

# Chapter 5

## Urgency of acquisition

5.1 At the time the Minister for Defence announced the tender arrangements for the two replenishment ships, he noted the important role of these ships. He said that replenishment vessels were 'essential to support sustained naval deployments'. Indeed as noted earlier, the capability provided by the supply ships enable the rest of the naval fleet to remain at sea for longer periods and to operate in areas far removed from its base. This capability is referred to as a 'force multiplier' and is considered an important part of the Navy's ability to meet its primary objective—to be able to fight and win in the maritime environment'.<sup>1</sup>

5.2 The Minister for Defence indicated, however, that both ships were approaching the end of their useful life: that HMAS *Success* was in urgent need of replacement and HMAS *Sirius* provided only limited replenishment capability.<sup>2</sup> He stated further:

HMAS *Success* was commissioned in 1986, this ship should have been transitioned out of service much sooner than now and, if you're familiar with the bathtub curve, the costs of running that particular replenishment ship are climbing, climbing very high and are very burdensome for the Navy.<sup>3</sup>

5.3 In his announcement, the Minister cited 'the urgent need to forestall a capability gap in this crucial area' as one of the main reasons for having the restricted tender.<sup>4</sup> According to the Minister, competition between the two experienced ship

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1 See for example, DMO, *Getting Sirius A Project Manager's Story: The acquisition and modification of an auxiliary oiler HMAS Sirius*, 2008, pp. 3–4 and ANAO, Audit Report No.20 2006–07, Performance Audit, *Purchase, Chartering and Modification of the New Fleet Oiler*, Department of Defence, Defence Materiel Organisation, p. 13, [http://anao.gov.au/~media/Uploads/Documents/2006%2007\\_audit\\_report\\_20.pdf](http://anao.gov.au/~media/Uploads/Documents/2006%2007_audit_report_20.pdf) (accessed 6 August 2014).

2 'Minister for Defence—Boosting Australia's maritime capabilities', 6 June 2014, <http://www.minister.defence.gov.au/2014/06/06/minister-for-defence-boosting-australias-maritime-capabilities/> (accessed 4 August 2014).

3 'Minister for Defence—Transcript—Naval shipbuilding announcement, CEA Technologies, Canberra', 6 June 2014, p. 2, <http://www.minister.defence.gov.au/2014/06/06/minister-for-defence-transcript-naval-shipbuilding-announcement/> (accessed 4 August 2014).

4 'Minister for Defence—Boosting Australia's maritime capabilities', 6 June 2014, <http://www.minister.defence.gov.au/2014/06/06/minister-for-defence-boosting-australias-maritime-capabilities/> (accessed 4 August 2014).

builders would be 'the best way to ensure delivery of capable, cost effective vessels in the time frame required'.<sup>5</sup>

5.4 Mr King supported the view that the ships needed to be replaced. He noted the requirement for at least three programs to be underway relatively quickly—the Future Frigates program, the AORs, and Pacific patrol boats. He indicated that the most urgent and highest priority was the AOR replacement for the Navy citing the age of *Success* whose life of type expires in 2016.<sup>6</sup>

5.5 In Mr King's assessment, if *Success* continued beyond 2017, which it would have to do, 'every year will get more expensive and more difficult'.<sup>7</sup> He noted that Defence was already spending a considerable amount of money to keep the old ship afloat. He also referred to the bathtub curve effect:

When you buy something you have early failures, then you use it for a large number of years pretty efficiently with limited maintenance, and then towards the end of its life it seems to become very old and in fact parts are not even replaceable. In terms of our ships they can be 35 years old. Imagine getting a pump that is 35 years old. *Success* is well and truly into that part of its life.<sup>8</sup>

5.6 Indeed, between 2010 and 2012, HMAS *Success* underwent significant maintenance over a 16 month period, which included an IMO requirement to complete a double-hulling process and the completion of a long standing propulsion alignment issue. Also, a significant amount of emergent work, consistent with a ship of this age, has been carried out. The expenditure on HMAS *Success* during the period December 2010 and April 2012 was:

December 2010–April 2011	IMO Hull Conversion	\$17.8M
June 2011–November 2011	Maintenance Period	\$13.8M
December 2011–April 2012	Propulsion Alignment and ongoing Maintenance	\$4.1M <sup>9</sup> (budgeted at April 2012)

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5 'Minister for Defence—Boosting Australia's maritime capabilities', 6 June 2014, <http://www.minister.defence.gov.au/2014/06/06/minister-for-defence-boosting-australias-maritime-capabilities/> (accessed 4 August 2014).

6 *Committee Hansard*, 21 July 2014, p. 12.

7 *Committee Hansard*, 21 July 2014, p. 25.

8 *Committee Hansard*, 21 July 2014, p. 12.

9 Department of Defence, 'Questions and Responses to David Ellery, the Canberra Times in relation to articles published on 9 April 2012', 9 April 2012, p. 6, <http://www.minister.defence.gov.au/2012/04/09/questions-and-responses-provided-to-david-ellery-the-canberra-times-in-relation-to-articles-published-on-9-april-2012/> (accessed 4 August 2014).

5.7 In addition to maintenance and repair costs, the Department received advice in 2012 indicating that 'extending the life of HMAS *Success* for five years beyond the current Planned Withdrawal Date of 2018 would require expenditure just in excess of \$20M'.<sup>10</sup> Mr King spoke of the three possible options:

- an offshore build, which is the option that Defence is taking;
- a complete onshore build; and
- a hybrid build, as with the LHD, with the bulk of the ship produced in Spain and elements of it fitted out in Australia.<sup>11</sup>

5.8 Mr King stated that the urgency associated with acquiring the two supply ships reflected the balancing of the complete suite of Defence's need against the budget and 'when you can afford to embark on programs'.<sup>12</sup> He then explained:

The quickest replacement time that we think is even remotely possible is about 3½ years build time—that sort of order. So we need to get into contract soon. Not only are these needed for military capability, but every year...*Success*...is not replaced is an increased maintenance cost that is likely to accelerate. It is beyond its design life in 2016. Even at the moment, we are offering 2017. So that is the principle behind it.<sup>13</sup>

5.9 Although noting that Defence sometimes has a capability gap due to a lack of funds, Mr King would not be drawn on whether a capability gap existed in respect of the supply ships. He stated that such a matter was getting well beyond his 'spectrum of business', which was 'to pursue acquiring products and so on'. He stated:

In terms of whole capability planning, where the money is spent and when, that is really better handled by Defence more broadly. But there is a reality: countries haven't the money, Defence has needs and they have to be balanced off.<sup>14</sup>

5.10 Witnesses agreed that Defence and industry had been aware of the need to replace the supply ships for years. For example, according to the AMWU, some of its members working on HMAS *Success*, understood that the ship was getting old, was becoming increasingly more expensive to maintain and needed to be replaced soon.<sup>15</sup> The Australian Business Defence Industry also referred to the imperative to replace

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10 Department of Defence, 'Questions and Responses to David Ellery, the Canberra Times in relation to articles published on 9 April 2012', 9 April 2012, p. 7, <http://www.minister.defence.gov.au/2012/04/09/questions-and-responses-provided-to-david-ellery-the-canberra-times-in-relation-to-articles-published-on-9-april-2012/> (accessed 4 August 2014).

11 *Committee Hansard*, 21 July 2014, p. 15.

12 *Committee Hansard*, 21 July 2014, p. 22.

13 *Committee Hansard*, 21 July 2014, p. 15.

14 *Committee Hansard*, 21 July 2014, p. 22.

15 *Submission 4*, p. [2].

the ships, which were near or at their end of operational life.<sup>16</sup> Likewise, Mr Dunk recognised that there were problems with *Success* and *Sirius* regarding their longevity. The Navy League of Australia similarly acknowledged that one of the main drivers to call a limited tender from the two overseas shipyards stemmed from the pressing need to replace the two supply ships. It noted that plans to replace HMAS *Success* had been around for some time but the passage of time without further action had led to the urgency:

HMAS *Success* is now 28 years old and at an age when she would normally be replaced. It is believed that the ship is now more difficult to support as her equipment ages and its reliability reduces. She has recently completed a major refit. It is understood that further work is planned to address equipment deficiencies to enable the ship to remain in service until a replacement can be acquired.<sup>17</sup>

5.11 The League also referred to HMAS *Sirius*, which, although relatively new, is a converted commercial tanker that, in its view, 'lacks the comprehensive support capability provided by HMAS *Success*'.<sup>18</sup>

### **Timing and schedule**

5.12 No one denied that the Navy needs replenishment ships to service the rest of the fleet and that their replacement was overdue. Even so, a few witnesses had proposals that, in their view, would maintain the afloat support capability and not cause significant delay to the acquisition of the vessels.

5.13 While Mr Christopher Burns, Defence Teaming Centre, acknowledged that no-one had put forward a proposal to build the whole vessel in Australia, he noted that two proposals for a hybrid build had been submitted.<sup>19</sup> For example, as noted earlier, BAE systems informed the committee that it had submitted an unsolicited proposal to government in September 2012 setting out a hybrid build program, with part of the ship built overseas and part of the ship built in Australia.<sup>20</sup> It estimated that the additional time required producing the replenishment ships according to its proposed hybrid model would be approximately six months.<sup>21</sup>

5.14 Mr King told the committee that even in informal discussions no company had suggested to him or his organisation that this ship should be built in Australia—a partnership though was different. Mr King informed the committee that he was aware

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16 *Submission 2*, p. [2].

17 *Submission 12*, p. [2].

18 *Submission 12*, p. [2].

19 *Committee Hansard*, 21 July 2014, p. 42.

20 *Submission 9*, p. 1.

21 *Submission 9*, p. 2.

of an unsolicited proposal from BAE for a hybrid build.<sup>22</sup> Returning to the matter of timing, however, Mr King argued that hybrid builds or Australian builds introduce complexity and pressure on schedule. He explained that he worked on the broad principle that:

...if we buy offshore, it comes on time; if we do hybrid; it comes a bit late; and if we do totally onshore, it is late. That is the basic premise.<sup>23</sup>

5.15 He used the LHD as an example, noting that the vessel was supposed to be delivered months ago but was still late by seven months. He explained further that the builders had all the time they wanted to construct that ship:

I have to make judgements over the top of a commercial proposal...On an LHD there were 30,000 man-hours of work left over that Navantia did not do. It cost 70,000 hours in Australia. I have to put forward a degree of credibility, and for someone to propose that a hybrid build would add only six months is not credible. I spend most of my time trying to explain to the public why the AWD is late, why the LHD is now seven months late. And it is because we get more ambitious than we are able to deliver. I would like to see an industry that can deliver.<sup>24</sup>

5.16 While stating clearly that it was not credible to suggest that the ship would only take an additional six months to deliver, Mr King indicated that he had subsequently received 'other unsolicited offers for offshore builds, which offered different numbers'.<sup>25</sup> He told the committee that he did 'not put a lot of confidence in any unsolicited proposals'.

5.17 When asked why Defence did not go to an open tender in order to test the claims being made about the various options and the potential to meet the challenges of the build, Mr King agreed that a tender process would test such claims, but went on to explain that the actual tenders:

...typically, tend to be wrong, at least in schedule. The point I have made on many occasions...is that since 2000 our Defence procurement has run seven per cent under budget. So, typically we get budget right. Our schedule is about 35 per cent later than we advertised. It is getting better, but I can assure you that if I relied on unsolicited information we would be getting worse again. So, you are right: we do go to tender. Even then, though, we still make judgements.<sup>26</sup>

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22 *Committee Hansard*, 21 July 2014, p. 19.

23 *Committee Hansard*, 21 July 2014, p. 31.

24 *Committee Hansard*, 21 July 2014, p. 19.

25 *Committee Hansard*, 21 July 2014, p. 19.

26 *Committee Hansard*, 21 July 2014, p. 19.

5.18 Mr King noted further that the main considerations centred on capability, time and cost.<sup>27</sup> According to Mr King, he was regularly chastised by members of parliament and the public and by journalists about projects being late when he had relied on industry giving him time and cost. He told the committee:

...over and over again, I rarely hear that industry is being criticised for that misjudgement; it is me. So we have learned to modify, if you like, industry claims about what they think on that.<sup>28</sup>

5.19 Based on his recent experience in a couple of Asian shipyards, Mr King told the committee that they have 'not missed a delivery for years, and they talk about three weeks as being a terrible error. We are talking about years'.<sup>29</sup> He noted that countries around the world 'can build these ships well'.

### Lease vessel

5.20 The AMWU was of the view that Defence had options other than the current proposal for a limited tender for the supply ships and that an open tender should have been on the table.<sup>30</sup> Mr Thompson, AMWU, informed the committee that in 2013, the union recommended that Defence investigate interim solutions to deal with Navy's requirement for replenishment vessels. The union proposed leasing a ship to temporarily replace *Success*, as Defence had previously done with the *Cantabria* when upgrade work was being done on *Success*. Mr Thompson suggested that the lease replacement may be for five to eight years, depending on how quickly an Australian project could be approved.<sup>31</sup> He reasoned:

This would take the interim schedule pressure off building the new ship and provide the opportunity to build new ships in Australia. A hull block could be built in different shipyards. A ship could be consolidated in Perth, Adelaide or wherever, subject to investment.<sup>32</sup>

5.21 The union was of the view that the circumstances of *Sirius* were not as urgent.<sup>33</sup> It noted that while the *Sirius* was an Auxiliary Oiler and not an Auxiliary Oiler Replenishment like *Success*, there was no pressing need to replace the ship because of its age or cost to maintain. It conceded that while it may be ideal to get the additional capability and replace the ship early, by 'all accounts, *Sirius* has served the Navy well for the past eight years'.<sup>34</sup>

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27 *Committee Hansard*, 21 July 2014, p. 17.

28 *Committee Hansard*, 21 July 2014, p. 17.

29 *Committee Hansard*, 21 July 2014, p. 31.

30 *Committee Hansard*, 21 July 2014, p. 34.

31 *Committee Hansard*, 21 July 2014, pp. 33 and 34.

32 *Committee Hansard*, 21 July 2014, p. 34.

33 *Committee Hansard*, 21 July 2014, p. 33.

34 *Submission 4*, p. [2].

5.22 According to Mr Thompson, if there were no interim option, there could be another solution, which would entail a hybrid build of ship 1 while sending Australian shipbuilders to that shipyard to learn. Then:

Ship 2 could be built in Australia, using this as an option to invest in the Australian capability and help bridge the gap between the current and future work.<sup>35</sup>

5.23 The option of leasing a vessel, as done previously, was put to Mr King who indicated that that arrangement had been a 'one-off, special arrangement' and that ultimately Defence had to purchase the replacement ships. He indicated that leasing a vessel or acquiring a second-hand AOR was considered and determined not to be feasible.<sup>36</sup> According to Defence, open market research revealed that there were no suitable vessels evident on the world market to purchase as a second hand AOR. Furthermore, that:

Defence engagement, primarily through navy-to-navy contacts, with allies for the prospect of leasing an in-service foreign navy AOR was also unsuccessful, with no suitable leasing options identified.<sup>37</sup>

5.24 Mr King informed the committee that Defence had, for several years, been working on this problem, working through options.<sup>38</sup>

## Conclusion

5.25 The committee understands the need to purchase the replacement replenishment ships to avoid a capability gap and to stem the continuing costs of maintaining an ageing vessel. The urgency of this situation highlights the need for government to have a realistic and practical long term capability plan.

5.26 A number of witnesses have put forward proposals that could address this potential shortfall in capability but without having to resort to a limited tender. They include a hybrid build with a slightly longer schedule or finding a temporary replacement by leasing a vessel. Defence indicated that leasing a vessel or purchasing a second-hand one were not viable options. Even so, the committee is concerned that the pressing need to acquire the vessels has led to a decision that effectively closes down options and prevents a more open, competitive and, indeed, fairer process.

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35 *Committee Hansard*, 21 July 2014, p. 34.

36 *Committee Hansard*, 21 July 2014, p. 18.

37 Department of Defence, answer to question on notice No. 3.

38 *Committee Hansard*, 21 July 2014, p. 18.

