

TO: SECRETARY OF STATE FOR TRADE AND
INDUSTRY

FROM: SIMON PRITCHARD, DIRECTOR MERGERS,
OFFICE OF FAIR TRADING

10 April 2007

**Anticipated acquisition by General Electric Company (GE) of the
aerospace business of Smiths Group plc (Smiths Aerospace)**

A REPORT TO THE SECRETARY OF STATE FOR TRADE AND
INDUSTRY PURSUANT TO ARTICLE 4(2)-(5) OF THE
ENTERPRISE ACT 2002 (PROTECTION OF LEGITIMATE
INTERESTS) ORDER 2003¹

1. This report is made following the European intervention notice (the Notice) given to the OFT by the Secretary of State for Trade and Industry on 20 March 2007 pursuant to section 67(2) of the Enterprise Act 2002 (the Act).

JURISDICTION

2. This transaction falls for consideration under the EC Merger Regulation (ECMR)². Although the European Commission has sole jurisdiction to investigate the competition aspects of the merger under the ECMR, Member States may exercise their residual power under Article 21(4) of the ECMR to take appropriate measures to protect legitimate interests others than those taken into consideration by the ECMR and compatible with the general principles and other provisions of Community law. The second paragraph of Article 21(4) states that public security shall be regarded as a legitimate interest.
3. As a result of this transaction arrangements are in progress by virtue of which a concentration with a Community dimension (within the meaning of Article 1(2) of the ECMR) will arise and in relation to which a reference under section 33 of the Act which would otherwise have been possible, is prevented from being made by virtue of Article 21(3) of the ECMR. The OFT therefore believes that it is or may be the case that arrangements are in progress or in contemplation which if carried into effect will result in the creation of

¹ S.I. 2003/1592.

² Council Regulation (EC) No 139/2004 on the control of concentrations between undertakings.

a European relevant merger situation within the meaning of section 68(2) of the Act.

4. You may therefore make a reference to the Competition Commission (the CC) under Article 5(3) of the Enterprise Act 2002 (Protection of Legitimate Interests) Order 2003 (the Order) to address public security concerns arising from the merger provide that you believe that the conditions set out in Article 5(3) of the Order are satisfied.

THE PARTIES

5. **GE Aviation UK** is a UK subsidiary of **General Electric Company (GE)**, a company incorporated in the United States of America. GE is a diversified industrial corporation which is active in numerous fields, including manufacturing, technology and services.
6. The Target is the aerospace business of **Smiths Group plc**, a company incorporated in England and Wales, (**Smiths Aerospace**). Smiths Aerospace is active in the supply of various types of aerospace systems and equipment. It has critically important capabilities within the UK in the areas of combat, weapon and communications system integration and research capabilities.

THE TRANSACTION

7. The Transaction relates to the anticipated acquisition of Smiths Aerospace by GE.

SUMMARY OF THIRD PARTY REPRESENTATIONS

8. Following receipt of the Notice, the OFT has consulted and invited comments on any national security concerns raised by interested parties. In response to the consultation, the Ministry of Defence (MoD) made the representations on national security issues which are summarised below.
9. The MoD has identified three main areas of concern arising from this European relevant merger situation: the transfer of ownership of Smiths Aerospace outside the UK, the maintenance of strategic UK capabilities and the protection of classified technology and information.
10. Regarding the transfer of ownership of Smiths Aerospace, the MoD has stated that GE may be able to influence Smiths Aerospace in ways that could prejudice national security unless the MoD obtains assurances over certain aspects of its behaviour.

11. With regard to the maintenance of strategic UK capabilities, the MoD has stated that Smiths Aerospace is a key supplier of sub-systems for a number of important current and future weapons platforms, including the Typhoon combat aircraft, Future Lynx helicopter and Taranis experimental Unmanned Combat Air Vehicle.
12. The MoD states that it is essential for the protection of the UK's national security that these capabilities are retained within the UK to develop, operate and maintain weapon systems incorporating the technologies that Smiths Aerospace provides, independently of other nations. The MoD submits that without retaining such capabilities within the UK, the UK will be unable to maintain the operational advantage that our armed forces gain from having unique, technologically-advanced equipment.
13. The MoD is also concerned that the move to US control may create difficulties due to the US International Traffic in arms Regulations (US ITAR) which would have profound implications for UK security of supply if UK information and technology was combined with US information and technology without UK knowledge or approval.
14. The MoD believes that it is necessary to obtain an assurance from GE that it will continue to make available to the UK the capabilities that Smith Aerospace possesses in these areas, and that, in the event of any proposed rationalisation by GE, such capabilities will be maintained within the UK and neither run down, nor transferred abroad, following the Transaction without prior consultation with the MoD.
15. In relation to the protection of classified technology and information the MoD notes that the above described capabilities are dependent, to different extents, on classified technology and information. Much of the information is available only to UK nationals and may therefore bear a UK EYES ONLY caveat. The 'leakage' of such information or technology outside the UK could directly prejudice the UK armed forces' operational security and capability.
16. If Smiths Aerospace, under the ownership and control of GE, were to continue its involvement in such work, it would be necessary to ensure that such information was retained and protected within the UK. The MoD considers legally binding undertakings from GE (combined with an appropriate compliance regime) would be necessary to assure the UK government that sensitive information and technology is adequately protected.

Undertakings in lieu

17. The MoD has identified national security concerns arising from the transaction. If you believe that the concerns raised by the MoD may be expected to operate against the public interest, you may either make a reference to the CC under Article 5(3) of the Order or accept undertakings in lieu of such a reference under paragraph 3(2) of Schedule 2 to the Order.
18. The draft undertakings in the attached appendix are intended to remedy, mitigate or prevent the particular effects adverse to the public interest identified by the MoD which may be expected to result from the creation of the European relevant merger situation. Specifically, the undertakings seek to address the areas of concern identified above.
19. GE and Smiths Aerospace have confirmed that they are willing to give the undertakings in the form attached in the appendix. They have signed the undertakings to indicate acceptance but this is, of course, without prejudice to your final decision.

Conclusions on national security considerations

20. The OFT is not expert in national security matters and therefore merely summarises here representations made by the MoD.
21. The OFT has no reason to doubt the representations made by the MoD on the appropriateness of the undertakings in order to remedy or prevent the specific effects adverse to the public interest identified by it and which are briefly described above.

CONCLUSIONS

22. The OFT advises you that it is or may be the case that arrangements are in progress or in contemplation which if carried into effect will result in the creation of a European relevant merger situation for the purposes of section 68(2) of the Act.
23. It appears that this transaction raises national security concerns identified by the MoD in its submission to the OFT. If you believe that as a result of this transaction a European relevant merger situation will be created; the national security consideration specified in the Notice is relevant to the merger; and, taking account only of the national security concerns raised, the merger may be expected to operate against the public interest, you can make a reference to the Competition Commission on such public interest grounds, or accept undertakings in lieu of such reference. The MoD has prepared undertakings, to be accepted in lieu of reference to the Competition

Commission, which it believes are the most effective means of remedying the national security concerns it has identified.

24. Following discussions with MoD and OFT officials, GE and Smiths Aerospace have confirmed that they are prepared to give the attached draft undertakings and have signed them to indicate acceptance. However, this does not fetter your discretion in determining whether to accept the proposed undertakings in their current form, or in a modified version, if found appropriate following public consultation.



Simon Pritchard
Director, Mergers Group
Office of Fair Trading