in legislation such as the Climate Change Act and Renewable and Energy Efficiency Directives will indirectly lead to targets for individual operators through more specific legislation and regulation. Next, for example, the Environment Agency leads on the integrated environmental permitting regime – individual permits are required for specific industrial activities and may impose targets and limits for air emissions, water discharges and so on. Also, for example, the EU Emissions Trading System (managed by the Department for Business, Energy and Industrial Strategy) requires participating companies with, for instance, larger generating capacity or heavy industrial operations to cover their greenhouse gas emissions by surrendering EU Emissions Trading System allowances. Finally, companies may face individual targets (including reducing waste, chemical spills and water consumption) through their own environmental management system or corporate reporting initiatives.

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40 | Do 'green' solutions have an advantage in procurements?

The UK government has mandatory and best practice government buying standards, and a greening government policy that may be required of applicants to public tenders. The government buying standards mostly look to reduce energy, water use and waste when dealing with contracts for transport, textiles and electrical goods, among other things. Under the DSPCR, only environmental issues relevant to the contract itself can be taken into account – not the supplier's wider efforts. In our experience, green solutions do not tend to gain any significant advantage; they do not carry significant weight in evaluation methodologies.

## UPDATE AND TRENDS

**Key developments of the past year**

41 | What were the key cases, decisions, judgments and policy and legislative developments of the past year?

Defence contracting was not immune to the impact of covid-19 as global supply chains were disrupted. However, the United Kingdom's government made a public policy decision to help support its contractors by suggesting that contracting authorities should look for alternatives to terminating or penalising contractors if delay or poor performance arose because of the pandemic.

The impact of Brexit will remain an issue for both UK and non-UK entities, as the UK-EU agreement reached could have a far-reaching

impact on many of the topics covered in this chapter – particularly procurement, labour, trade and export, aviation and the environment.

The Single Source Contract Regulations 2014 (SSCRs) remain a topic of interest as the contract profit rate and reporting requirements in those regulations in particular continue to be reviewed and amended.

**Coronavirus**

42 What emergency legislation, relief programmes and other initiatives specific to your practice area has your state implemented to address the pandemic? Have any existing government programmes, laws or regulations been amended to address these concerns? What best practices are advisable for clients?

In March 2020, a Defence Procurement Policy Note (DPPN 02/20) was released, highlighting the pro-active measures that were being taken to protect 'at risk' suppliers – especially where there was a threat the supplier's financial viability or ability to retain key capabilities. Contractors were able to submit 'interim relief' proposals, which were agreed on a case-by-case basis with the Ministry of Defence (MoD). Such relief proposals would generally involve:

- continued payment to suppliers (notwithstanding any reduced performance) via relief from key performance indicators and service credits;
- extensions of time (so relief from liquidated damages); and
- prompt payment.

Suppliers were then required to flow any of the above-agreed proposals into their supply chains and operate on an open-book basis to show how monies received are being spent (either productively on on-going operations or on employees on effective furlough).

As well as this, there were exceptions to the national 'lockdown' requirements for defence workers, to ensure the continuity of key defence operations and programmes. Although the government introduced the Coronavirus Job Retention Scheme (CJRS) this was not always beneficial to defence contractors, who can only receive one benefit or relief for the same underlying cost. For example, contractors could not claim employees wages under the above interim relief scheme and the CJRS and CJRS monies could also not be claimed for employees funded by government monies (eg, for employees working directly on government programmes).

These initial measures are likely to be scaled back in line with the reduction in benefits available from other government relief schemes. The June 2020 Procurement Policy note acknowledges that relief provisions may still be appropriate, but calls for authorities and contractors to work in partnership to 'develop transition plans to exit from any relief as soon as reasonably possible'.

Contractors might rely more heavily on contract terms, for example, whether covid-19 or its consequences can be classed as force majeure events (although note that the MoD standard definition of a force majeure event still excludes pandemics). It would also be useful to look to see if other provisions help (eg, Relief Events, Change in Law and service credit relief).

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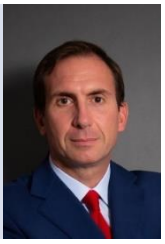

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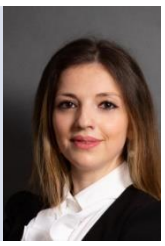


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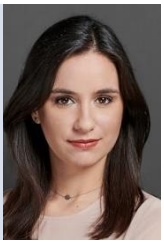

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