

Chapter 1

Introduction

1.1 On 25 June 2014, the Senate referred the matter of the future of Australia's naval shipbuilding industry to the Senate Economics References Committee for inquiry and report by 1 July 2015. The term of reference for the inquiry is straightforward yet comprehensive in its coverage—the future sustainability of Australia's strategically vital naval ship building industry.

Conduct of inquiry

1.2 The committee advertised its inquiry on its website and in *The Australian* seeking views directly from a range of people interested in the future of Australia's naval shipbuilding and repair industry. In addition, the committee wrote to, and invited submissions from, shipbuilders, suppliers, unions, professional associations and individuals engaged in the shipbuilding industry such as engineers and architects as well as academics and economists. The committee also invited state governments and relevant Commonwealth government departments to lodge written submissions.

Submissions and hearings

1.3 The committee received 38 submissions, eight supplementary submissions as well as additional information, which are listed at Appendix 1. The committee also received over 250 brief messages supporting strongly Australia's naval shipbuilding industry and urging the government to ensure that the future submarines would be built in Australia. In all, the committee held eight public hearings. The following were held in 2014:

- 21 July in Canberra, which concentrated solely on the tender for the navy's two new supply ships;
- 30 September in Canberra, which focused on the acquisition of the future submarines;
- 8 October in Newcastle;
- 13 October in Melbourne; and
- 14 October in Adelaide.

1.4 The committee also held three hearings in 2015 on 19 February in Canberra; 6 March in Melbourne; and 14 April in Adelaide. A list of witnesses is at Appendix 2.

1.5 It is also worth noting that during the main round of estimates hearings in late May/early June 2015, two Senate committees took evidence on matters that relate to this inquiry, including a comprehensive examination of representatives from the ASC on progress with the Air Warfare Destroyers (AWDs). The committee has drawn on this evidence in order to provide information on recent developments.

1.6 References to the committee Hansard are to the proof Hansard and page numbers may vary between the proof and the final Hansard transcripts.

Site visits

1.7 The committee also undertook site visits to shipbuilding and Defence facilities. In Melbourne, the committee visited the BAE Systems Williamstown dockyard and, accompanied by Captain Craig Bourke and Mr Bill Saltzer, toured BAE facilities including the plate shop, panel line and profile cutter, a module hall, blast and paint, the dry dock and slipway. The committee also inspected the Landing Helicopter Dock (LHD) ships at Nelson Pier.

1.8 In Adelaide, committee members visited the AWD Systems Centre, where they were briefed by Mr Warren King, CEO, Defence Materiel Organisation (DMO), Mr Peter Croser, AWD Program Manager and Commodore Steve Tiffen, General Manager Stakeholder Engagement. Committee members met Mr Roger Duffield, AWD Platform System Coordinating DAR and toured ASC's AWD shipyard to see progress on construction of AWD Ship 01 and Ship 02.

1.9 Committee members then visited ASC North, where Commodore John Chandler provided an introductory briefing. Members toured the shipyard to view maintenance reforms and work being carried out on the submarines. They inspected a Collins class submarine. To conclude the visit, ASC CEO, Mr Stuart Whiley, provided an ASC presentation and was available to answer questions.

First report, Part I—tender process for navy's new supply ships

1.10 As part of this broad inquiry into Australia's naval shipbuilding industry, the committee resolved to inquire into the tender process for the Royal Australian Navy's (RAN) new replenishment ships as its first order of business. The committee's decision was prompted by the government's announcement on 6 June 2014 that it had given approval for Defence to conduct a limited competitive tender between Navantia of Spain and Daewoo Shipbuilding and Marine Engineering of South Korea (DSME) for the construction of two replacement Auxiliary Oiler Replenishment (AOR) ships. The then Minister for Defence, Senator the Hon David Johnston, explained that the decision to exclude Australian companies from the tender and involve only two overseas companies was due to: the urgent need to replace the vessels and avoid a capability gap; the current low productivity of shipbuilders involved with the AWD project; and value for money considerations.¹

1.11 During this inquiry into the acquisition of the AORs, the committee considered the strategic importance of the replenishment or supply ships to the

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

Australian Navy; the capacity of Australian industry to build the ships; and the contribution that such construction could make to sustaining Australia's naval shipbuilding industry. Evidence taken on the tender process for the new supply ships highlighted a number of concerns. They related to the lack of contestability and competition in the proposed limited tender, the lack of industry engagement in the process undertaken so far and the absence of long-term strategic planning that led to the decision.²

1.12 In particular, the committee found that Defence had not consulted industry or encouraged open discussion about possible Australian engagement with the project. Indeed, it appeared as though local shipyards were shut out of all consideration. In this regard, the committee formed the view that Defence should have consulted local shipyards and allowed them to present their case when it came to building the supply ships in Australia. The committee was not convinced that the government's choice of a limited tender involving only two companies was the best way to obtain the necessary information to proceed to second pass.³

1.13 The committee also believed that the way in which the decision for a limited tender was taken and announced was a significant blow to Australian industry. The absence of consultation was at odds with Defence's stated industry policy objectives, which seek to promote competitive, collaborative and innovative industry in Australia.⁴

1.14 Overall, the committee concluded that decisions, such as the acquisition of the supply ships, were extremely important for both defence capability and for the sustainability of defence industry in Australia. These critically important decisions involve huge amounts of taxpayers' money and have long-term implications for the navy's future procurement strategies and, importantly, its capability. In the committee's view, such decisions should be well considered, based on sound research and analysis, and informed through close consultation with industry. The committee recommended that the tender process for the two supply ships be opened up to allow all companies, including Australian companies, to compete in the tender and, furthermore, to make clear in the tender documents that a high value would be placed on Australian content in the project.⁵

1.15 The committee tabled its first report on the tender for the navy's new supply ships on 27 August 2014. The report is available on the committee's website.

2 Senate Economics References Committee, Part 1, *Future of Australia's naval shipbuilding industry: Tender process for the navy's new supply ships*, August 2014, p. 98.

3 Senate Economics References Committee, Part 1, *Future of Australia's naval shipbuilding industry: Tender process for the navy's new supply ships*, August 2014, pp. xii–xiii and 93–98.

4 Senate Economics References Committee, Part 1, *Future of Australia's naval shipbuilding industry: Tender process for the navy's new supply ships*, August 2014, p. 98.

5 Senate Economics References Committee, Part 1, *Future of Australia's naval shipbuilding industry: Tender process for the navy's new supply ships*, August 2014, pp. xiii and 98.

Second report, Part II—acquisition of future submarines

1.16 Shortly after presenting its first report, the committee's focus was drawn to developments regarding the future submarine project. The statement by the Foreign Minister in August 2014 that discussions with Japan had included the possibility of purchasing 'entire submarines' fuelled public speculation that the government planned to break its commitment to build 12 submarines in Adelaide. The major concern centred on the possibility that the government was about to make pre-emptive decisions that would effectively shut down potential and viable avenues for acquiring the submarines and would again opt for a limited tender. Questions were also raised about the effects that such a decision would have on the future of Australia's shipbuilding industry and the overall success of the future submarine project. Rather than subside, talk of a possible agreement with Japan to acquire submarines for the Australian Navy, without a genuine competitive process, persisted.⁶

1.17 In light of these developments, the committee resolved on 25 September 2014 to hold public hearings to further investigate the various statements and assumptions about the future submarine project. As noted earlier, the committee held public hearings in Canberra on 30 September; Newcastle on 8 October; in Melbourne on 13 October; and in Adelaide the following day, where it took evidence on the future submarine project.

1.18 Given the seriousness of the matter and the thrust of the evidence being gathered, the committee resolved on 28 October 2014 to present its findings to the Senate in the form of a second report that was dedicated to the future submarines. The committee took this step because it feared that critically important decisions were about to be made without adequate public consultation and, moreover, without a fair, proper and transparent competitive tender process.

1.19 In this second report, the committee recognised the immense national importance of the future submarine project and of every decision relating to the project. The committee highlighted the vital importance of having ideas and proposals thoroughly tested and assumptions about the future submarines objectively and critically assessed by competent personnel in order to provide government with the

6 See for example, Minister for Defence—Transcript—Interview with Tony Jones, 'Lateline', 27 August 2014, <http://www.minister.defence.gov.au/2014/08/27/minister-for-defence-transcript-interview-with-tony-jones-lateline-3/>; ABC News, 'Japanese submarine experts visit Adelaide, sparking fears for shipbuilding future', 27 August 2014, <http://www.abc.net.au/news/2014-08-27/japanese-delegates-spark-fears-submarine-future/5699076>; 'Johnston plays down SA submarine fears', 27 August 2014, <http://www.news.com.au/national/breaking-news/sa-govt-fears-over-submarine-project/story-e6frfku9-1227038567300>; Minister for Defence—Transcript—Interview with Justin Smith, 2UE Drive, 9 September 2014, <http://www.minister.defence.gov.au/2014/09/09/minister-for-defence-transcript-interview-with-justin-smith-2ue-drive/> (accessed 27 September 2014); ABC News, 'Soryu submarine deal: Japanese insiders warn submarine program will cost more, hurt Australian jobs', <http://www.abc.net.au/news/2014-09-15/japanese-concerns-over-submarine-deal/5743022> (accessed 27 September 2014).

best possible advice. In its view, open and informed debate would confer much needed transparency on government decisions; it would allow genuine scrutiny of government decisions and provoke robust and informed analysis. Such a process would also be a means of garnering public, industry and multi-partisan political support for the proposed acquisition. Overall, the committee asserted that the decision to acquire the future submarines was a decision in the national interest and should be owned by Australians.

1.20 The committee's second report was intended to start this process of much needed transparency and informed debate on the acquisition of the future submarines. On presenting this report, the committee encouraged all those interested in the purchase of the future submarines to assess critically the evidence taken by the committee and to agitate for a more open and inclusive process. The committee's principal recommendations were that the government:

- not enter into a contract for the future submarine project without conducting a competitive tender for the boats, including a funded project definition study;
- begin this competitive tender immediately;
- ensure a submarine capability gap is avoided;
- given the weight of evidence about the strategic, military, national security and economic benefits, require tenderers for the future submarine project to build, maintain and sustain Australia's future submarines in Australia;
- formally and publically rule out a military-off-the-shelf (MOTS) option for Australia's future submarines; and
- strengthen and build a more collaborative relationship with Australia's Defence industry and engender a co-operative environment in which industry is encouraged to marshal its resources in support of a broader Australian shipbuilding industry capable of acquiring and building a highly capable fleet of submarines.⁷

1.21 The report is available on the committee's website.

1.22 To date, the government has not responded to the committee's recommendations on the future submarines but has announced significant developments including the government's intention to conduct a competitive evaluation process. This matter is discussed thoroughly in chapter 3.

Part III—the future of naval shipbuilding in Australia

1.23 This third report on the future of Australia's naval shipbuilding further develops and expands on the findings of its first and second reports but looks beyond the acquisition of the supply ships and submarines. In this third report, the committee

7 Economics References Committee, Part II, *Future of Australia's naval shipbuilding industry: Future submarines*, November 2014, p. ix.

examines developments since it tabled its second report in November 2014, including the publication of a number of major studies—*Keeping Major Naval Ship Acquisitions on Course: Key Considerations for Managing Australia's SEA 5000 Future Frigate Program* and *Australia's Naval Shipbuilding Enterprise: preparing for the 21st Century*.⁸ The Acquisition and Technology Policy Center of the RAND Corporation produced both reports and the Australian Department of Defence sponsored the work.⁹

1.24 Other developments since November 2014 include: tabling of the government's response to the committee's first report on the new supply ships; the appointment of a new Minister for Defence in December 2014; the announcement that Defence would conduct a competitive evaluation process for the future submarines; and importantly the completion of an independent audit of the AWD project.¹⁰ The government has also made a number of significant announcements that have a direct bearing on the future of naval shipbuilding in Australia. For example, on 25 March 2015, the Minister announced the development of an enterprise-level Naval Shipbuilding Plan.¹¹

Structure of the report

1.25 Although the committee's first and second reports dealt with the tender process for the navy's new supply ships and the pre-tender process for the future

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- 8 Schank, John F., Mark V. Arena, Kristy N. Kamarck, Gordon T. Lee, John Birkler, Robert Murphy and Roger Lough. *Keeping Major Naval Ship Acquisitions on Course: Key Considerations for Managing Australia's SEA 5000 Future Frigate Program*, Santa Monica, CA: RAND Corporation, 2014, http://www.rand.org/pubs/research_reports/RR767 (accessed 18 May 2015); Birkler, John, John F. Schank, Mark V. Arena, Edward G. Keating, Joel B. Predd, James Black, Irina Danescu, Dan Jenkins, James G. Kallimani, Gordon T. Lee, Roger Lough, Robert Murphy, David Nicholls, Giacomo Persi Paoli, Deborah Peetz, Brian Perkinson, Jerry M. Sollinger, Shane Tierney and Obaid Younossi, *Australia's Naval Shipbuilding Enterprise: Preparing for the 21st Century*, Santa Monica, CA: RAND Corporation, 2015, http://www.rand.org/pubs/research_reports/RR1093.html (accessed 30 June 2015).
- 9 In September 2014, the Government commissioned RAND to conduct a detailed review of the Australian naval ship building industry. According to the Minister for Defence, the report is one of the most detailed studies undertaken into the Australian naval shipbuilding industry. Department of Defence Ministers, Minister for Defence—Release of the RAND Corporation report, 16 April 2015, <http://www.minister.defence.gov.au/2015/04/16/minister-for-defence-release-of-the-rand-corporation-report/> (accessed 18 May 2015).
- 10 Department of Defence Ministers, Minister for Defence—Speech—RUSI Submarine Summit, 25 March 2015, <http://www.minister.defence.gov.au/2015/03/25/speech-rusi-submarine-summit-25-march-2015/> (accessed 18 May 2015). Department of Defence Ministers, Minister for Defence—Minister Andrews welcomes Defence appointment, 21 December 2014, <http://www.minister.defence.gov.au/2014/12/21/minister-for-defence-minister-andrews-welcomes-defence-appointment/> (accessed 18 May 2015).
- 11 Department of Defence Ministers, Minister for Defence—Speech—RUSI Submarine Summit, 25 March 2015, <http://www.minister.defence.gov.au/2015/03/25/speech-rusi-submarine-summit-25-march-2015/> (accessed 18 May 2015).

submarines respectively, the committee also made findings applicable to the broader topic of Australia's future shipbuilding industry. By necessity and for completeness, the committee provides a brief summary of its earlier findings where required in this third report and builds on them in order to explore fully a number of key aspects of Australia's naval shipbuilding industry. The report comprises 7 chapters including this introduction. In summary:

- Chapter 2—considers the government's response to the recommendations made in the committee's first report, which provides a solid platform for further exploration of matters such as competitive tendering and the role, importance and sustainability of Australia's naval shipbuilding and repair industry;
- Chapter 3—assesses developments in the acquisition process for the future submarines, including a number of government announcements on the progress made on the competitive evaluation process;
- Chapter 4—looks at Australia's naval shipbuilding and repair industry—its productivity, including an assessment of the various audits on the performance of the AWD project, implementation of the third reform strategy, the critically important supply chain, and the training and recruitment of the workforce;
- Chapter 5—examines the impending gap in ship production, whether it is inevitable and/or the extent to which it could be mitigated or overcome including the consequences of the current downturn in production for Australia's naval shipbuilding workforce and for the future of naval shipbuilding in Australia;
- Chapter 6—focuses on the need for a national strategic naval shipbuilding plan, comparing government announcements, stated commitments and key policy documents (white papers, Defence Capability Plan and the announced enterprise-level Naval Shipbuilding Plan) with the day-to-day experiences in the shipyards;
- Chapter 7—brings together the findings contained in parts I and II of its reports and in this third report and presents its final recommendations.

1.26 While this report is intended to be a standalone document, by necessity it draws heavily on the evidence taken from its two earlier reports. To avoid duplication but to give coherence, the committee, where relevant throughout this report, provides some background to the committee's findings contained in these earlier reports.

Acknowledgements

1.27 The committee thanks all those who assisted with the inquiry, especially those who made written submissions and attended the committee's public hearings.

