



Australian Government

Australian Government response to the
Joint Standing Committee on Foreign Affairs,
Defence and Trade report:

Principles and Practice – Australian Defence
Industry and Exports

April 2016

Recommendation 1

The Committee recommends that the Department of Defence incorporate into policy, doctrine, procurement instructions and all associated training the addition of defence industry as the ninth fundamental input to capability.

Government response **Agreed**

The Government acknowledges Australian defence industry provides a critical role in delivering and sustaining Defence capability. A key element of the 2016 Defence Industry Policy Statement (DIPS) is the formal recognition of Australian industry as a discrete Fundamental Input to Capability (FIC) and its integration into the new Defence capability life cycle.

This recognition will provide industry an earlier and stronger voice across the capability life cycle and drive more formal consideration of industry impacts through the early stages of the capability development process. This strategy will better position Defence to match the development of new capabilities with industry's ability to deliver them and provide more opportunities for Australian industry while ensuring the best capability is delivered to Defence.

A significant amount of work is being progressed on the Smart Buyer model and on improving industry engagement across the capability life cycle which directly relate to integration of industry as a FIC within Defence's policy framework. This work and formal consideration of industry as a FIC will enable opportunities for Australian defence industry in the acquisition and sustainment of capability to be maximised.

As part of the White Paper implementation plan, Defence will progressively update all related policy to embed industry as a FIC into Defence processes and culture.

Recommendation 2

The Committee recommends that the Department of Defence build on previous activities in Australia and abroad to develop a system to identify those elements of industrial competence or capacity that are deemed to be fundamental inputs to ADF capability (FIC). This activity should be led by the Service Chiefs and implemented by Capability Acquisition and Sustainment Group at a strategic level with an assessment of how each new significant project may change the assessment of FIC or indeed could contribute to the maintenance of FIC from a whole of program perspective.

Government response **Agreed in Principle**

The recognition of industry as a FIC will ensure Defence considers the industrial capabilities and the capacity of Australian businesses to deliver Defence capability, including operational capabilities and the full spectrum of support functions.

Defence capability managers will consider the industrial base as capability plans are developed, including the reliability and health of supply chains. This approach will

ensure Defence capability managers consider and manage industry inputs as they would any other FIC.

The 2016 Defence Industry Policy Statement (DIPS) sets out the specific measures the Government will take to implement the Defence industry policy. These include streamlining the numerous Defence industry and innovation programs under two broad initiatives: the Centre for Defence Industry Capability (CDIC) and a new approach to innovation.

The DIPS also emphasises the need to change the way Defence identifies and manages strategically important capabilities. Defence is introducing the Sovereign Industrial Capability Assessment Framework to manage this important requirement. As a result of this change, Defence recognises the need for policy relating to the PIC framework to be updated to account for the new framework.

A key responsibility of the CDIC, in collaboration with Defence, is the identification and management of Sovereign Industrial Capabilities. These are capabilities that exist within the industrial base and develop or support critical ADF capabilities. These might include, for example, Sovereign Industrial Capabilities that develop and support the Nulka active missile decoy and the CEA Phased Array Radar.

A Defence Industrial Capability Plan will be created that identifies the Sovereign Industrial Capabilities that are required to be maintained and supported in Australia. Existing contracts that support Priority and Strategic Industry Capabilities will continue until a transition takes place to the new Sovereign Industrial Capabilities, scheduled for the second quarter of 2017.

Defence will also provide recommendations to the Government on Sovereign Industrial Capabilities as part of the Government's consideration of discrete capital investment proposals.

Recommendation 3

The Committee recommends that when implementing the First Principles Review changes to roles and responsibilities, capability development, procurement and sustainment, Defence take into account the framework for industry engagement based around the fundamental inputs to capability illustrated in Figure 1.

Government response **Agreed in Principle**

As outlined in the Defence White Paper and the Defence Industry Policy Statement (DIPS), the Government recognises that an internationally competitive Australian defence industry is a fundamental input to Defence capability.

The ambitious and extensive program of future investment in major defence capability that is set out in the Integrated Investment Program provides significant opportunities for industry; the program's scope will also set challenges for industry in responding in an effective and timely manner to these opportunities.

The DIPS sets out the Government's commitment to resetting the partnership with industry and the ways in which Defence engages with industry. Fundamental initiatives to

achieve this are the Centre for Defence Industry Capability (CDIC), the new approach to innovation, recognising industry as a Fundamental Input to Capability, and revitalising the Capability Life Cycle process.

Under the direction of the First Principles Review, industry will be an integral part of the Smart Buyer Framework and engagement with industry will be targeted and tailored depending on the acquisition strategy. In the early stages of the capability lifecycle, this will involve engaging with industry through dialogue mechanisms including through the CDIC.

Through the CDIC and the new approach to innovation, Defence will also have a better understanding of the industrial capabilities, capacity and innovation of Australian business – micro, small, medium and large – to deliver Defence capabilities, including operational capabilities and the full spectrum of support functions.

Recommendation 4

The Committee recommends that in areas where an aspect of industry is identified as a fundamental input to capability, Defence's procurement and probity guidelines provide suitable pathways for long term partnerships to be the default approach to driving innovation, productivity and value for money rather than a primary focus on open competition. Defence should publicly report savings achieved by virtue of this revised approach to procurement.

Government response Agreed in Principle

The Defence White Paper 2016 and associated Defence Industry Policy Statement (DIPS) indicates the Government's commitment to forming a new partnership with Australian defence industry to ensure Defence gets the equipment, systems and personnel it needs on time and budget. The Government will strengthen Defence's collaboration with Australian defence industry, cut red tape and invest in new technologies to help build Australian defence industry competitiveness. Defence will also streamline its approach to tendering and contracting to make it easier for Australian industry to support Defence.

The DIPS states that where the value for money concept is clear in the context of Defence procurement, capability decisions will continue to be based on the Commonwealth Rules, and include explicit consideration of:

- the sovereign requirements for Australian industry involvement, which would help guarantee the ADF's independence of action; and
- the identification of opportunities to maximise internationally competitive Australian industry involvement.

In considering Defence capability proposals, comprehensive information will be provided to Government in relation to Australian industry issues to ensure informed decisions are made based on the evidence presented. Integration of industry as a Fundamental Input to Capability across the capability lifecycle and the introduction of the Smart Buyer Framework will drive longer term and improved relationships with industry and ensure Defence receives the capability it needs.

The Government also recognises the importance that Defence's strategic research has for Australia's future prosperity and that game changing military capabilities such as the

Jindalee over-the-horizon radar arise from the pursuit of next generation research. Through the 2016 DIPS, the Government has invested around \$730 million (over the decade) in new funding to develop these game-changing capabilities and \$640 million (over the decade) in redirected funding for the Innovation Hub to nurture and mature innovation proposals through a single innovation pipeline.

Defence is establishing contracting and intellectual property regimes to maximise incentives to innovation and attract investment. Importantly, Defence will also develop new approaches to risk to allow innovation to flourish across the Defence enterprise.

Recommendation 5

The Committee recommends that where a procurement activity is linked to a fundamental input to capability, the Department of Defence develop guidelines that encourage identification and management of risk rather than avoidance of risk through defaulting to an offshore contract.

Government response **Agreed in Principle**

Defence has mature risk management approaches in place which seek to assess and treat the risks inherent within each procurement on their merits. As part of developing the Smart Buyer Framework, Defence will review its risk management framework as it applies to procurement activity linked to the Fundamental Input to Capability.

Recommendation 6

The Committee recommends that the Department of Defence significantly expand its investment in activities that generate fundamental input to capability-related innovation and intellectual property, and support commercialisation through partnership models such as the Defence Materials Technology Centre.

Government response **Agreed**

Driving Australian innovation is a critical element of the Government's vision for the nation. As outlined in the DIPS, Defence is committed to transforming the way it approaches innovation, and to working collaboratively with industry to identify, nurture and grow innovation solutions which deliver better Defence outcomes.

A key initiative of the DIPS is a new approach to innovation. As part of this initiative, Defence is investing around \$640 million (over the decade to financial year 2025-26) in a new virtual Defence Innovation Hub to enable industry and Defence to undertake collaborative innovation activities throughout the Defence Capability Life Cycle, from initial concept, through prototyping and testing to introduction into service.

The Hub will assist Australian companies and academic and research organisations to assess whether innovations have a Defence application and will provide access to funding to collaboratively mature those ideas.

As part of the new approach to innovation, supporting policies will be developed and a culture will be fostered to make it easier for industry to collaborate with Defence on

innovative ideas. This will include new contracting and intellectual property regimes which maximise incentives to innovation and attract investment from a range of local and international sources. New approaches to risk will also be adopted, recognising the importance of embracing risk where necessary and appropriate in order to further develop innovative solutions.

Another key initiative of the new approach to innovation is the establishment of a Next Generation Technologies Fund. Funded at around \$730 million (over the decade to financial year 2025-26), the Next Generation Technologies Fund will invest in strategic next generation technologies that have the potential to deliver game-changing capabilities. Defence will work with industry and academia on how they can partner with Defence on priority areas of work, such as space capabilities and quantum technologies.

Defence will also work closely with the Government and industry bodies across Australia, such as the Cooperative Research Centres, which are participating in innovation activities. This will provide greater opportunities for collaboration and leverage the substantial national investment in research and development. The Next Generation Technologies Fund will work closely with the Innovation Hub to identify opportunities for promising technologies to transition to the Hub and access further funding in order to develop into operational capabilities.

Recommendation 7

The Committee recommends that where an industry-related fundamental input to capability has been identified, the Department of Defence prioritise Australian based procurement contracts so that relevant industry and Defence staff can develop competence in specific tasks via hands-on experience, or where this is not possible, through making the placement of Australian staff in original equipment manufacturers or foreign military engineering bodies a condition of contract.

Government Response Agreed in Principle

Where there is a requirement for relevant industry or Defence staff to develop and maintain competency in specific tasks, this requirement is included as part of the contract statement of work or Australian Industry Capability (AIC) plan. In delivering this requirement there are a variety of methods from embedding staff through to routine training courses to ad-hoc on-the-job training, either domestically or internationally, that can be included in the contract.

Where a Priority Industry Capability has been determined as relevant to a procurement activity, a costed Australian solution for development or support of the critical ADF capabilities is a requirement of tender.

The introduction of the Sovereign Industrial Capability Assessment Framework will see the Sovereign Industrial Capabilities considered in the early stages of the capability development process. This will drive longer term partnerships to be the default approach to ensuring the ADF critical capabilities are developed and supported in Australia.

Recommendation 8

Subject to acceptance of Recommendations 1-7, the Committee recommends that the Department of Defence discontinue the Priority Industry Capability and Strategic Industry Capability programs, retain the Australian Industry Capability targets for procurement activity that do not involve an identified fundamental input to capability and continue to promote the Global Supply Chain scheme wherever possible.

Government Response Agreed in principle

The Government is committed to maximising opportunities for competitive Australian industry and to ensuring that the industry base associated with critical ADF capabilities is maintained and supported by Defence.

The existing Priority and Strategic Industry Capability policy is being replaced by the Sovereign Industrial Capability Assessment Framework to improve the identification and management of Sovereign Industrial Capabilities that develop and support our ADF capabilities. Existing contracts and programs that support Priority and Strategic Industry Capabilities will continue until a transition takes place to the new Sovereign Industrial Capabilities, scheduled for the second quarter of 2017.

The Sovereign Industrial Capabilities will be identified in the Defence Industrial Capability Plan to be developed by Defence and the Centre for Defence Industry Capability by the second quarter of 2017.

The Australian Industry Capability Program and the Global Supply Chain Program continue to provide real benefit and growth to small to medium sized companies through the award of domestic and international bid opportunities. The improved competitiveness means Australian businesses are realising opportunities to diversify into other sectors and overseas markets, competing on the world stage.

Both these programs will be enhanced under the expanded governance framework of the Centre for Defence Industry Capability when it commences operations in the second half of 2016.

Recommendation 9

The Committee recommends that the Department of Defence increase the level of support to defence exports where such exports will help sustain or develop a fundamental input to capability.

Government Response Agreed in principle

The Australian Government encourages the export of defence and dual-use goods and technology, while recognising that there is a need for appropriate controls over the export of such goods to protect and promote Australia's strategic and foreign policy interests and fulfil Australia's international obligations.

The Defence Export Controls Branch will continue to work closely with exporters and other agencies to facilitate exports of Australian indigenous military and dual-use

technologies that support Australia's defence and security interests. Through the Sensitive Technologies Advisory Group (STAG), Defence engages with producers of technology critical to Australia's defence capabilities to assist them to understand possible future export restrictions, to develop exportable variants, and encourage them to make commercial decisions about exports early in a technology's life-cycle.

As part of Government's commitment to improve opportunities for Australian business, the Centre for Defence Industry Capability (CDIC) will provide coordinating efforts in relation to export opportunities with AusTrade and the Department of Foreign Affairs and Trade, as well as the States and Territories.

In accordance with the Defence Industry Policy Statement, the "CDIC will guide and mentor companies to improve their international competitiveness through exports programs. The CDIC will do this by:

- acting as a trusted broker of relationships between defence companies, Defence and other Government agencies (for example, with AusTrade)
- offering advisory services to Defence industry to assist enterprises to become 'export ready' and globally competitive
- offering market advice to help guide potential export opportunities
- facilitating Defence trade missions
- facilitating interaction with the Defence Export Controls Branch
- providing a Supplier Continuous Improvement Program, aimed at systematically embedding corporate, operational and continuous improvement capability as required by global defence businesses".

Investment in innovation also helps to ensure Defence remains resilient to emerging threats and provides export opportunities for competitive companies. The Defence Industry Policy Statement outlines the Government's intention to making significant reductions in red tape associated with industry and innovation programs, fundamentally reshaping the way industry engages with Defence. The streamlining of Defence industry and innovation programs into the Defence Innovation Hub and the CDIC will make it simpler and cheaper for business to engage with Defence.

Recommendation 10

The Committee recommends that the Minister for Defence Materiel and Science have responsibility for how the capability development, procurement and sustainment systems work, the investment in fundamental input to capability-related innovation and export opportunities including an increased focus on Government to Government sales.

Government Response **Agreed in principle**

The Minister for Defence, supported by the Minister for Defence Materiel, has responsibility for the overall Defence capability program, including delivery of major projects and management of defence industry policy.

Recommendation 11

The Committee recommends that Defence develop performance measures relevant to the management of the defence industry as a fundamental input to capability and publicly report the outcomes.

Government Response **Agreed in principle**

As part of the implementation of a Smart Buyer Framework to the acquisition and sustainment of Defence materiel identified in the Defence First Principles Review, Defence is establishing a supplier relationship team within the Capability Acquisition and Sustainment Group. The team will develop and maintain successful collaborative relationships with key suppliers to maximise the benefit to both Defence and industry.

The newly formed supplier relationship team will review existing performance measures and amend or develop performance measures relevant to the management of defence industry with consideration given to making relevant information publically available.

Recommendation 12

The Committee recommends that defence export assistance efforts be prioritised based on a distinction between areas of core and secondary export focus:

- Core export focus would apply to elements of industry output recognised as a fundamental input to capability (FIC), where defence exports can help sustain or spread production costs. This support should extend to funding for research and development that supports exports that will have an impact on the associated FIC; and
- Secondary export focus would apply to those elements of industry output not recognised as a FIC. In such cases, Defence and other related agencies should provide assistance where practicable

Government Response **Agreed in principle**

The Government is committed to providing industry with greater opportunity to develop internationally competitive capabilities and to enabling better access to global markets.

Defence and the Centre for Defence Industry Capability (CDIC) are developing a Defence Industrial Capability Plan that identifies the Sovereign Industrial Capabilities required to support critical ADF capabilities. In developing the plan, consideration will be given to the types of management approaches both Defence and the CDIC can take to support the Sovereign Industrial Capabilities. This might include priority access to defence industry programs including export programs, the facilitation of Government to Government sales by the Australian Military Sales Office (AMSO) and funding for research and development activities through the Defence Innovation Hub in order to develop or support the capability.

The new approach to innovation is a cornerstone initiative of the Defence Industry Policy Statement enabling Defence and industry to undertake collaborative innovation activities from initial concept, through prototyping and testing to introduction into service. For many of the mature technologies and products, the large defence prime companies will be

Team Defence Australia and Austrade will continue to provide assistance and facilitation with the export of a product or service and the CDIC will provide companies with priority assistance where the potential export is in support of a critical ADF capability.

Recommendation 13

The Committee recommends that the Australian Government develop a defence exports strategy and the Department of Defence expand the role of the Australian Military Sales Office to include implementing the objectives of this strategy, based upon the defence industry as a fundamental input to capability.

Government Response Agreed in principle

Defence manages a number of programs to increase the international competitiveness of defence industry and to subsequently increase the export of technologies, products and services. These programs are currently administered by Defence or in partnership with the Department of Industry, Innovation and Science.

The Centre for Defence Industry Capability (CDIC) will be established in the second half of 2016 and the role of the Australian Military Sales Office (AMSO) within the framework of the CDIC will be considered as the Centre matures. AMSO continues to be involved with Government to Government transfers, assisting Commercial to (Foreign) Government sales and will provide assistance with export facilitation associated with the Sovereign Industrial Capabilities.

The CDIC will fund critical skilling, industry development and export programs and manage the Australian Government Defence Export Support Forum (AGDESF). This forum consists of the major stakeholders involved in the promotion and facilitation of defence exports and provides a forum to address sectoral wide export issues.

The CDIC will lead development of a defence export strategy with stakeholder input and coordination to be provided by the AGDESF.

Recommendation 14

The Committee recommends that the Department of Defence task appropriate Australian Defence Force personnel to assist at trade shows or exhibitions, alongside defence industry participants, to inform and advise foreign customers of the Australian Defence Force's experience using the displayed products.

Government Response Agreed in principle

Experienced senior ADF personnel continue to lead Team Defence Australia (TDA) delegations at overseas trade events. They provide an important advocacy role on behalf of Australia's defence industry and facilitate meetings between the participating TDA companies and foreign military personnel and defence primes.

Defence Capability Acquisition and Sustainment Group staff and, where appropriate, the Defence Attachés in key regions may also assist in the organisation of trade missions with a focus on addressing the capability needs of particular countries.

Defence will make available Defence Force personnel with experience using the displayed products to promote Australian industry where appropriate and where it provides a strategic benefit to Defence.

Recommendation 15

The Committee recommends that the Department of Defence revise the roles of defence attachés to include:

- Gathering information relevant to defence export opportunities on behalf of the Australian defence industry;
- Relaying this information to industry, along with other advice on export opportunities and constructive feedback on Australian defence industry performance, via the Australian Military Sales Office;
- Initiating discussions with foreign governments regarding potential military sales from Australia; and
- Where appropriate, the promotion of Australian products.

Further, pre-deployment training for defence attachés should include mandatory familiarisation with, and understanding of, the Australian defence industry.

Government Response Agreed in principle

In accordance with the 2010 Prime Minister and Cabinet Directive *Guidelines for Management of the Australian Government Presence Overseas*, the primary responsibility of a Defence Attaché is to advise and assist the Head of Mission to represent the Government of Australia on Defence matters. In turn, the Defence Attaché's primary role is to support the Department of Defence's international engagement with the country(ies) to which they are accredited. One of the 20 roles and functions identified in the Defence Attaché's Directive is to promote Australian defence industry and provide assistance to representatives of Australian defence industry seeking to market defence products or services in the accredited country, within policy guidelines, and as resources permit.

To support this function, the Australian Military Sales Office now briefs Defence Attachés on matters relating to Australian Defence Industry and how Defence Attachés assist in supporting stakeholders, as well as recent case studies. In 2015, this component was re-introduced into Defence Attaché pre-posting preparation conducted by Defence International Policy Division.

Defence Attachés are often the in-country contact point for many transactions and provide invaluable in-country situational awareness. This information is then passed back to International Policy Division and the Australian Military Sales Office to ensure a coordinated departmental response.

Recommendation 16

The Committee recommends that relevant Government Ministers fulfil a prominent advocacy role on behalf of the Australian defence industry, in particular the Minister for Defence Materiel and Science.

Government Response

Agreed

Subject to export controls, the Ministers already strongly advocate for and on behalf of Australia's defence industry both domestically and internationally. In addition, the Minister for Defence Materiel has portfolio responsibilities covering industry capacity, structure, policy and engagement.

Recommendation 17

The Committee recommends that the Department of Defence enhance the existing risk-based approach to assessing applications to export materiel and technology subject to Australian export control laws.

Government Response

Agreed

The Government has implemented the Committee's recommendation to enhance existing application assessment processes by introducing a range of risk-based licence options. Since August 2015, exporters have been able to apply for Australian General Export Licences which are open licences valid for five years that enable licence holders to export approved items to approved countries within the five year period without needing to seek further government authorisation. In January 2016, for lower risk exports, the Government also extended the maximum permit period to five years or the life of the project.

Recommendation 18

The Committee recommends that the Defence Export Control Office improve the defence export approval process by:

- Providing timely updates to applicants on the status of their application;
- Ensuring information regarding regulatory change is promptly communicated to relevant stakeholders;
- Allowing export licences to be valid for longer periods;
- Introducing a simplified process for renewal where approval expires; and
- Managing this process depending on the risks in each case.

Government Response

Agreed

The Government has introduced measures to address each aspect of the recommendation.

The Defence Exports Control Branch keeps applicants informed if target timeframes are not met; for example, if a case will exceed the routine 15-day assessment period. For complex cases, applicants are notified by letter and provided an opportunity to

provide additional information to support their case. At any stage, applicants are able to contact the Defence Exports Control Branch via email or phone to seek an update on their application.

The Defence Exports Control Branch communicates regulatory changes to stakeholders through the Defence Export Controls website, via email and at forums. The Government is increasingly targeting relevant stakeholders through interagency cooperation and communication with member-based and representative peak organisations.

In January 2016, for lower risk exports, the Government extended the maximum permit period to five years or the life of the project.

Improvements to the online application system have simplified the process for renewal of expired and nearly-expired licences. Applicants are now only required to provide the previous licence number, and the system will automatically generate the licence details from the previous application.

The Defence Exports Control Branch manages applications on a case-by-case basis, depending on the risks posed by the sensitivity of the goods, consignee, end-user and end-use, and destination.

Recommendation 19

The Committee recommends that the Department of Defence publicly report the Defence Export Control Office's budget, expenditure, numbers of applications processed and overall performance on an annual basis.

Government Response Agreed in principle

The Defence Exports Control website includes a statistics page which reports on the numbers of applications received and processing times.

As the Defence Export Controls Branch is not a separate statutory body, its budget and expenditure are managed and acquitted within the Department of Defence budget. Details are publicly reported in the Defence Annual Report under Program 1.1.