



Auditor-General for Australia



2 December 2019

Senator Alex Gallacher
Chair
Senate Economics References Committee
By email: Economics.Sen@aph.gov.au

Dear Senator Gallacher

Inquiry into Australia's sovereign naval shipbuilding capability

The Australian National Audit Office (ANAO) has published the following performance audit reports that you may find relevant to the Inquiry into Australia's sovereign naval shipbuilding capability.

- Report no. 30 of 2018–19, [ANZAC Class Frigates — Sustainment](#)
- Report no. 39 of 2017–18, [Naval Construction Programs—Mobilisation](#)
- Report no. 48 of 2016–17, [Future Submarine — Competitive Evaluation Process](#)

Information about what these audits assessed, concluded and recommended is attached. The audit reports are available online at www.anao.gov.au.

Should the Committee require further information in relation to the tabled audits, my office would be pleased to provide you with a briefing at a time convenient to you or appear as a witness at a hearing. To arrange a briefing, please contact our External Relations area at [REDACTED]

Yours sincerely

[REDACTED]

Grant Hehir

[REDACTED]

Report no. 30 of 2018–19, ANZAC Class Frigates — Sustainment examined whether the Department of Defence has effective and efficient sustainment arrangements for the Royal Australian Navy's fleet of eight ANZAC class frigates. To form a conclusion against the audit objective, the ANAO adopted the following high-level criteria:

- Defence has a fit-for-purpose sustainment framework between Navy and the Capability Acquisition and Sustainment Group.
- Defence has an appropriate framework to monitor and report on the effectiveness and efficiency of operating the ANZAC fleet.
- Defence effectively administers the ANZAC sustainment strategic partnership to achieve specified availability and performance outcomes.

The audit concluded:

- While the ANZAC class frigates are meeting Navy's current capability requirements and continue to be deployed on operations in Australian, Middle Eastern and Asia-Pacific waters, Defence has been aware since at least 2012 that sustainment arrangements have not kept pace with higher than expected operational usage. Further, Defence cannot demonstrate the efficiency or outcomes of its sustainment arrangements, as the necessary performance information has not been captured. Defence will need to address relevant shortcomings in its sustainment arrangements to meet the requirement that the ANZAC class remain in service for an extra 10 years to 2043, pending the entry into service of the replacement Hunter class.
- The effectiveness of Defence's framework for sustaining the ANZAC class frigates has been reduced because the sustainment plans and budget outlined in the ANZAC class Product Delivery Schedule in Navy's Materiel Sustainment Agreement do not align with the frigates' higher than expected operational use. Defence has been aware of this misalignment since at least 2012.
- Defence's advice to the government to extend the ANZAC class' life-of-type to 2043 was not based on a transition plan or informed by an analysis of the frigates' physical capacity to deliver the required capability until then. Navy will need to address potential risks, relating to the frigates' material condition, to maintain seaworthiness and capability.
- Defence has established a performance framework for the ANZAC class frigates' sustainment, with performance measures included in the Materiel Sustainment Agreement and reports provided to senior Defence leaders. While the performance measures adopted by Defence are relevant, the performance framework is not fully effective because the performance measures are:
 - only partially reliable — as targets and/or plans regularly change; and
 - not complete — as the measures do not address sustainment outcomes and efficiency.In 2017–18 most of the Key Performance Indicators reported against were consistently not met.
- The transparency of external reporting on the ANZAC frigates' sustainment expenditure is reduced as it does not include Defence staffing costs or operational sustainment expenditure.
- Defence entered into a sole sourced alliance contract with its existing industry partners, without a competitive process.
- It is too early to assess the effectiveness of Defence's administration of the new contracting arrangements, known as the Warship Asset Management Agreement, which took full effect in

January 2018 after an 18-month transition period. Defence's regular internal performance reporting and monitoring does not capture the performance of the Agreement.

The ANAO recommended:

- Defence update the ANZAC class Product Delivery Schedule of the Navy Materiel Sustainment Agreement to align sustainment plans for the ANZAC class frigates with their operational use and material condition.
- In the context of developing its transition plan for the ANZAC class life-of-type extension, Defence review the capital and sustainment funding required to maintain the ANZAC class frigate capability until 2043, and advise the Government of the funding required to meet the Government's capability requirements for the class or the capability trade-offs to be made.
- Defence review the key performance measures for the ANZAC class frigates' sustainment to ensure they are reliable and complete.
- To align with the strategic planning approach outlined in the Defence Integrated Investment Program, Defence develop guidance in the Capability Life Cycle Manual on when a proposal to establish or amend a sustainment program should be provided to the Defence Investment Committee and the Minister for Finance for consideration.
- Defence refine its performance reporting and management arrangements for the ANZAC class frigates by aligning Key Performance Indicators in the Warship Asset Management Agreement and those in the ANZAC class Product Delivery Schedule of the Navy Materiel Sustainment Agreement.

Report no. 39 of 2017–18, *Naval Construction Programs—Mobilisation* assessed the effectiveness to date of the Department of Defence's (Defence) planning for the mobilisation of its continuous shipbuilding programs in Australia. To form a conclusion against the audit objective, the ANAO adopted the following high-level criteria:

- Defence has developed an integrated approach to the mobilisation of its shipbuilding programs;
- Defence has developed fit-for-purpose plans for each of its shipbuilding programs, which address key requirements, schedules and enablers; and
- Defence has commenced mobilisation activities in accordance with relevant plans and government decisions.

The audit concluded:

- Defence continues to work towards effective planning and mobilisation to deliver the Australian Government's Naval Shipbuilding Plan. Successful implementation will depend on actively managing the high to extreme levels of associated risk. While the key elements for success have been identified through the Naval Shipbuilding Plan—focussing on infrastructure, workforce, the industrial base, and a national approach—progress in the planning and delivery of those key elements is mixed. High-level governance arrangements to coordinate and advise on implementation of the Plan are still evolving. Defence is currently meeting scheduled milestones to deliver the Offshore Patrol Vessel, Future Frigate and Future Submarine construction programs, although each program is still at an early stage.

- Defence has identified the key elements for a successful continuous shipbuilding enterprise. The Australian Government identified four key program enablers in its 2017 Naval Shipbuilding Plan—infrastructure, workforce, the industrial base, and a national approach. Implementation of the Plan is based on ‘guiding principles’ adopted by the Government, which were informed by lessons learned from previous Australian shipbuilding programs including the Collins Class submarine and Hobart Class Destroyer. The guiding principles focus on achieving productivity, the selection of mature ship designs¹, limiting unique Australian design changes, and adopting an integrated approach to design and construction.
- At this early stage, the effectiveness of governance arrangements cannot be established. In response to internal governance reviews, Defence appointed a senior responsible officer for the Plan in early 2018. A framework of senior advisory and coordinating committees has also been established.
- Defence’s planning and mobilisation activities relating to the four key enablers of the Naval Shipbuilding Plan remain a work in progress. Specifically:
 - short term shipbuilding infrastructure requirements have been identified and construction of infrastructure has commenced, with longer term requirements under development;
 - a workforce plan for the naval construction programs as a whole is currently under development, however, the cost-effectiveness of Defence’s approach to maintaining a shipbuilding workforce between the end of the Hobart Class Destroyer build and the new surface ship programs has not been established;
 - the broad areas of industrial reform required to achieve productive and cost-effective naval construction programs have been identified, but there has been no decision how these reforms might be achieved; and
 - initial activities have commenced towards adopting a national approach.
- Defence is currently meeting scheduled milestones for the naval construction programs, noting that each program is in its early stages. Over time, Defence has advised the Government of the high to extreme risks the shipbuilding programs present. Certain risks are now being realised, including the progress of the Offshore Patrol Vessel through second gate approval without detailed sustainment costs and finalised commercial arrangements.
- Defence has not updated its cost assumptions for its naval construction programs to reflect the earlier design and build milestones for its surface ships and the decision to build the Future Submarine in Australia.

The ANAO recommended that Defence, in line with a 2015 undertaking to the Government, determine the affordability of its 2017 Naval Shipbuilding Plan and related programs and advise the Government of the additional funding required to deliver these programs, or the Australian Defence Force capability trade-offs that may need to be considered.

¹ The Future Submarine is not subject to military-off-the-shelf design constraints. This reflects the Government’s policy that the Future Submarine will be a developmental acquisition.

Report no.48 of 2016–17, *Future Submarine — Competitive Evaluation Process* assessed the effectiveness of Defence's design and implementation of arrangements to select a preferred Strategic Partner for the Future Submarines Program. To form a conclusion against the objective, the ANAO adopted the following high-level audit criteria:

- Defence designed a fit-for-purpose process for evaluating and selecting an international partner for the Future Submarine program, and to support the establishment of a sovereign capability to sustain the Future Submarine Fleet.
- Defence effectively implemented the agreed evaluation process to select an international partner for the Future Submarine program, and to support the establishment of a sovereign capability to sustain the future submarine fleet.

The audit concluded that Defence had effectively designed and implemented a competitive evaluation process to select an international partner for the Future Submarine program.

There were no recommendations made in this report.