

Merger between British Aerospace plc and the Marconi Electronic Systems business of the General Electric Company plc: request for variation

Undertakings given by British Aerospace plc (subsequently re-named BAE SYSTEMS PLC) to the Secretary of State for Trade and Industry on 28 March 2000.

Advice given to Secretary of State 18 December 2006

1. In this submission the OFT advises under section 75J of the Fair Trading Act following a review of the above undertakings.

RECOMMENDATION

2. Following consideration of the representations made by BAE SYSTEMS plc (BAE SYSTEMS), the Ministry of Defence (MoD) and the responses to the consultations held on this issue, the OFT recommends the following:
 - a. the provisions of Undertaking 9 be retained (save for replacing the reference to the 'DGFT' with the 'OFT') but superseded and re-numbered as necessary in a new instrument (see 3 below);
 - b. the information retention provisions of Undertakings 2 and 5 be retained but superseded and re-numbered as necessary in a new instrument (see 3 below);
 - c. the supporting Undertakings 1, 16 and 17 be revised to reflect the changes and superseded and re-numbered as necessary in a new instrument (see 3 below); and
 - d. the other Undertakings (Undertakings 4, 6, 7, 8, 10, 11, 12, 13, 14 and 15) be released.
3. For practicality, in view of the substantial changes that would result, the OFT is recommending that the changes recommended in a, b and c above, if accepted, are brought together within a new single

replacement set of undertakings that supersedes the Undertakings rather than seeking to further amend the document containing the Undertakings given in 2000. The changes recommended in d above would, if accepted, be effected by way of issue of a release.

Timing

4. Due to the impending departure of the current Compliance Officer, the new suggested compliance regime would, if accepted, need to be in place by 1 January 2007.

Transparency

5. We propose to publish this advice in due course.

Background

6. On 28 March 2000, the then Secretary of State for Trade and Industry, Steven Byers, announced that he had accepted undertakings (the Undertakings) in lieu of reference to the Competition Commission under section 75G of the Fair Trading Act 1973 (the Act) from British Aerospace plc (subsequently re-named BAE SYSTEMS) to remedy competition and other public interest concerns arising from the acquisition by BAE SYSTEMS of the Marconi Electronic Systems business (MES) of The General Electric Company, plc. The Undertakings include measures to safeguard competition at prime contractor and subcontract level and to address national security concerns.
7. The Undertakings have been changed on two occasions. On 10 January 2002, BAE SYSTEMS was released from undertaking 3. This applied to a UK / US jointly funded competition to design a ground-based reconnaissance vehicle (TRACER). The purpose of the undertaking was to address the competition concerns arising from the fact that BAE SYSTEMS and MES were members of competing teams bidding for this same contract. The UK and US governments subsequently decided not to proceed with the programme and the undertaking became redundant.
8. On 29 September 2005 the Undertakings were varied to allow the extension of the current Compliance Officer's (CO) 5-year term of appointment. The CO's term of appointment was subsequently extended by BAE SYSTEMS to 31 May 2006 and has subsequently

been extended until 31 December 2006. The CO's role is to facilitate and oversee compliance with the Undertakings and report to the Ministry of Defence (MoD) and the OFT on compliance.

9. As you are aware, the Undertakings have not been transferred to the OFT under the provisions of the Enterprise Act 2002 and responsibility for the Undertakings remains with the Secretary of State for Trade & Industry. The role of the OFT is to keep the Undertakings under review and advise on the Undertakings¹ but the decision-making role on matters relating to the Undertakings lies with the Secretary of State.

BAE SYSTEMS request for review

10. BAE SYSTEMS requested that the OFT review the Undertakings accepted on 28 March 2000 with a view to releasing BAE SYSTEMS from all (or substantially all) of the Undertakings. If, consequent to the advice of the OFT on the matter, the Secretary of State considers that the Undertakings (or part of them) are no longer appropriate by reason of any 'change of circumstances',² BAE SYSTEMS can be released from them (or part of them) or the Undertakings (or part of them) can be varied or superseded.
11. Since acceptance of the Undertakings in 2000 a number of changes have taken place both to BAE SYSTEMS as a company and within the defence industry (in the UK and worldwide) which, BAE SYSTEMS contends, have had an impact on the scale and scope of the matters covered by the Undertakings as well as, in some cases, the Undertakings themselves.

Consultation

12. On 9 February 2006, the OFT launched a public consultation on the question of whether the Undertakings were still appropriate or need to be varied or superseded, or whether BAE SYSTEMS could be released from them. A total of seven responses were received to the consultation. Some respondents considered that despite changes and developments in the UK defence sector over the last few years, the Undertakings remain relevant particularly as BAE SYSTEMS maintains a strong position in certain key capabilities where it is the owner and / or guardian of important UK technology or where it controls access to

¹ Section 75J of the Act continues to apply for the purposes of the Undertakings by virtue of the Enterprise Act 2002, section 276(1) and Schedule 24, paragraph 13(1).

² Section 75J(a) of the Act.

key capabilities. A number of respondents did however recognise that changes in the sector had made a case for removal of some if not all of the Undertakings. The MoD, through the Defence Procurement Agency, have also provided their views as part of the consultation process.

13. On 20 November, the OFT launched a further consultation outlining its provisional view on the outcome of the review. This provisional view was, in material respects, as outlined at paragraph 2 above. A total of three responses to this consultation were received. Where appropriate, substantial comments are addressed below.

Summary

14. The OFT considers that, in accordance with section 75J(a) of the Act, a change of circumstances has occurred which justifies the release or variation of the majority of the Undertakings. The only undertaking which it is recommended is retained in its entirety is Undertaking 9 (save for replacing the reference to 'DGFT' with the 'OFT'). The change of circumstances which justifies the release or variation of each Undertaking is discussed in relation to each Undertaking in the text below.

The undertakings

Undertaking 1

15. Undertaking 1 required BAE SYSTEMS to appoint a CO to facilitate and oversee compliance with the Undertakings and report to the MoD and the OFT on compliance. This has been an important role in terms of the implementation of and compliance with the Undertakings. This role was considered particularly crucial when the Undertakings were accepted in view of their breadth and depth and the fact that they required certain behavioural and structural changes to businesses carried on by BAE SYSTEMS. In this connection, the Interim Compliance Officer and current CO have set up internal compliance practices and procedures to ensure that the requirements within the Undertakings are embedded within the structure of the organisation.
16. Key questions raised by this review are i) whether, in light of any proposed changes to the Undertakings, a CO is required in the future and ii) if a CO is required does the CO need to be an external candidate independent of BAE SYSTEMS. Given the changes of

circumstances for the purposes of the test in section 75J of the Act referred to below which lead to the recommendation to release BAE SYSTEMS from the majority of the Undertakings, the OFT considers that the compliance role in relation to the remaining undertakings (as will be amended) can be fulfilled by an internal BAE SYSTEMS appointment. The CO will continue to act as a first port of call for any businesses who consider that BAE SYSTEMS is not complying with the Undertakings and will undertake his or her own investigation of any such complaints. The OFT will continue to act as final arbiter, subject to review by the courts, in the event of dissatisfaction with the findings of the CO. The OFT therefore recommends that in view of the changes of circumstances for the purposes of the test in section 75J of the Act justifying the changes to the Undertakings, Undertaking 1 should be revised to reflect the changes and superseded and re-numbered as may be necessary in a new instrument (see 3 above).

17. For consideration of the remaining Undertakings there is some merit in splitting their assessment between the various matters which they are designed to cover, beginning with the Undertakings covering the specific competitive programmes which were in place in 2000.

Competitive programmes

Undertakings 2, 4 and 5

18. These undertakings concerned the competitive programmes for: Joint Strike Fighter; Skynet 5 and associated satellite communications programmes; and the Astute Training Programme respectively. As with Undertaking 3, the purpose of these undertakings was to address the competition concerns arising from the fact that BAE SYSTEMS and MES were members of competing teams bidding for the same contracts. The competitive programmes covered by these undertakings have now been decided and these undertakings (apart from the information retention provisions) are no longer in effect. The OFT considers that this is a 'change of circumstances' for the purposes of the test in section 75J of the Act and the Undertakings should be revised to reflect this fact. The OFT therefore recommends that the information retention provisions of Undertakings 2 and 5 be retained but superseded and re-numbered as may be necessary in a new instrument (see 3 above). The relevant provisions of the Undertakings accepted in 2000 are referred to, but not reproduced, in the new Undertaking so that the information retention provisions can be understood in context should it prove necessary. As BAE

SYSTEMS withdrew from the bid in relation to Skynet 5, this constitutes an additional 'change of circumstances' for the purposes of the test in section 75J of the Act such that the OFT believes that there is no need for the continued operation of the information retention provisions of Undertaking 4.

The shipyards

Undertaking 6

19. Undertaking 6 relates to MES shipyards and requires the shipyards to be vested in a separate subsidiary of BAE SYSTEMS, with its own management and published accounts, and to be available to all potential prime contractors (including BAE SYSTEMS) on fair, reasonable and non-discriminatory terms. BAE Systems Marine Limited was established as the separate subsidiary holding the Shipbuilding Business and Shipbuilding Assets of BAE SYSTEMS. The rationale for undertaking 6 was to counteract the reduction in competition in naval ship prime contracting. In effect it separated the Prime Contract Offices (PCOs), located within BAE SYSTEMS, from the shipbuilder with the PCO providing an independent prime contract service for the MoD.
20. BAE SYSTEMS has argued that this forced separation has adversely affected the project management of its programmes and led to cost and other inefficiencies. As a result BAE SYSTEMS formed, with MoD's knowledge and consent, two dedicated BAE SYSTEMS business units for shipbuilding: a 'Submarines' business unit specialising in the design and construction of submarines; and a 'Naval Ships' business unit to build surface ships. This new structure also put responsibility for the management of the PCO function under the Managing Director of the relevant shipbuilding business unit. The composition of the shipbuilding business units and management arrangements are no longer fully compliant with Undertaking 6. However, BAE SYSTEMS contends that the shipbuilding business units have remained compliant with Undertakings 7, 9 and 10 and no complaints have been received either by BAE SYSTEMS or the CO³ from any third parties concerning these organisational changes (which have been made public).
21. Undertaking 6 also requires separate accounts to be produced for the shipbuilding business (in part to monitor arm's length trading), and

³ It is also the case that the OFT has not received any complaints.

- provides for access by third parties to the shipbuilding business capabilities when bidding into new programmes as well as the preservation of confidentiality as regards commercially sensitive or competition-sensitive business or financial information. BAE SYSTEMS has been fully compliant with this requirement of the Undertaking.
22. In response to the first consultation, one third party drew particular attention to the continued importance of Undertaking 6 since, it said, the concentration of UK naval shipbuilding capacity in BAE SYSTEMS ownership is no less today than it was in 2000. However, the BAE SYSTEMS / MES transaction did not, in itself, impact on the concentration of UK naval shipbuilding capacity and therefore the OFT believes that such issues are not relevant to the consideration of Undertaking 6. The Undertaking is primarily seeking to address the reduction in competition at the naval ship prime contracting level. In line with this, both the MoD and BAE SYSTEMS have drawn the OFT's attention to developments in the project management solutions now adopted by MoD and which they contend, when combined with the impact of new competition at the relevant levels of the industry, amount to a change of circumstances which warrants release from Undertaking 6.
23. From detailed discussions with the MoD it is clear that, unlike in 2000, competitive whole ship design and manufacture prime contracting is no longer considered to be the primary option for UK naval procurement. In recent years the MoD has developed alternatives to the concept of prime contractor, such as the role of 'Lead Systems Integrator' ('LSI') and 'Alliancing'. The LSI while tasked with overall project management responsibility for a programme, plays a much less significant role in the overall project than a prime contractor and has allowed the MoD to introduce competition for project management from a wide range of companies as the LSI will often not have core defence capabilities. By contrast, a traditional prime contractor would retain core domain skills and would traditionally expect to carry out approximately 30 per cent of a programme's industrial work as a result of its vertical link.
24. Alliancing is a project management option that has been developed in the oil and construction sectors and is now used by MoD. An example is the Future Carrier (CVF) project which is being pursued through the CVF Alliance made up of MoD, KBR, Thales, Babcock, BAE SYSTEMS and Vosper Thornycroft (VT) and involves a modular ('block') approach to shipbuilding with work on individual blocks distributed across a number of suppliers including the shipyards of Babcock, BAE

- SYSTEMS and VT. The MoD selects Alliance partners on the basis of strength and expertise and risk and reward is shared amongst members and linked to overall project success. This contrasts with the traditional prime contractor role where the Prime Contractor would assume overall responsibility and liability. Within the Alliance no one entity has overall control and individual members are required to commit to operate in the overall best interests of the project. In this case the benefit of any vertical linkage is removed by the spreading of rewards amongst the Alliance participants.
25. In terms of an overview it can be considered that adoption of the above options shows the MoD moving away from vertically linked project management options towards more horizontal or co-operative options. As well as limiting the potential benefits of vertical linkages, one further effect of this has been to increase the level of competition at the project management level and allows MoD to draw on the project management expertise of companies without significant direct defence experience as well as established defence players.
 26. As stated in its Defence Industrial Strategy White Paper of December 2005, the MoD will now look beyond the UK for shipbuilding capabilities. The effect of this policy change is that the MoD will now build naval ships in the UK to the extent it is necessary to sustain the ability to design and physically integrate complex warships. In a different approach from that taken when the Undertakings were accepted in 2000, non-complex naval vessels and complex warships in excess of that necessary to sustain a sovereign UK capability may be procured off shore.
 27. Taken together the OFT considers that the above changes in the MoD's procurement processes in the shipbuilding sector amount to a 'change of circumstances' for the purposes of the test in section 75J of the Act which would justify releasing BAE SYSTEMS from Undertaking 6.1-6.7 since it removes the concerns leading to the requirement to establish a separate Shipbuilding Subsidiary. In consequence, the information flow restrictions (in Undertaking 6.11) associated with the requirement to establish a separate Shipbuilding Subsidiary would no longer be appropriate and, therefore, BAE SYSTEMS should be released from Undertaking 6.11.
 28. Undertaking 6 also contains provisions relating to vertical concerns regarding continued access to shipbuilding capacity for the purposes of an MoD programme by other potential prime contractors (Undertaking 6.8-6.10 and 6.12). If accepting that BAE SYSTEMS

should be released from the requirement to establish a separate Shipbuilding Subsidiary, then Undertakings 6.8-6.10 and 6.12 will, effectively, mirror those requirements and obligations which are contained in Undertaking 9 and which will continue to apply to BAE SYSTEMS' shipbuilding capacity. Therefore, upon release of Undertakings 6.1-6.7 and 6.11 there appears to be no requirement to retain Undertakings 6.8-6.10 and 6.12.

29. In response to the second consultation one third party commented that as prime contracting has not been entirely precluded by the MoD then the reasons for the imposition of Undertaking 6 remain. The MoD comment that prime contracting may remain an option for some future programmes but, as noted above, other procurement options are now also available (as used in the CVF project for instance). MoD also comment that the retention of Undertaking 9 would allow third parties to use, under exactly the same terms as have existed since 2000, BAE SYSTEMS' resources required to bid for or perform contracts for the purposes of an MoD programme. Noting those comments and referring also to the policy change introduced in the December 2005 Defence Industrial Strategy White Paper of the MoD looking beyond the UK for shipbuilding capacity, the OFT remains of the view that Undertaking 6 should be released.

Undertaking 13

30. Undertaking 13 which covered the maintenance of capacity at the Clyde Shipyards is no longer relevant as the design and build contract for the Type 45 Warship has now been awarded. Given this 'change of circumstances' for the purposes of the test in section 75J of the Act the Undertaking can be released.

General competition

31. Undertakings 7, 9 and 10 (Teaming, Access to in-house suppliers and Subcontract competition respectively) are behavioral undertakings, relating to BAE SYSTEMS' approach to new business with MoD, or choice of sub-contractors for MoD programmes. The Undertakings were given to address concerns that BAE SYSTEMS' position would allow it to unduly influence the market. BAE SYSTEMS submits that in light of the significant changes in the defence industry and MoD's procurement practices since 2000 the Undertakings are no longer necessary.

Undertaking 7

32. The purpose of undertaking 7 is to ensure that for future MoD competitions, BAE SYSTEMS and a third party do not form a single team to bid as prime contractor without first consulting with MoD. The aim of this undertaking was to reduce the potential for collapsing competitions during the bidding phase where there was a restricted field of bidders. Due to the increase in project management options since the Undertakings were accepted, while the concern over collapsing competitions remains, such concerns now exist in all competitions and is not something specific to those where BAE SYSTEMS alone is involved.⁴ On the basis of the foregoing, the OFT considers that, for the purposes of the test in section 75J of the Act, there has been a 'change of circumstances' which would justify releasing BAE SYSTEMS from Undertaking 7.

Undertaking 9

33. Under this Undertaking BAE SYSTEMS is required to make available, on request and on fair, reasonable and non-discriminatory terms, its capabilities to other prime contractors or potential contractors to permit them to undertake or bid for work on MoD programmes. The purpose of this undertaking is to ensure that other prime contractors have access to the resources of BAE SYSTEMS, since without such access other actual or potential prime contractors may be unable to bid for or perform contracts for the purposes of a MoD programme.
34. BAE SYSTEMS contend that the underlying concern regarding access to BAE SYSTEMS in-house suppliers is now redundant for the following reasons:
- i. the main vertical links created by the BAE SYSTEMS / MES transaction, namely in the avionics sector, have been removed;
 - ii. changes to MoD procurement models which have resulted in moves away from the traditional horizontal / prime contractor model limit the economic benefits of being a vertically integrated defence contractor due to the more collegiate approach fostered in the new procurement models (such as LSI or Alliancing) which spread risk, reward and decision making through the participants; and

⁴ In this respect it is noted that the MoD now has a model clause for Invitation to Tender documentation which adopts the requirement in Undertaking 7 for all potential prime contractors.

- iii. the increased protection available as a result of changes to competition law (namely the Competition Act 1998) which mirrors the protection provided by the Undertakings.
35. While noting (i) and (ii), the OFT considers that BAE SYSTEMS still retains a significant amount of production capacity in the UK defence industry, and while changes have occurred (in both avionics and the MoD's procurement practices for instance) the requirement for the Undertakings remains due to the concentration of UK defence manufacturing capacity in sectors such as warship-building, combat aircraft and general munitions. There has been much third party support for the retention of this Undertaking in both consultations and the MoD considers that it should be retained in order to protect the potential for effective competitions where BAE SYSTEMS controls production capacity in the sector. Weighing up all these factors, the OFT considers that this undertaking should be retained (save for replacing the reference to the 'DGFT' with the 'OFT') but superseded and re-numbered as may be necessary in a new instrument (see 3 above). The OFT does not believe that the application, or otherwise, of the provisions of the Competition Act 1998 to activities which are also brought within these Undertakings is relevant to the review of these Undertakings.

Undertaking 10

36. The purpose of this Undertaking was to address general concerns about vertical integration arising from the merger, including in avionics and naval shipbuilding. BAE SYSTEMS as a prime contractor could favour its in-house suppliers to the detriment of competition at the sub-contract level. By agreement with MoD, the CO's verification activities under this Undertaking have been restricted to sub-contracts placed competitively at the first level relevant to a prime contract (i.e. those contracts placed directly by a prime contractor onto a sub-contractor).
37. At the time of the merger, BAE SYSTEMS was the most vertically integrated supplier in the UK defence sector, and the Undertaking was put in place to ensure that MoD could monitor and control such a situation. In terms of the 'change of circumstances' test in section 75J of the Act, changes in the UK defence sector have lessened the pre-eminence of BAE SYSTEMS in terms of vertical integration (see references to Avionics below) which, together with the wider drive for value for money in defence acquisition, has led the MoD to impose

industry wide codes of practice which impose the same requirements on all players in the sector. Such contracts cover sub-contract competition and allow the MoD to set out the requirements for sub-contract competition as part of the contract. On the basis of these facts, the OFT considers that there has been a change of circumstances justifying the release of Undertaking 10.

Avionics business

Undertaking 8

38. This required the former MES Avionics Business to be vested in a separate subsidiary of BAE SYSTEMS, with its own management and published accounts, and to be available to all potential prime contractors (including BAE SYSTEMS) on fair, reasonable and non-discriminatory terms. The concern in 2000 was that BAE SYSTEMS' ownership and control of the business would create vertical concerns relating to BAE SYSTEMS' ability as a prime contractor to prefer its in-house avionics business.
39. Since 2000, BAE SYSTEMS' avionics business has gradually been either sold or transferred out of UK control and in each case the MoD has consented to the transfer of the assets of the Avionics Business. Parts of the business (Air Data Computers and the Data Acquisition Products businesses) were sold to Meggitt plc in June 2002. In January 2003 the Inertial Systems Division was transferred to the control of BAE Systems N.A. In June 2003 the Avionics Systems Division was also transferred to the control of BAE Systems N.A.
40. BAE SYSTEMS has sold off its remaining economic interest in the Avionics Business in two separate stages. In early 2005, BAE SYSTEMS sold 100 per cent of its stake in the Avionics Business in exchange for cash and a 25 per cent interest in SELEX SpA (SELEX), which now wholly owns both the BAE SYSTEMS avionics subsidiary and the avionics assets of Finmeccanica SpA (Finmeccanica). Finmeccanica holds the remaining 75 per cent interest in SELEX. BAE SYSTEMS states that its interest in retaining the 25 per cent stake was effectively a right to receive proceeds of sale of the 25 per cent interest upon exercise of the put or call option (the put option to be exercised by 30 May 2007).
41. BAE SYSTEMS has confirmed that it is party to arrangements under which the 25 per cent interest will be disposed of by no later than May 2007 and that it is not entitled to any board representation in

SELEX, has no other rights which would allow BAE SYSTEMS to influence key business decisions and, except in the ordinary course of business between third parties, BAE SYSTEMS has no right of access to confidential information of SELEX. BAE SYSTEMS Annual Report for 2005 states that the BAE SYSTEMS group is treating the remaining amount of consideration 'as deferred consideration' as it does not exercise any control or significant influence.

42. BAE SYSTEMS asserts that it retains no management control or influence over the avionics business which is the subject of the Undertaking and no vertical link exists between BAE SYSTEMS and the Avionics Business.
43. Given the above facts, the OFT is of the view that BAE SYSTEMS no longer has control or material influence over any of the Avionics Business or its assets for the purposes of section 65 of the Act and therefore this amounts to a 'change of circumstances' for the purposes of the test in section 75J of the Act which would justify releasing BAE SYSTEMS from Undertaking 8.

Ancillary provisions

Undertaking 11

44. This Undertaking covers access to Intellectual Property Rights and Technical Information for Follow-on Work. BAE SYSTEMS and MoD have confirmed that they entered into the agreement containing the Principles of Agreement specified in the Undertaking on 25 May 2000 and they consider the Undertaking is no longer required. However, the mere fact that the agreement has been entered into does not necessarily mean that the undertaking can fall away. For example, if the undertaking is released and the MoD and / or BAE SYSTEMS subsequently terminate or vary the agreement in a way that is inconsistent with the undertaking (in particular the principles set out in Annexe B of the Undertakings), the protection of the undertaking will have been lost. However, no complaints or issues have arisen about this arrangement in our consultation and as BAE SYSTEMS and the MoD appear to be the only parties affected by this undertaking and both of them no longer require the undertaking, the OFT considers that the foregoing amounts to a change of circumstances such that this undertaking could be released.

Undertaking 12

45. The undertaking requires BAE SYSTEMS to assist MoD in obtaining competitive tenders for JTIDS support or further production by entering into licensing agreements with other companies designated by the MoD. This obligation relates to a technology for which it is no longer expected that there will be any scope for new competitions given the maturity and nature of the product. Therefore given this 'change of circumstances' for the purposes of the test in section 75J of the Act the undertaking can be released.

Undertaking 14

46. This undertaking requires BAE SYSTEMS to consult the MoD on any proposals for redeployment of engineering staff or reduction in the range of technical competencies currently available. Changes in the Defence sector in the UK referred to earlier in this document have lessened the importance of this Undertaking. The need to monitor the capability and capacity of all prime contractors has led MoD to establish detailed Key Supplier Management processes (including contractual arrangements relating to the monitoring of staff deployments) and also placing a stronger emphasis on closer relationships with industry players. Taken together, these factors allow MoD to have good access to company staffing information as and when required and it is no longer the case that BAE SYSTEMS needs to be considered as a special case with, compared to other players, additional reporting requirements on such matters backed up by statutory undertakings. Given these factors, the OFT considers that there has been a 'change of circumstances' for the purposes of the test in section 75J of the Act to justify the release of Undertaking 14.

Undertaking 15

47. This undertaking requires BAE SYSTEMS to take on all Parent Company Guarantees that GEC had given to the MoD in respect of MES contracts. Action to satisfy this requirement was confirmed in March 2002 and the undertaking is no longer required and given this 'change of circumstances' for the purposes of the test in section 75J of the Act the undertaking can be released.

Undertakings 16 and 17

48. Undertakings 16 and 17 exist only to support, clarify and ensure compliance with the substantive Undertakings and therefore the OFT recommends that in view of the 'change of circumstances' for the purposes of the test in section 75J of the Act justifying changes to the Undertakings, they be revised to reflect the changes and superseded and re-numbered as may be necessary in a new instrument (see 3 above).

CONCLUSION AND RECOMMENDATION

49. Following the request for a review from BAE SYSTEMS, the OFT has consulted widely with interested parties, including the MoD, which is the main UK customer of BAE SYSTEMS. We have consulted on the basis of the proposal outlined, in all material respects, at paragraph 2 above and have not received any comments during this second consultation which led the OFT to change the proposal.
50. Taking account of the views expressed during the consultation and the changes which have occurred in the defence sector since the undertakings were adopted, and which in the majority of Undertakings amounts to the 'change of circumstances' for the purposes of the test in section 75J of the Act discussed in relation to each Undertaking above, the OFT therefore recommends the following:
- a. the provisions of Undertaking 9 be retained (save for replacing the reference to the 'DGFT' with the 'OFT') but superseded and re-numbered as necessary in a new instrument (see 51 below);
 - b. the information retention provisions of Undertakings 2 and 5 be retained but superseded and re-numbered as necessary in a new instrument (see 51 below);
 - c. the supporting Undertakings 1, 16 and 17 be revised to reflect the changes and superseded and re-numbered as necessary in a new instrument (see 51 below); and
 - d. the other Undertakings (Undertakings 4, 6, 7, 8, 10, 11, 12, 13, 14 and 15) be released.
51. For practicality, in view of the substantial changes that would result, the OFT is recommending that the changes recommended in a, b and c above, if accepted, are brought together within a new single replacement set of undertakings that supersedes the Undertakings rather than seeking to further amend the document containing the

Undertakings given in 2000. The changes recommended in d above would, if accepted, be effected by way of issue of a release.

52. I recommend that you accept the revised undertakings by way of a new instrument as suggested above and attached to this advice. BAE SYSTEMS has already signed the undertakings to indicate its willingness to give such revised undertakings. Although this is helpful, this obviously does not fetter your decision whether to accept them or not.