



## Joint Committee of Public Accounts and Audit

### Inquiry into the 2018-19 Defence Major Projects Report and the Future Submarine Project – Transition to Design (Auditor-General Reports No. 19 and 22 (2019-20))

20 May 2020

#### Opening Statement by the Auditor-General — Auditor-General Reports No. 22 2019-20 *Future Submarine Project – Transition to Design*

1. Auditor-General Report No. 22 2019-20 *Future Submarine Program—Transition to Design* was presented for tabling in the Parliament on 14 January 2020.
2. This is the third in a series of performance audits examining the Future Submarine Program. The first audit, Auditor-General Report No. 48 2016–17 *Future Submarine—Competitive Evaluation Process*, examined the process underpinning the selection of an international partner to design Australia’s Future Submarine. The second audit, Auditor-General Report No. 39 2017–18 *Naval Construction Programs—Mobilisation*, examined the effectiveness of Defence’s planning for the mobilisation of its continuous shipbuilding programs, focusing on the Future Submarine, Future Frigate and Offshore Patrol Vessel programs.
3. The rationale for undertaking this audit and a rolling audit program relates to the significance, materiality and inherent risk of the Future Submarine Program. At a reported cost in the order of \$80 billion, the design and construction of the Future Submarine fleet represents the largest Defence procurement in Australia’s history. Defence has described it as a ‘megaproject’ by all international standards and the most challenging acquisition program it has undertaken, the success of which will be driven by preparations during the design phase, which is the focus of the most recent audit. The decision not to acquire a military-off-the-shelf submarine platform, and instead engage a ‘strategic partner’ to design and deliver the submarines with significant Australian industry input, has increased the risk of this acquisition. As reported in the audit, Defence advised the Government in February 2019 that the Future Submarine Program risks remain ‘high.’

4. This audit focuses on the platform design phase of the Future Submarine Program, which represents the largest material component of the program to date—approximately 47 per cent of all program expenditure as of 30 September 2019. At that date, Defence had spent \$834,891,390 on the Future Submarine Program, with \$396,068,415 spent on design work.
5. The audit objective was to examine the effectiveness of Defence's administration of the future submarine program to date, with a focus on program activities relating to design. Accordingly, the ANAO did not examine in any detail non-design program activities and expenditures to date, such as the combat systems integrator contract with Lockheed Martin Australia, the Collins class life-of-type extension, or the achievement of Australian industry objectives.
6. To assess the effectiveness of Defence's administration of the Future Submarine Program to date, and assist me to form a conclusion against the audit objective, the ANAO adopted the following high-level audit criteria:
  - Has Defence established a fit-for-purpose strategic partnership in accordance with government requirements?
  - Is Defence meeting the planned design milestones for the Future Submarine Program?
  - Has Defence's expenditure to date on design been effective in achieving the Future Submarine Program's milestones?
7. Against the audit criteria, I concluded that:
  - Defence has established the formal arrangements for the effective administration of the Future Submarine Program, through the Strategic Partnering Agreement (SPA) with Naval Group. Defence, through the SPA, has established a fit-for-purpose strategic partnership framework that addresses the Government's objectives for the program. The SPA includes provisions which address 11 of the 12 documented contract goals and provide a basis for establishing a successful strategic partnership and delivering shared program objectives. Defence has assured the Government that the remaining contract goal has been addressed.
  - However, the two key mandated design milestones were extended. The program is currently experiencing a nine-month delay in the design phase against Defence's pre-design contract estimates, and two major contracted milestones were extended. As a result, Defence cannot demonstrate that its expenditure of \$396 million on design of the Future Submarine has been fully effective in achieving the program's two major design milestones to date. As discussed, Defence expenditure on design represents some 47 per cent of all program expenditure to 30 September 2019.

- Program success is dependent on Defence establishing an effective long term partnership with Naval Group. Defence's overall assessment of risk for the Future Submarine Program is 'high' and Defence has adopted relevant risk mitigation strategies, including the long-term partnership with Naval Group. This key relationship is at a relatively early stage and the parties' active management of both specific issues and the partnership is essential for effective risk management and program success.
8. The ANAO reported on the following specific delays experienced by the Future Submarine Program:
- There was a delay in commencing negotiations and the Strategic Partnering Agreement was signed 16 months later than the objective.
  - The design schedule was extended by nine months against Defence's pre-design contract estimates, to help retire design risk.
  - The concept studies review commenced two months later than scheduled, and there were incomplete work items at completion.
  - The systems requirements review commenced five weeks later than scheduled.
9. The ANAO sought representations from Defence regarding the impact of these specific delays on the overall schedule for the Future Submarine Program. Defence's advice to the ANAO is reported at paragraphs 2.27 and 3.7 of the audit report. Defence's response to the audit, reproduced at paragraph 20 and Appendix 1 of the report, was that 'the commencement of construction activities in Australia, and the delivery of the Future Submarines has not been delayed.'
10. The report did not include any recommendations, but did identify key messages from this audit relating to procurement, which may be relevant for the operations of other Australian Government entities. The key messages, which include instances of good practice observed in the course of the audit, can be found at page 11 of the report:
- When planning for complex technical negotiations, consider establishing expert oversight arrangements to support the negotiating team.
  - When undertaking complex negotiations, maintain adequate records, continually assess risks and engage actively with those charged with oversight.
  - When negotiating and contracting for complex procurements, appropriately identify and advise government on major risks and proposed mitigation strategies.
  - When developing long-term contracts, incorporate formal review and exit points.

- Complex contracts will generally require active management to achieve contracted outcomes. A clear and consistent approach to contract management, particularly in the early stages of a long-term relationship, will help establish mutual understanding between the parties.
- Realising value-for-money under a contract requires a close watch over the timely and cost-effective delivery of contracted milestones as well as the achievement of program outcomes.

11. The audit team and I would be happy to answer any questions the Committee may have.