

Chapter 5

An Australian naval shipbuilding sovereign capability

5.1 The Coalition government's naval shipbuilding plan, published in May 2017, reiterated its commitment to developing an Australian naval shipbuilding sovereign capability:

The Government is investing in a sovereign naval shipbuilding and sustainment capability for the long-term, with the firm belief that as a nation we are up to this challenge.¹

5.2 The naval shipbuilding plan explained that possessing a naval shipbuilding sovereign capability was a strategic national asset:

A productive Australian naval shipbuilding and sustainment industry that is able to deliver affordable and achievable naval capability is a strategic national asset. A sovereign capability to achieve that aim is the Government's clear priority.²

5.3 The committee heard evidence in support of an Australian naval shipbuilding sovereign capability. The lack of a shared, clear definition of *sovereign capability*, however, is an obstacle to achieving it. The way the term is used in the Naval Shipbuilding Plan has not assisted in reaching such a definition. Ideally, Australian companies, workers, and products should be involved throughout the entire process. However, the committee heard that there is some difficulty in maintaining local capability throughout key stages of the process, such as the design stage. Further discussion focused on mandating Australian involvement and content in projects, through maximising participation or setting percentage targets specified in legislation or contracts.

5.4 This chapter examines support for an Australia sovereign capability and Australia's involvement in the build and content of programs set out in the naval shipbuilding plan. It examines existing legislation and procurement requirements for Australian Industry Participation and concludes with a discussion of the future use of Australian shipyards.

A sovereign capability

Definition of sovereign capability

5.5 The committee heard a range of definitions of the term 'sovereign capability'. The naval shipbuilding plan outlined the government's understanding of sovereign capability as an industrial capability so essential that it is developed and supported only by Australian defence industry because 'overseas sources do not provide the required availability, security, or warfighting advantages we need for the Australian

1 Department of Defence, *Naval shipbuilding plan*, 16 May 2017, p. 21.

2 Department of Defence, *Naval shipbuilding plan*, 16 May 2017, p. 18.

Defence Force'.³ This translates to naval capabilities for the Australian shipbuilding industry.⁴

5.6 According to Austal, a sovereign (shipbuilding) capability 'is the ability to design, build, sustain, upgrade and export Australian-built vessels, in Australian shipyards by Australian workers'.⁵ Mr Singleton, CEO, Austal, advised the committee that in his view sovereign capability means more than simply 'made in Australia':

It meant conceived, designed, supported and even funded out of this country in a way that gave industry in this country the ability to act as a prime contractor in the export of ships overseas. I think that's a very laudable aim by the government, stated very clearly in the white paper, and I still feel that that is an objective that we should be seeking to achieve.⁶

5.7 Mr Dean Rosenfield, Managing Director, Saab Australia suggested that a definition of sovereign capability should include a focus on developing something new that can be exported:

... it is about having that ability to design from first principles and develop or build something that is for use by your nation and then generates the export potential.⁷

5.8 Mr Mike Deeks, Managing Director, Forgacs Marine and Defence provided a definition of a naval shipbuilding sovereign capability with four key elements: design; construction; acceptance into naval service; and through-life sustainment. These four elements have a number of supporting elements—the facilities and infrastructure, skilled workforce recruitment and training, supply chain development and management, and research and development. Within these elements are capabilities that support Australia's ability to:

...exercise its rights as a sovereign state, in terms of ensuring its security and stability and protection of its national interests in whatever political or security environment [Australia] may find [itself] at the time.⁸

5.9 Mr Deeks identified these capabilities as:

...design intellectual property; construction skills, equipment and facilities; technical understanding of the design philosophy; detailed technical knowledge of ship systems and equipment; reliable and assured access to

3 Department of Defence, *Naval shipbuilding plan*, 16 May 2017, p. 85.

4 For instance, sustainment of the future submarine fleet must be undertaken by a sovereign Australian company, due to the classified nature of the technologies and systems. See Department of Defence, *naval shipbuilding plan*, 16 May 2017, p. 85.

5 AUSTAL, *Submission 58*, p.2.

6 Senate Economics References Committee, *Proof Committee Hansard* (Future of Australia's naval shipbuilding industry), 7 June 2018, p. 26.

7 Senate Economics References Committee, *Committee Hansard*, (*Future of Australia's naval shipbuilding industry*), 4 April 2017, p. 14.

8 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 3 April 2017, p. 40.

original equipment manufacturers to ensure detailed design knowledge and spare part availability; and sufficient knowledge, IP, skills and equipment to allow upgrades and enhancements throughout the life of the vessels...⁹

5.10 At the recent Foreign Affairs, Defence and Trade Legislation Committee's estimates hearing on 29 May 2018, Rear Admiral Gregory Sammut, Head Future Submarine Program, commented that there was no single definition of sovereign capability. However, there are many things Defence is doing to achieve sovereignty, including understanding from Defence's past experiences with the Collins Class submarine program. He stated that in relation to the Future Submarine program, sovereign capability consists of three legs on a tripod:

- Part one—the ability to build the submarines domestically, to manage their upkeep, update and upgrade within Australia. This requires the ability to deploy intellectual property appropriately for that purpose (and rights over intellectual property).
- Part two—the transfer of technology into Australia so that there is the means to make the building, upkeep, updates and upgrades work well.
- Part three—the involvement of Australian industry to make sure that there are resident capabilities in the country to do the work.¹⁰

5.11 The range of definitions of 'sovereign capability' offered by witnesses and submitters reveal some common areas of agreement of what sovereign capability is, or could be. Witnesses and submitters also offered general support for sovereign capability.

Support for a sovereign capability

5.12 The government's 2016 Defence Industry Policy Statement states that securing sovereign industrial capabilities is important for Australian defence security. This is because some capabilities are so important to Australian Defence Force (ADF) missions that only an indigenous industry can provide the required security assurances. Therefore, it is 'critical that the industry base associated with these capabilities is maintained and supported by Defence as sovereign industrial capabilities'.¹¹ A similar reference to providing the ADF with security that cannot be provided by overseas sources can be found in the naval shipbuilding plan's statement on sovereign capability.¹²

5.13 The Hon Malcom Turnbull MP, Prime Minister further reinforced the need for a sovereign naval shipbuilding capability stating:

9 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 3 April 2017, p. 40.

10 Senate Foreign Affairs, Defence and Trade Legislation Committee, *Proof Committee Hansard* (Budget Estimates), 29 May 2018, p. 62.

11 Department of Defence, *2016 Defence Industry Policy Statement*, 2016, p. 23.

12 Department of Defence, *Naval Shipbuilding Plan*, 16 May 2017, p. 85.

... [it] is about national security and it is about economic security. It is about security. It is about opportunity.¹³

5.14 Mr Graeme Dunk, Executive Manager, Australian Business Defence Industry was supportive of building an Australian sovereign capability and the benefits it would bring. He stated that:

[b]uilding sovereign capability will not only grow our industry for future shipbuilding but also improve our capability in maintaining and sustaining our own fleet.¹⁴

5.15 While statements by the government indicated that they were committed to building a naval shipbuilding sovereign capability, witnesses noted that substantial sovereign capability already exists in Australia both in defence and commercial sectors.

5.16 For example, at the 24 May 2017 Senate Finance and Public Administration Legislation Committee Estimates hearing, Mr Mark Lamarre, then Chief Executive Officer, Australian Submarine Corporation Shipbuilding (ASC) expressed support for the establishment of an Australian naval shipbuilding sovereign capability.¹⁵ Lamarre said that Australia has an existing sovereign capability in the government-owned ASC:

... the government have indicated that they are looking for affordable, achievable outcomes for shipbuilding and sustainment. They want an industry that has been reformed and is secure, productive and cost competitive. ASC, as Australia's only builder of complex surface combatants, is sovereign, of course. We are headquartered here and we are owned by Australia...¹⁶

5.17 Mr Peter Horobin, Submarine Institute of Australia, agreed that 'there is a substantial sovereign capability in the country right now and it is pretty close to cutting edge', however, he cautioned that this capability would be lost if it was not utilised.¹⁷ Dr Renilson, President, Australian Division, Royal Institution of Naval Architects, also noted his concern that if existing Australian sovereign design capabilities are not utilised, they will be lost:

13 The Hon Malcolm Turnbull MP, Prime Minister, Senator the Hon Marise Payne, Minister for Defence and the Hon Christopher Pyne MP, Minister for Defence Industry, *Doorstop transcript*, 16 May 2017, Adelaide.

14 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 3 April 2017, p. 33.

15 Senate Finance and Public Administration Legislation Committee, *Committee Hansard* (Budget estimates), 24 May 2017, p. 12.

16 Senate Finance and Public Administration Legislation Committee, *Committee Hansard* (Budget estimates), 24 May 2017, p. 15.

17 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 4 April 2017, p. 33.

If you do not use them then you will lose them. If Australia has a habit of constantly going overseas for such services then it will be difficult to keep the naval architects within Australia current and trained up and able to assist.¹⁸

5.18 Leading examples of Australian sovereign capability that Australian companies own and export around the world include Saab's 9LV combat management system, Austal's aluminium ships, and Incat's high speed passenger ferries. In chapter 6 of this report, the committee discusses Australia's thriving exports industry and support available to SMEs to consolidate further capability in the industry.

Australian content and build

Involvement in the design phase

5.19 A persistent theme arising in the evidence was the importance of Australian industry involvement in the design stage of defence programs. This involvement places Australian industry in the best position to undertake sustainment and repair of ships, and to enable industry to increase its knowledge of the design process for future projects.

5.20 Mr Deeks, Forgacs, supported Australian involvement in the entire shipbuilding process to enable the most qualified and knowledgeable individuals to undertake ship maintenance later on. He stated that the best people to do this are those who have:

...built up a body of knowledge and understanding of the build techniques and the design philosophy. Similarly, the remaining service life of an asset is subject to periodic survey and assessment of the remaining cost of ownership, including enhancements and modernisation versus replacement costs. The know-how and 'know why' behind a submarine or frigate design means that local industry will be able to provide enduring support to such a complex asset.¹⁹

5.21 Dr Martin Renilson, President, Australian Division, Royal Institution of Naval Architects, agreed that Australia should be involved in the design of its ships, to assist with repair and maintenance later on. Dr Renilson explained that:

[It] would be very difficult...to have a situation where Australia does the repair and maintenance but is not involved in the design.

...

If it is only involved in the repair and maintenance you can understand that the people involved would not get to see the big picture and would not understand the whole issues about the ship design when they are conducting maintenance. That in itself can be really quite dangerous if they are making modifications to the ship but do not actually have the original design

18 Senate Economics References Committee, *Committee Hansard (Future of Australia's naval shipbuilding industry)*, 3 April 2017, p. 24.

19 Senate Economics References Committee, *Committee Hansard (Future of Australia's naval shipbuilding industry)*, 3 April 2017, p. 41.

philosophy; if they only have the ship and they are trying to make modifications. Ships are modified during their lifetime as well as repaired. If you are not involved in the original designing it would be much more difficult to safely make the changes or modifications.²⁰

5.22 Australian industry is involved in the design process conducted by Naval Group, with Australians travelling to France.²¹ Naval Group staff will travel to Australia to train Australian industry in building the submarines. Defence will bring white collar workers from Naval Group to Adelaide to train and skill the Australian workforce.²²

5.23 At the 20 June 2017 Canberra public hearing, Rear Admiral Greg Sammut, Head Future Submarine Program, Department of Defence, explained that Australians are currently building both project management and design skills and ensuring the transfer of information and sovereign capability in the process. He stated:

There are project management skills that we are currently building up now in terms of our engagement with Australian industry. Also, our engagement with [Naval Group] in terms of understanding the specifics of the submarine design process that they apply. An important part of this, in selecting [Naval Group], is to ensure that we do not introduce changes to their design processes. It is the experience and skills they have in that design process that we want to make sure is transferred to Australia, and particularly into a company like the [Naval Group] Australia, such that we can be in a position where the management of the program takes place from Australia.²³

5.24 While Australians will be involved in the design stage of the future submarine project, it may not be possible for Australia to create and sustain its own design industry into the future. At the 29 May 2017 Senate Foreign Affairs, Defence and Trade Legislation Committee Estimates hearing, Rear Admiral Greg Sammut, argued that it is not possible for Australia to have a sovereign 'design' capability in relation to submarines. This is because an indigenous design capability is a large and expensive capability that requires regular use to be of long-term benefit. He suggested it is difficult for any one country to maintain the capacity to design a new submarine from 'scratch'. For this reason Defence sought an international partner for support.²⁴

20 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 3 April 2017, p. 25.

21 The Hon Malcolm Turnbull MP, Prime Minister, *Doorstop Transcript*, 16 May 2017, Adelaide.

22 The Hon Malcolm Turnbull MP, Prime Minister, *Doorstop Transcript*, 16 May 2017, Adelaide.

23 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 20 June 2017, p. 25.

24 Senate Foreign Affairs, Defence and Trade Legislation Committee, *Committee Hansard* (Budget estimates), 29 May 2017, p. 136.

Australian industry build and content

5.25 The committee heard that primes managing defence programs should be required to involve Australian industry in these projects. However, there was no clear or consistent understanding of what Australian involvement should mean. No common definition of “involvement”, “content” or “participation” was presented in evidence, and the evidence revealed sharp differences between supporters of minimum percentage targets for Australian industry involvement and supporters of providing opportunities to maximise Australian involvement.

5.26 This lack of clarity about what constitutes Australian involvement means that a project may be described as an 'Australian build' even though it is comprised of substantial foreign content. As Mr Glenn Thompson, Assistant National Secretary, Australian Manufacturing Workers Union (AMWU) informed the committee:

Our experience from what we know on Collins ... the figure was 70 per cent local content, but we know for a fact that many of those companies that were deemed to be local in actual fact sourced the content offshore.²⁵

5.27 Mr Andy Keough, Chief Executive, Defence SA, explained that the distinction between build and content was important, particularly in how Australian involvement is measured. He explained that the value-add component of the content should not be conflated with the labour component of the content. He added:

In some cases, you may have components that are manufactured overseas. They may be shipped to Australia and assembled in Australia and the entire component is then assessed as being AIC [Australian Industrial Capability], whereas in fact the value-adding component of the labour to assemble the parts is only a small component of the total cost of that component.²⁶

5.28 The AMWU suggested one way of measuring Australian content might be the calculation used by Naval Group in its Australian Industry Capability (AIC) Plan, based only on the value 'that has been added by Australian companies and their workers in Australia'. The calculation used in Naval Group's definition of 'Australian Industrial Content' excluded any imported goods and services from Australian content calculation.²⁷

5.29 Although the government has stated that it is committed to maximising Australian involvement and a local build of defence programs, it has not attributed a minimum percentage figure of Australian involvement that primes must meet. Nevertheless, the Minister for Defence Industry advised that the government

25 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 4 April 2017, p. 6.

26 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 4 April 2017, p. 27.

27 Australian Manufacturing Workers Union, *Answers to questions on notice*, 3 and 4 April 2017 hearings (received 12 July 2017).

considered a local build to be 'about 60 per cent or above'.²⁸ The Minister for Defence Industry explained the government is seeking to maximise as much local work as possible, rather than seeking to limit it to a minimum requirement.²⁹ The Minister has not explained why the government believes that reaching a minimum would inhibit striving to reach a maximum.

5.30 Mr Thompson, AMWU, expressed concern that if the government only encouraged primes to aim for maximum participation, primes may argue that Australian SMEs are unsuitable and use their own international supply chains. He stated that despite Defence's advice to Naval Group that it has to maximise Australian participation and include the supply chain into its project, there was nothing to enforce this.³⁰

5.31 Ministers for defence industry from Western Australia, South Australia and Victoria, provided a joint submission stating their shared view on achieving Australian involvement in the future submarine program. The Ministers called for 'a minimum level of Australian participation by value of the contract entered into'.³¹

5.32 Mr John O'Callaghan, Executive Director, Australian Industry Group Defence Council, was supportive of focusing on maximising Australian involvement, stating that it was essential to make sure Defence contracts 'locked in' maximising that content.³²

5.33 Dr Michael Green, Executive Director, Victorian Department of Economic Development, Jobs, Transport and Resources suggested that there are other measures that could be used to promote Australian industry participation. For example, Australian industry value-add and the number of employees or hours worked on a project in Australia. Noting the difficulty of measuring Australian content in relation to intellectual property, Dr Green suggested that a significant build-up of capability around design and engineering beyond 'just operating and sustaining vessels' in the country was desirable.³³

Mandated Australian industry participation

5.34 Evidence presented to the committee supported government mandated Australian industry participation in defence projects. Mr Thompson, AMWU, reiterated his concern that the government had not stipulated precise definitions or

28 The Hon Malcolm Turnbull MP, Prime Minister, *Doorstop transcript*, 16 May 2017, Adelaide.

29 The Hon Malcolm Turnbull MP, Prime Minister, *Doorstop transcript*, 16 May 2017, Adelaide.

30 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 4 April 2017, p. 5.

31 The Hon. Wade Noonan MP, the Hon. Paul Papalia CSC MLA, and the Hon. Martin Hamilton-Smith MP, correspondence received 16 June 2017, p. 1.

32 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 4 April 2017, p. 19.

33 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 4 April 2017, p. 36.

percentage figures of Australian industrial involvement in defence programs. He called for the government to mandate Australian industry participation, stating that the government did 'not come out hard enough' and was 'not transparent enough on what they mean by maximum participation and local content'.³⁴ Mr Thompson called for the government to provide clarity on the meaning of Australian industry participation and 'what they are doing and mandating in relation to Australian content and supply chain'.³⁵

5.35 The Victorian government's submission suggested that local content be mandated similar to the Victorian Industry Participation Policy (VIPP). According to the submission, mandating local content maximises the benefit for the nation and will have a positive multiplier effect—creating business opportunities, underpinning ongoing direct economic benefits through jobs and supply chain creation throughout the county.³⁶

5.36 At the Adelaide public hearing Dr Green restated the Victorian government's position that those measures should be in place to establish a 'robust and achievable local content and for that to be increased over time'. The increase could be achieved:

...both through the life of each vessel and as the vessels get built and for that to be a critical part of the overall plan and contractual arrangements to deliver these programs.³⁷

5.37 The Hon Greg Combet, Victorian Defence Industry Advocate agreed, noting that ultimately it was up to the Commonwealth government to mandate that local content and participation is achieved. He added:

...it will require appropriate determination on the part of the Commonwealth and Defence to ensure that a rigorous approach to the achievement of Australian industrial capability and therefore local content is achieved.³⁸

5.38 Mr Serge DeSilva-Ranasinghe, President, Australian Industry & Defence Network Western Australia, also supported the enforcement of a local industry requirements stating:

We [Australian Industry & Defence Network WA] would like to see enforcement of the sovereign industrial capability that demonstrates, based

34 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 4 April 2017, pp. 5 and 6.

35 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 4 April 2017, pp. 5 and 6.

36 Victorian Government, *Submission 54*, p. 2.

37 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 4 April 2017, p. 35.

38 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 4 April 2017, p. 36.

on evidence, that Australian companies and SMEs are actually getting substantial opportunities.³⁹

5.39 Mr Keough, Defence SA, suggested that the government set mandated requirements. However, he acknowledged that in some projects it may be difficult to reach a high bar of Australian industrial content due to the nature of the work. This would come down to the particular platform—the more complex the project, the harder it is to drive local AIC. Also, the technologies may not be available in Australia.⁴⁰ Mr Keough, added:

Certainly for OPVs it is fairly simple—you should have a very high level of AIC for that. In submarines, particularly in the first stage, it may be a lot lower AIC and then that is built on. Really, that is an issue for the government to look at, make its decision on and set the leadership on. It needs to set the floor, that floor needs to be in the contract and anything above that is a significant bonus to Australia.⁴¹

5.40 Witnesses suggested that the government could mandate Australian industrial participation through contracts between primes and the government to lock in sovereign capability and local industry involvement. Mr Deeks, Forgacs Marine and Defence, argued that:

As the government moves forward with major ship and sovereign acquisition programs, they must put in place contractual mechanisms and intergovernmental agreements and treaties that ensure we have access to, and ownership of, the relevant information to ensure the above-mentioned elements are in our control.⁴²

5.41 Mr Keough, Chief Executive, Defence SA, also suggested that Australian industry requirements be contained within contracts as 'ultimately, the AIC content must be specified in the contract if you are going to have any aspirations of delivering against it'. Otherwise, it would be based on the contractor's best endeavours.⁴³ He emphasised that:

[t]he contractor's responsibility is not to develop the Australian industry. They are there to deliver a submarine, to deliver a product, on time to a specified price to meet a certain capability, so [the] contract [must] make

39 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 3 April 2017, p. 36.

40 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 4 April 2017, p. 27.

41 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 4 April 2017, p. 27.

42 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 3 April 2017, pp. 40 and 41.

43 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 4 April 2017, p. 24.

sure that [it is added] in the contractor's best interest to make sure they hit certain targets that we specify.⁴⁴

5.42 Further, there must also be an incentive for the contractor to comply as it would be naïve to suggest that technology and intellectual property would be transferred from France to Australia without any incentives or motivations simply to assist Australian industry.⁴⁵

5.43 Some witnesses recommended going beyond simply minimum percentage targets, and called for a focus on ensuring that the government attains sovereign control and intellectual property of these naval ship programs. Mr Deeks explained that:

The Australian industry participation should be viewed by the government from a position of the sovereign capability that they wish to have in Australia. It is not a matter of a percentage of Australian industry participation; it is a matter of identifying the key capabilities, the key competencies, the key controls that the Australian government sees as essential in the operation and maintenance of the submarines through their entire life.⁴⁶

5.44 Mr Deeks also suggested that the government be careful to make sure that it has 'an avenue through which it can direct or dictate the terms of the subcontractors supplying into the Future Submarine project to ensure that [Australia] retain[s] that sovereign capability'.⁴⁷ Sovereign capability can be managed through the control of IP, or by ensuring a level of Australian industry participation.⁴⁸ Mr Graeme Dunk also supported this position stating that 'Australia needs to have access to all intellectual property in order to [...] address its sovereignty concern'.⁴⁹

5.45 At the 20 June 2017 Canberra public hearing, Mr Brent Clark, Senior Advisor to the Chairman, Naval Group Australia, explained that in the case of the future submarine program:

44 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 4 April 2017, p. 24.

45 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 4 April 2017, p. 24.

46 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 3 April 2017, p. 44.

47 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 3 April 2017, p. 44.

48 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 3 April 2017, p. 44.

49 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 3 April 2017, p. 27.

[T]he background [IP] obviously resides with the company in France; the foreground IP obviously will reside with the Commonwealth. And there is an arrangement in place to transfer that IP.⁵⁰

5.46 Rear Adm. Sammut, Department of Defence, further explained that:

Any new information that is developed, as is stated in the treaty and elsewhere in our arrangements with [Naval Group], becomes foreground IP, ownership of which vests with the Commonwealth upon its creation.⁵¹

90 per cent Australian build?

5.47 The National Shipbuilding Plan and related documents do not contain official percentage targets of Australian participation rates for building. The committee heard evidence throughout the inquiry that the failure of the government to set clear targets caused confusion amongst stakeholders. Two examples of confusion created by the government, in relation to submarines and frigates, are discussed below.

5.48 For example, at the 4 April 2017 Adelaide public hearing, speculation about what percentage of the future submarine build would take place in Australia was discussed. In the previous month, Naval Group advised that over 90 per cent of the future submarine build would occur in Australia.⁵² On the day of the committee's hearing the Minister for Defence Industry stated that 60 per cent of the future submarines project build would take place in South Australia. The Minister confirmed that the figure of a '90 per cent' Australian build was provided by Naval Group, not the government.⁵³

5.49 The confusion around the percentage of Australian involvement remained during the Adelaide hearing. Mr Thompson, AMWU, noted his surprise at comments made by the Minister for Defence Industry on radio that morning, regarding a change from a 90 per cent Australian build to a 60 per cent South Australian build. Mr Thompson suggested that these comments highlighted the general confusion about Australian participation:

The point that I would make is this, once again: there is no clear public position in relation to the [Request for Tender]—for example, on frigates. It talks about maximum Australian participation; it does not mandate or it does not put any emphasis on the French, for example, or on whoever it is

50 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 20 June 2017, p. 10.

51 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 20 June 2017, p. 25.

52 Joint Standing Committee on Treaties, *Committee Hansard* (Agreement with France on the Future Submarine program, Maritime arrangements with Timor-Leste), 14 March 2017, p. 41. The JSCOT inquiry examined the treaty *Framework Agreement between the Government of Australia and the Government of the French Republic concerning Cooperation on the Future Submarine Program* (Adelaide, 20 December 2016).

53 The Hon Christopher Pyne MP, Minister for Defence Industry, *ABC Radio Adelaide Breakfast*, Transcript, 4 April 2017.

going to be on the frigates, to engage Australian companies to assist Australian companies to be supply-chain ready.⁵⁴

5.50 At the 20 June 2017 Canberra public hearing, and again on 7 June 2018, Mr Clark explained that the 90 per cent figure mentioned by the former Naval Group Australia CEO pertained to assembly and production activities only and not the overall content of the submarine.⁵⁵

5.51 In 2017 Mr Clark stated that he could not confirm what the percentage of Australian industry content would be as Naval Group were still working with the Commonwealth and the Department of Defence. This work included examining the Commonwealth and Department of Defence 'system by system to look at what can be done on the submarine from an Australian industry capability perspective'.⁵⁶ Naval Group would aim for a minimum target of 60 percent industry involvement.⁵⁷ Naval Group expected to complete the work and to refine a figure of Australian industry content by the end of 2017 early 2018.⁵⁸ Mr Clark advised the committee that Naval Group would provide a figure for local content by the end of 2017.⁵⁹ However, at the committee's hearing on 7 June 2018, Mr Clark was still unable to provide a figure.⁶⁰

5.52 Defence Teaming Centre supported the requirement for maximising Australian industry involvement in the future submarine program, suggesting that a more sophisticated solution was required than simply determining a percentage of involvement; this would involve a determination of the meaning of sovereign capability:

The Federal Government must then focus on developing a transparent plan with [Naval Group] as to how and when the knowledge and skills to build

54 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 4 April 2017, p. 6.

55 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 20 June 2017, p. 2. Naval Group, *Answers to questions on notice*, 20 June 2017 hearing (received 13 July 2017). See also, Mr Brent Clark, Senior Advisor to the Chairman, Naval Group Australia, Senate Economics References Committee, *Proof Committee Hansard* (Future of Australia's naval shipbuilding industry), 7 June 2018, pp 18-9.

56 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 20 June 2017, p. 2.

57 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 20 June 2017, p. 12.

58 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 20 June 2017, p. 2.

59 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 20 June 2017, p. 2.

60 See also, Mr Brent Clark, Senior Advisor to the Chairman, Naval Group Australia Naval Group Australia, Senate Economics References Committee, *Proof Committee Hansard* (Future of Australia's naval shipbuilding industry), 7 June 2018, p. 14.

the Future Submarine will be transferred to Australians. Australia will need to make itself ready for this knowledge and skills transfer.⁶¹

5.53 At the June 2018 hearing, Naval Group was questioned again in relation to the former CEO's comment about a 90 per cent Australian build. Mr Clark clarified that his predecessor's comment applied to production and not the overall Australian industry content. Mr Clark confirmed that he could not find any documentation produced by the company that referred to 90 per cent local content.⁶²

5.54 Naval Group has still not provided a figure about the level of content it will use for the submarine program. Mr Clark advised that Naval Group was still in the design phase and would be in a better position to answer the question during the procurement phase. Mr Clark advised that the company has been engaging with Australian industry for nearly three years and the number of prequalified suppliers is growing rapidly. He expressed confidence in what Naval Group has seen from an Australian industrial perspective.⁶³

5.55 Relatedly, the Minister for Defence Industry's reference to a minimum 60 per cent local build (which he defined as Australian content), attracted media attention following the release of unclassified sections of the future frigate program's request for tender documents on 25 January 2018. The documents were subject to a protracted FOI process which included a review by the Information Commissioner. The media reported that the future frigate program would achieve a minimum 50 per cent local content.⁶⁴ The documents stated that the Air Warfare Destroyers (AWD) had achieved Australian contract expenditure of 60 per cent across the whole program, and anticipated that the frigates would achieve the same or higher. Minister Pyne referenced the level of Australian content in the AWD (beyond 60 per cent) and the Collins (beyond 80 per cent) programs as basis for his claim.⁶⁵

5.56 Mr Keough, Defence SA, warned at the April 2017 hearing, when the Naval Shipbuilding Plan had not yet been released, that without a naval shipbuilding plan

61 Defence Teaming Centre, *Answers to questions on notice*, 4 April 2017 hearing (received 17 July 2017).

62 Senate Economics References Committee, *Proof Committee Hansard* (Future of Australia's naval shipbuilding industry), 7 June 2018, pp. 14-15. See also Naval Group, *Answers to questions taken on notice*, 20 June 2017 hearing (received 13 July 2017).

63 Senate Economics References Committee, *Proof Committee Hansard* (Future of Australia's naval shipbuilding industry), 7 June 2018, p. 14

64 More documents were released on 11 May 2018 on the Future Frigate procurement process under the Senate Order for production of document.

65 Andrew Tillett, 'Fresh fight over frigate build as government spruiks local defence industry', *Financial Review*, 30 January 2018, <https://www.afr.com/news/fresh-fight-over-frigate-build-as-government-spruiks-local-defence-industry-20180130-h0qfyn> (accessed 15 June 2018). See also Amelia McMahon, '50 industry participation target for SEA 5000 slammed', *DefenceConnect*, 30 January 2018, <https://www.defenceconnect.com.au/maritime-antisub/1827-50-industry-participation-target-for-sea-5000-slammed> (accessed 18 June 2018).

containing official percentage targets, the confusion and discussion would continue.⁶⁶ Unfortunately, as the two examples outline above illustrate, this remains the case following the release of the naval shipbuilding plan, as plan does not contain percentage targets.

Contracts underway

5.57 Initial contracts for the future submarine program have been signed. As at 20 June 2017, Naval Group had signed approximately \$11 million worth of contracts with 91 Australian subcontractors.⁶⁷ At that time, the value of contracts with French companies exceeded the value of contracts with Australian companies. This increased to 107 subcontracts valued at about \$26 million at the end of May 2018.⁶⁸ The committee heard that the number of contracts signed with Australian companies exceeded the number of contracts signed with French companies over the same period.

5.58 However, without similar figures available to the committee on the number of contracts signed with French companies, the committee cannot fully understand how capabilities are being developed.⁶⁹

2017 Naval Group (formerly DCNS) Australian Industry Capability Plan

5.59 Although the government has not specified any percentage targets (or other measures) for Australian industrial requirements, tenderers bidding for defence contracts must provide an Australian Industry Capability (AIC) plan that sets out how it will maximise Australian industry involvement should it be successful in winning the tender. The successful tenderer then develops a subsequent AIC with the government.

5.60 Non-corporate Commonwealth entities under the *Public Governance, Performance and Accountability Act 2013* (PGPA Act) (which includes the Department of Defence), require successful tenderers to prepare and implement AIC plans for Commonwealth tenders of \$20 million or more.⁷⁰ The Department of Defence procurement policy manual outlines the requirements of the AIC plan:

[T]enderers are required to submit an AIC plan which sets out the tenderers' Local Industry Activities (LIAs) to meet the specified Industry

66 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 4 April 2017, p. 26.

67 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 20 June 2017, p. 9.

68 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 7 June 2018, pp. 17-18.

69 Senate Economics References Committee, *Proof Committee Hansard* (Future of Australia's naval shipbuilding industry), 7 June 2018, pp. 17-18. Figures available for the French side went back to the beginning of April 2017—24 project-related contracts signed with French companies valued at 12.4 million euros [approximately 18.25 million AUD]: Naval Group, *Answers to questions on notice*, 20 June 2017 hearing (received 13 July 2017).

70 Department of Industry, Innovation and Science, *AIP Plans: User Guide*, p. 5.

Requirements of the *procurement*. Tenderers are required to describe the benefits of their LIAs, including the significance of the work, the skills and knowledge that will be transferred, the training that will be provided, the new technologies or innovations that will be introduced, and the contribution to Australian company competitiveness, including access to global supply chains, technical data and intellectual property.⁷¹

5.61 Tenderers are not required to specify a percentage target of Australian industrial involvement, only how they will endeavour to maximise Australian involvement.

5.62 On 30 September 2016, the government and Naval Group signed the Design and Mobilisation contract. The contract required both parties to produce an AIC plan to commence the design phase of the program.⁷² This is in addition to the AIC plan produced earlier by Naval Group as part of Competitive Evaluation Process (CEP) in accordance with the PGPA Act, outlined above. The committee was advised in October 2017 that delays in developing the AIC plan related to establishing security arrangements for Australian companies.⁷³ The government was not provided with a final AIC plan by the Naval Group until April 2018.⁷⁴ Defence has advised that it is working towards releasing the AIC plan by October 2018.⁷⁵ As the committee does not have access to the AIC plan provided to Defence by Naval Group in April 2018, the committee provides some commentary on the contents of the earlier AIC plan.

5.63 Due to delays in preparing the final AIC plan, the committee initially sought access to the AIC plan submitted as part of the CEP. At the 4 April 2017 Adelaide

71 Department of Defence, *Defence Procurement Policy Manual*, April 2017, pp. 12.

72 The Hon Christopher Pyne MP, Minister for Defence Industry, 'First contract signed with Naval Group to commence design phase', *Media release*, 30 September 2016, <https://www.minister.defence.gov.au/minister/christopher-pyne/media-releases/first-contract-signed-dcns-commence-design-phase> (accessed 12 June 2018).

73 Rear Admiral Sammut, Senate Foreign Affairs, Defence and Trade Legislation Committee, *Committee Hansard* (Supplementary estimates), 25 October 2017, pp. 158-159.

74 Rear Admiral Sammut, Senate Foreign Affairs, Defence and Trade Legislation Committee, *Proof Committee Hansard* (Budget estimates), 29 May 2018, p. 57. Defence has also received the Australian Steel Development and Qualification Plan in April 2018. Testing of steel in Australia has commenced, and Bisalloy and Bluescope will be involved in determining its suitability for the construction of the submarine's pressure hull.

75 Senate Foreign Affairs, Defence and Trade Legislation Committee, *Proof Committee Hansard* (Budget estimates), 29 May 2018, p. 57.

public hearing, a copy of the redacted March 2017 Naval Group AIC plan for the future submarine program was tabled.⁷⁶

5.64 The 2017 AIC plan outlined Naval Group's plans, procedures and responsibilities for the management of Australian Industry Capability during the future submarine program.⁷⁷ One interpretation of the document is that any final decision as to the involvement of Australian companies, products and services in the Future Submarine project is a matter for Naval Group, not the Australian government. For example, Mr Thompson, AMWU, expressed concern that the Naval Group AIC plan suggested that Naval Group had the decision making power about what could and could not be built in Australia, noting that when Naval Group 'was announced as the preferred design partner, the French community were dancing on the streets in relation to the establishment of 4,000 jobs in France'.⁷⁸

5.65 At the 20 June 2017 Canberra public hearing, Mr Clark stated that 'the Commonwealth always has the final say in these matters'.⁷⁹ Mr Clark also stated that he would not provide the committee with the percentage figure of Australian involvement outlined in the CEP 'because the plans that were done during the CEP obviously involved a lot of assumptions'.⁸⁰ In a response to questions on notice, Naval Group confirmed that the 90 per cent figure discussed by the former CEO was not provided in any Australian industry participation plan documentation.⁸¹

76 The document was tabled by former Senator Xenophon and was dated March 2017. Although the document indicated that it was a final version, Defence emphasised at the 4 April 2017 hearing that the government has not accepted the document, which based on Naval Group's view of 'the way in which Australian industry engagement will work'. Senate Economics References Committee (Future of Australia's naval shipbuilding industry), *Committee Hansard*, 4 April 2017, p. 25. The Department of Defence received a final version of this document from Naval Group in April 2018, and is working towards providing it to the Senate: Senate Economics References Committee, *Proof Committee Hansard* (Future of Australia's naval shipbuilding industry), 7 June 2018, p.57. The 2015 version of this document, prepared as part of the CEP process, was tabled in the Senate on 10 May 2018, following an order for the production of documents. See *Journals of the Senate*, 12 February 2018, p. 2667. The document is available online:

http://parlinfo.aph.gov.au/parlInfo/download/publications/tailedpapers/f95d14f8-d23d-42ff-bc12-2a503d480d8b/upload_pdf/submarine.pdf;fileType%3Dapplication%2Fpdf (accessed 11 May 2018).

77 Naval Group, *Australian Future Submarine Program: Australian Industry Capability Plan*, March 2017, p. 6.

78 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 4 April 2017, p. 5.

79 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 20 June 2017, p. 9.

80 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 20 June 2017, p. 13. Mr Clark also advised on 7 June 2018 that a number of these assumptions had changed: Senate Economics References Committee, *Proof Committee Hansard* (Future of Australia's naval shipbuilding industry), 7 June 2018, p. 14.

81 Naval Group, *Answers to questions on notice*, 20 June 2017 hearing (received 13 July 2017).

5.66 Mr Clark explained that the CEP was quite a short process and Naval Group was not able to do a robust analysis of Australian industry during this period. However, since Naval Group had been selected as the designer of the future submarine program, Naval Group has 'spent a considerable amount of time travelling around Australia and looking at Australian industry and the capabilities and understanding what exists'.⁸² According to Mr Clark, this process would provide a robust, defensible and justifiable percentage for the committee.⁸³

5.67 On 29 June 2017, the government announced changes to the AIC template to strengthen the requirement for Australian involvement in Defence projects. The new template is intended to require defence companies to outline how and where they will involve Australian industry before bids are considered.⁸⁴

5.68 The Defence Teaming Centre stated that they would expect the Commonwealth to seek supplementary information from Naval Group to ensure its AIC plan meets the new template requirements.⁸⁵ The AMWU stated that it reserved its judgement on the efficacy of the AIC plan. It welcomed the 'strengthened guidelines and additional focus on using defence procurement to foster longer term investment and diversification' but was less optimistic about the new AIC plan requirements. It noted that 'without pressure from government, the plans required under the AIC plan may just become hollow promises sitting forgotten on a government website'.⁸⁶

5.69 On 12 February 2018, the Senate ordered that government table the AIC plan submitted by Naval Group to the Department of Defence as part of the CEP for the submarines.⁸⁷ The Minister for Defence tabled the document on 10 May 2018. The document, created in 2015, contained redactions on the grounds of public interest immunity. There have been some criticisms about the material that remains, not least that the Naval Group initially planned to use 1,700 ASC employees.⁸⁸ During the

82 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 20 June 2017, p. 12.

83 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 20 June 2017, p. 13.

84 The Hon Christopher Pyne MP, Minister for Defence Industry, 'Turnbull Government moves to increase Australian involvement in Defence Projects', *Media release*, 29 June 2017.

85 Defence Teaming Centre, *Answers to questions on notice*, 4 April 2017 hearing (received 17 July 2017).

86 Australian Manufacturing Workers Union, *Answers to questions on notice*, 3 and 4 April 2017 hearings (received 12 July 2017).

87 *Journals of the Senate*, 12 February 2018, p. 2667. The document is available online: http://parlinfo.aph.gov.au/parlInfo/download/publications/tailedpapers/f95d14f8-d23d-42ff-bc12-2a503d480d8b/upload_pdf/submarine.pdf;fileType%3Dapplication%2Fpdf (accessed 11 May 2018). The order was on the motion of Senator Patrick.

88 See for example, *Defence Connect*, 'Naval Group's Australian Industry Plan released', 12 May 2018, <https://www.defenceconnect.com.au/maritime-antisub/2280-naval-group-s-australian-industry-plan-released> (accessed 14 May 2018).

committee's hearing on 7 June 2018, Naval Group advised that the assumptions made when developing the 2015 AIC plan had changed by the time it completed a later plan in 2017. In particular, Naval Group were not aware of the government's intention that the designer of the submarines would also build the submarines.⁸⁹

The Merchant Marine Act of 1920 (The Jones Act)

5.70 At the Adelaide public hearing, Mr David Singleton, Chief Executive Officer, Austal, informed the committee about the United States Jones Act,⁹⁰ which enshrines the United States' shipbuilding sovereign capability by requiring all shipbuilding work to take place in the United States.⁹¹ Mr Singelton explained that:

The Jones Act is a piece of legislation in the United States that requires that any commercial vessel that goes port to port in the US or any military vessel in the United States is built in the United States. It also requires that certain maintenance activities on military ships are also carried out in US ports as well. So it is not possible by law in the United States to build ships anywhere other than in continental US for defence purposes.⁹²

5.71 Section 1 of the Jones Act outlines the purpose of the Act:

It is necessary for the national defense and for the proper growth of its foreign and domestic commerce that the United States shall have a merchant marine of the best equipped and most suitable types of vessels sufficient to carry the greater portion of its commerce and serve as a naval or military auxiliary in time of war or national emergency, ultimately to be owned and operated privately by citizens of the United States; and it is declared to be the policy of the United States to do whatever may be necessary to develop and encourage the maintenance of such a merchant marine, and, in so far as may not be inconsistent with the express provisions of this Act, the Secretary of Transportation shall, in the disposition of vessels and shipping property as hereinafter provided, in the making of rules and regulations, and in the administration of the shipping laws keep always in view this purpose and object as the primary end to be attained.⁹³

5.72 Mr Matthew Primiero, an AMWU delegate, explained the impact of the Jones Act on the shipbuilding industry:

89 Mr Clark, Senior Advisor to the Chairman, Naval Group Australia, Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), pp. 11-12.

90 Formally known as the *Merchant Marine Act of 1920*.

91 Observers have noted that while the Jones Act requires ships to be assembled in the US, foreign parts, investment and expertise are often utilised. Bryan Riley, 'Are Jones Act ships really 'made in the USA'? Well, sort of', *The Hill.com*, 6 July 2016, <http://thehill.com/blogs/pundits-blog/transportation/282455-are-jones-act-ships-really-made-in-the-usa-well-sort-of> (accessed 7 August 2017).

92 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 3 April 2017, p. 10.

93 *Merchant Marine Act of 1920* (United States of America), section 1.

The Jones Act in the US is anything built and sought in the US. Any defence contract is done in the US with US labour. It allows outside companies to bid for the work, but it puts a tax on them...[but they] still has to use US labour.⁹⁴

5.73 Mr Singleton explained that in order for Austal to undertake work for the United States government, ships had to be built in the United States by local workers. Austal currently has approximately four and a half thousand employees in the United States.⁹⁵ Mr Singleton explain that when establishing the Austal shipyard in the United States:

We took 300 Australians from Henderson—from the design and product areas at Henderson—to Mobile, Alabama to set up the facilities. They designed not only the vessel and then modified it to the needs of the US Navy but also the manufacturing system, which is extremely novel and the most efficient manufacturing system for warships in the United States—and that was all done with Australians in the US.⁹⁶

5.74 Australia does not have an equivalent piece of legislation in relation to mandating Australian industry involvement and content in the construction of Australian naval vessels. The *Australian Jobs Act 2013*(Cth) requires consideration of Australian involvement in procurements through Australian Industry Plans, discussed above in relation to the Naval Group Australian Industry Plan. However, the Act does not mandate the use of Australian entities, only that Australian entities should have full, fair and reasonable opportunity to bid for the supply of key goods or services for a project or a new facility's initial operational phase.⁹⁷

Australian industry participation in the future submarine program

5.75 On 7 June 2018, the committee was advised Naval Group issued 1,623 requests for information to 541 Australian companies.⁹⁸ This was an increase from the previous year where there had been 793 requests for information to 174 companies.⁹⁹ In 2017, it pre-qualified 52 Australian companies who were considered appropriate to

94 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 4 April 2017, p. 3.

95 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 3 April 2017, p. 10.

96 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 3 April 2017, p. 11.

97 Australian Industry Participation Authority, *User Guide for developing an Australian Industry Participation Plan*, June 2016, p. 4.

98 Senate Economics References Committee, *Proof Committee Hansard* (Future into Australia's naval shipbuilding industry), 7 June 2018, p. 18

99 Senate Foreign Affairs, Defence and Trade Legislation Committee (Additional Estimates 2016-17), *Answer to question on notice*, Question reference no. 49.

participate in supply chain activities for the future submarines program.¹⁰⁰ This number increased to 86 as at 1 May 2017.¹⁰¹

5.76 The committee notes the lack of comparable information on the French side made it difficult for the committee to assess whether Australian or French companies were getting the majority of contracts. Mr Clark from Naval Group Australia agreed to provide the information to the committee as soon possible, noting the inquiry's tight reporting date of 27 June 2018.¹⁰²

Australian shipyards

5.77 The naval shipbuilding plan set out infrastructure upgrades required for shipyards in both South Australia and Western Australia to enable construction of programs outlined in the plan.

5.78 As outlined in chapters two and three, following Defence's assessment that current shipyards in Osborne and Henderson were inadequate and required substantial upgrades to meet the requirements of the naval shipbuilding programs, Defence contracted Odense Maritime technology to redesign the shipyard at Osborne and allocated \$100 million to improve the infrastructure at the Henderson shipyard. The ANAO reported that work on the physical infrastructure at the Osborne (south) shipyard was already underway and is on track for the future frigate's commencement. The infrastructure requirements at the Henderson shipyard for the offshore patrol vessel program are in the process of being finalised whereas the shipyard requirements for the future submarines at Osborne (north) are still at an early stage.¹⁰³

Infrastructure for build of future submarines

5.79 The committee heard that the future submarine program would not use the existing Collins facilities in Techport, but that facilities for the build of the future submarines will be built and designed to meet the requirements of the program. Rear Adm. Sammut noted the facilities used by the Collins submarines were designed and built in the early 1980s. It was necessary to build a shipyard with the capacity to efficiently and effectively build a submarine that is designed differently to the Collins one and 'can continue to build submarines on a rolling acquisition program'.¹⁰⁴

5.80 The committee was informed that the new facilities for the future submarines will be built around existing facilities used for the sustainment of the Collins class.

100 Senate Foreign Affairs, Defence and Trade Legislation Committee (Additional Estimates 2016-17), *Answer to question on notice*, Question reference no. 50.

101 Senate Foreign Affairs, Defence and Trade Legislation Committee, *Committee Hansard* (Budget estimates), 29 May 2017, p. 59.

102 Senate Economics References Committee, *Proof Committee Hansard* (Future of Australia's naval shipbuilding industry), 7 June 2018, p. 18.

103 Australian National Audit Office, Audit Report No. 39 2017-18, *Naval Construction Programs—Mobilisation*, pp. 9-10.

104 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 20 June 2017, p. 20.

These new facilities will have to be built to match Naval Group's design and build processes and provide Defence with 'the ability to efficiently build submarines into the future'. Rear Admiral Sammut advised:

There has to be a new whole construction hall. There has to be facilities for the building of modules. There will be land-based test sites that are necessary and so forth that currently do not exist on the existing ASC site.¹⁰⁵

Sustainment

5.81 At the 20 June 2017 Canberra public hearing, the committee heard that Defence was seeking to ensure that Australia obtains the sovereign sustainment capability for the future submarines through the appropriate transfer of information and technology. Rear Admiral Sammut advised that one of the lessons learnt from the Collins class program was the importance of obtaining the sovereign sustainment capability:

One of the key lessons of the Collins program was that, regardless of the level of Australian industry involvement that we had, we did not end that program with the sovereign sustainment capability. In other words, the enduring industrial capability in Australia to look after the boats through time. It is only at this point in the boats lives, through the improvements and transformations that ASC have been largely involved in, that we have developed that capability. So we are working on the mechanisms now to make sure the transfer of that information and technology into Australian industry occurs so that we have those outcomes.¹⁰⁶

Future location of sustainment of Collins

5.82 In April 2016 the Prime Minister stated that that all heavy sustainment work would remain in South Australia:

Sustainment at the moment is done both between Henderson [Perth] and Osbourne [Adelaide] and that would continue...it will be shared between the two but the heavier work was obviously always going to be done here at Osbourne, as it is now.¹⁰⁷

5.83 Defence stated that there was no decision to move sustainment of the Collins class from Adelaide. Rear Adm. Sammut stated that was no plan 'at this stage' to change the current arrangements 'whereby full-cycle dockings are conducted in Adelaide on the Collins submarines and other dockings an maintenance activities are conducted in Western Australia.'¹⁰⁸ Defence was considering options on how best to

105 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 20 June 2017, p. 20.

106 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 20 June 2017, p. 25.

107 Tory Shepherd 'Fears SA defence jobs may go west', *Adelaide Advertiser*, 2 September 2016 (accessed 2 February 2018).

108 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 20 June 2017, p. 19.

manage the sustainment work of the Collins fleet while embarking on the construction of the future submarine. Relevant considerations include the necessary workforce expansion and the ability to 'grow the infrastructure in Adelaide to support the build of the submarine'.¹⁰⁹

5.84 The issue was also canvassed at a recent estimates hearing on 29 May 2018. Information was sought from Defence on the Collins Class tasking statement, which raised the prospect of relocating sustainment and full-cycle docking activities to Western Australia.¹¹⁰ Mr Stephen Johnson, General Manager Submarines, explained that Defence was exploring a variety of contingency plans with respect to full-cycle dockings for the Collins Class submarines. Mr Johnson discussed types of considerations involved in the year 2034 when:

...there is a good chance that we'll have two full-size submarines in the water in the final test mode, there'll be a full-size submarine in the building ways, there'll be a submarine in modules, there'll be a submarine in the warehouse, so to speak, in terms of parts, a full-size Collins and the first full-cycle docking. So we're sceptical that we have the right footprint in that shipyard for seven submarines, for example.¹¹¹

5.85 The committee heard that there will also need to be the capacity to increase production.¹¹²

5.86 The Western Australian government argued that it made sense to transfer sustainment of the Collins fleet to Western Australia because the fleet is already based there at HMAS Stirling and the state has the capability and capacity to meet sustainment requirements.¹¹³

Committee comment

5.87 An Australian sovereign capability in naval shipbuilding is vital for the defence of the nation and the capacity of Australian industry to meet future defence needs. However, without clearly defined and mandated requirements outlining the level of Australian industry involvement and content required in defence projects, the survival of an Australian naval shipbuilding industry with sovereign capability is at risk.

5.88 The recent Industrial Capability Plan has moved in the right direction by requiring an Australian company to have more than an ABN to be considered local.

109 Senate Economics References Committee, *Committee Hansard* (Future of Australia's naval shipbuilding industry), 20 June 2017, p. 19.

110 Senate Foreign Affairs, Defence and Trade Legislation Committee, *Proof Committee Hansard* (Budget estimates), 29 May, pp. 58-59.

111 Senate Foreign Affairs, Defence and Trade Legislation Committee, *Proof Committee Hansard* (Budget estimates), 29 May, p. 58.

112 Senate Foreign Affairs, Defence and Trade Legislation Committee, *Proof Committee Hansard* (Budget estimates), 29 May, p. 58.

113 Western Australian Government, *Submission 56.2*, p. 9.

The government states that it is committed to achieving 'maximum participation' of local industry. But the phrase 'maximum participation' does not describe what is being evaluated. Does this phrase refer to Australian labour involvement in the build, the percentage of Australian products used, or both? The committee did not receive advice about what constitutes Australian involvement, or definitions of terms such as 'involvement', 'content' and 'participation'. Clear and precise definitions agreed to by industry and the government are essential in the examination of any mandated requirements. This is a necessary first step in securing Australian sovereign capability for each of the major projects set out in the government's naval shipbuilding plan.

5.89 The committee heard that mandating percentage targets for both Australian involvement and content would be more effective at guaranteeing Australian industry involvement than the government's commitment to achieving maximum participation. It was also argued by some witnesses that setting only minimum percentage targets might encourage shipbuilding companies to meet that set target but not endeavour to exceed it. In regards to mandated targets, the committee believes that further clarification is required from the government about the definitions of key terms before decisions about quantitative or qualitative metrics are mandated. In the meantime, this does not preclude projects from continuing to be subject to close examination of how Australian industry will be utilised.

5.90 The committee believes that close examination of major defence contracts between primes and the government is important to enable transparency around taxpayer funded projects. For example, in relation to the future submarine program, the treaty between the governments of France and Australia was examined by the JSCOT and a report produced.

5.91 The committee has seen a copy of the draft Naval Group AIC plan for the future submarine project, obtained through a Senate order for production. The release of this draft document enabled the committee to examine the plan, and discuss its contents with industry witnesses and the Department of Defence at public hearings. The final document was provided to the Department of Defence in April 2018. The committee notes that the Department has indicated an intention to comply with the order for the production of the document. The document is yet to be released to the committee or tabled in the Senate

5.92 Draft tenderer AIC plans submitted to the Department of Defence during the competitive evaluation processes for Defence projects should be made available for scrutiny by the Senate. This would occur after a successful tenderer has been selected, but before the AIC plan is finalised between the Department of Defence and the successful tenderer. This is preferable to using coercive measures, such as an order for production of document in the Senate, before such information is made available.

5.93 In addition, the committee believes there is value gained through prescribing a formal, periodic Senate examination of these plans against actual project progress to ensure that Australian industry commitments outlined in the plan are met. The drafting and finalisation of contracts and AIC plans should not take place behind closed doors. These processes should be transparent and subject to parliamentary and public debate considering how much taxpayer money is at stake.

Recommendation 7

5.94 The committee recommends that the government provide clear definitions about what constitutes Australian involvement, content, and participation, and how this will be achieved in each project outlined in the government's naval shipbuilding plan. These definitions and requirements for Australian industry involvement are to be stipulated in each contract.

Recommendation 8

The committee recommends that Australian Industry Capability plans for new Defence naval projects are subject to examination by the Senate – conducted in a manner similar to international treaties. The committee further recommends that finalised Australian Industry Capability plans are subject to six monthly reviews against progress by the Senate.

