

Chapter 2

Systemic issues

Introduction

2.1 As noted in the committee's interim reports, the *2016 Defence White Paper* (the White Paper) sets out the government's intent to strengthen and increase investment in defence capabilities to meet the challenges of the strategic environment. This intent is supported by an increase in defence funding, a program of upgrading infrastructure initiatives, including training facilities, over the next 10 years and a policy framework focusing on small and medium enterprises (SMEs).

2.2 As highlighted in the committee's first interim report, at the launch of the White Paper, the Prime Minister spoke about the job creation aspects:

Importantly, this White Paper will also affect the working lives and prospects of many civilian Australians – creating thousands of jobs across the regions and cities of Australia.¹

2.3 Following the release of the White Paper, a number of other ministers highlighted the potential of jobs for regional Australia and the job creation that will apply across the supply chain.²

2.4 During its inquiry, the committee sought to investigate how the intended benefits of the White Paper would be implemented, and in particular how the benefits will be realised in rural and regional areas. The committee wanted to find out about the current experiences of local communities and SMEs and what communication mechanisms are currently in place to facilitate information exchange and collaboration with the Department of Defence (Defence).

2.5 This chapter presents the evidence provided to the committee highlighting a range of systemic issues including: the policy framework to implement the White Paper, the use of Tier 1 contractors, the Commonwealth Procurement Rules, existing communication mechanisms and the information collected by Defence to measure the regional impact of its activities.

Policy settings

2.6 The implementation of the White Paper is supported by a number of policy documents and initiatives.

2.7 The *2016 Integrated Investment Program* and the *2016 Defence Industry Policy Statement* were launched in conjunction with the White Paper. The Integrated

1 The Hon Malcolm Turnbull MP, Prime Minister, 'Launch of the Defence White Paper', *Transcript*, 25 February 2016.

2 See: Senator the Hon Fiona Nash, Minister for Regional Development, 'Regional Jobs boost through Defence White Paper investment', *Media release*, March 2016, The Hon Christopher Pyne MP, Minister for Defence Industry, Speech to CEDA State of the Nation 2017, 1 June 2017.

Investment Program will guide the implementation of the bulk of investment over the decade to financial year 2025–26 to build the future force and Defence capability goals of the Defence White Paper. The Defence Industry Policy Statement will ensure opportunities are maximised for competitive Australian businesses and streamline the delivery of Defence industry programs.

2.8 The White Paper is also supported and implemented by a number of other policies including: the Defence Industrial Capability Plan and the Defence Export Strategy.

2.9 Defence has published a diagram to illustrate the 'Defence Industry Policy Agenda' as shown below.

Figure 1: Defence Industry Policy Agenda



Source: 2018 Defence Industrial Capability Plan, p. 14.

2.10 In addition to the policy framework, as discussed in the committee's interim reports, six projects have been nominated under the Local Industry Capability Plan pilot. The outcomes of this pilot will inform the development of the Defence Industry Participation Policy to be released in 2018.

2.11 The White Paper also signalled a new approach to Australian defence industry policy with a focus on SMEs. This focus was reiterated in the 2016 Defence Industry Policy Statement which emphasised the importance of SMEs and local businesses to support Defence across the country.³ The White Paper noted that a new Centre for Defence Industry Capability funded to 2025–26 at a cost of \$230 million 'will connect

3 Australian Government, Department of Defence, 2016 Defence Industry Policy Statement, p. 8.

Defence needs with the innovation and expertise of defence industry, as well as help grow a competitive, sustainable Australian defence industry base'.⁴

2.12 Evidence to the committee at each of its hearings and through submissions demonstrated that rural and regional communities welcome commitments that seek to increase employment prospects for Defence industry as well as other areas of the supply chain. A particular focus of the committee was to investigate how the anticipated benefits of the increased expenditure would deliver positive outcomes for rural and regional communities.

Focus on small and medium enterprises

2.13 In accordance with the Commonwealth Procurement Rules (CPRs), it is a government requirement for non-corporate entities to source at least 10 per cent of procurement by value from SMEs.⁵

2.14 In its submission and in evidence to the committee, Defence emphasised that it recognises the importance of SMEs:

Defence recognises that small to medium enterprises are important to the generation of business opportunities, employment and sustainment of defence capability, including for the construction, enhancement, and management of Defence facilities and training areas. Defence's in country spend is significant at a regional level. This is partly due to the Australia-wide footprint of Defence facilities and because a number of suppliers are located outside, or on the periphery, of major metropolitan areas.

Defence recognises that there are benefits of drawing support from local contractors and suppliers, where there is the capacity and capability available in the local market and they are able to demonstrate value for money.⁶

2.15 Defence has consistently reported exceeding the Commonwealth Government's 10 per cent target for participation from SMEs:

In 2015-16 Defence gazetted contracts in excess of \$30 billion, representing 53.7 per cent of the total value of all Commonwealth contracts gazetted. Of these, Defence awarded 18 per cent by value and 58 per cent by volume to small and medium enterprises (contracts and amendments as published on AusTender) and 8 per cent by value and 30 per cent by volume to small businesses. While this significantly exceeds the Commonwealth's small and medium enterprise target of 10 per cent, Defence is continuing efforts to grow small and medium business opportunities in both materiel and non-materiel procurements.⁷

4 Australian Government, Department of Defence, *2016 Defence White Paper*, p. 110.

5 Department of Finance, Commonwealth Procurement Rules, 1 January 2018, p. 14.

6 *Submission 9*, p. 32.

7 *Submission 9*, pp. 32–33.

2.16 In the 2016-17 financial year, Defence awarded 21 per cent of contracts by value and 59 per cent of contracts by volume to SMEs.⁸

2.17 Defence provided evidence outlining how the focus on SMEs will be embedded into the relevant policy documents:

The Defence Industry Participation Policy is one element of the Defence Industrial Capability Plan. The Defence Industrial Capability Plan sits, if you like, directly below the Defence Industry Policy Statement, and there are a number of initiatives within it—the sovereign industrial capabilities part, the local industry participation policy and the Defence Industry Participation Policy—all of which are dealing with specific challenges that are faced either by small to medium enterprises or by large companies. We are providing the detail of how the companies in that particular problem set—whether it's small to medium enterprises or others—can engage in contracting work or engaging with us in the investment in the capabilities of the ADF.⁹

2.18 A particular focus of the Defence Industry Participation Policy is in recognition that 'there are specific challenges for small to medium enterprises'.¹⁰ Defence explained further:

If you're a small-to-medium enterprise that hasn't typically dealt with Defence in the past but have something that is of value, it points out how you as a small to medium enterprise can engage with the existing programs like the Defence Innovation Hub, the Next Generation Technologies Fund and other elements, through the Centre for Defence Industry Capability. They work with companies that have never worked with Defence in the past, which they call 'working with Defence 101', where they say, 'These are the sorts of things you need to think about if you want to work with Defence'.¹¹

2.19 Further to this, Mr Marc Ablong, Acting Deputy Secretary, Strategic Policy and Intelligence, Defence, recognised that prime contractors have different priorities and needs to SMEs and this is reflected in the policy framework:

Beneath the Defence industry policy statement there are a number of different initiatives helping to either make you ready to work with Defence or provide you with support if you're going from one level of capability—for instance, a small-to-medium enterprise might have been doing very well working with Defence and is thinking about expanding their business to become a medium sized enterprise. We can do some things to help them.

8 Department of Defence, Answers to written questions on notice in advance of 21 March 2018 hearing (received 20 April 2018).

9 Mr Marc Ablong, Acting Deputy Secretary, Strategic Policy and Intelligence, Department of Defence, *Proof Committee Hansard*, 21 March 2018, p. 15.

10 Mr Marc Ablong, *Proof Committee Hansard*, 21 March 2018, p. 15.

11 Mr Marc Ablong, *Proof Committee Hansard*, 21 March 2018, p. 15.

For the large end of town, the prime contractors, it's about working to identify areas in which they can support the rest of the industry.¹²

2.20 The committee sought information from Defence about how the White Paper and the associated policies are being embedded at all levels across the Department.

2.21 Defence advised that there are a 'range of communication channels to inform staff of updates to Defence policies'¹³ and these are considered as part of policy implementation. In particular, Defence provided information about how policies are communicated across the Department:

Effective implementation of the above initiatives ensures that there are structures and procedures in place across Defence to recognise the importance of Australia's defence industry, including competitive SMEs, to delivering and supporting Defence capability. Notably, as part of the implementation of industry as a Fundamental Input to Capability, the Smart Buyer, Capability Life Cycle and Force Design Cycle have already integrated earlier and more regular consideration of industry into Defence's processes.

The DIPS [Defence Industry Participation Policy] and major policy initiatives, such as the Defence Export Strategy, Defence manuals and procedures, such as the Defence Procurement Policy Manual, are distributed to all Defence staff to ensure awareness. Senior Defence personnel are also regularly briefed on industry policy issues and priorities. This ensures ongoing awareness throughout Defence of the Government's industry policy agenda, including key components such as a focus on SMEs.¹⁴

2.22 In addition to the increased focus on SMEs as specified in the policy documents, Defence is also implementing other initiatives to support SMEs as outlined below.

Local Industry Capability Plan pilot

2.23 One example of the increased focus on SMEs is the Local Industry Capability Plan (LICP) pilot, announced by the Minister for Defence in August 2017 to facilitate more opportunities for local industry to participate in major Defence infrastructure projects.¹⁵

2.24 Initially to include three projects, the LICP pilot has been expanded to six projects: Explosive Ordnance Logistics Reform Program, Shoalwater Bay Training Area Redevelopment, Townsville Field Training Area Mid Term Refresh, RAAF Base

12 *Proof Committee Hansard*, 21 March 2018, p. 15.

13 Department of Defence, Answers to written questions on notice in advance of 21 March 2018 hearing (received 20 April 2018).

14 Department of Defence, Answers to written questions on notice in advance of 21 March 2018 hearing (received 20 April 2018).

15 Senator the Hon Marise Payne, Minister for Defence, 'Strengthening opportunities for local industry', *Media release*, 31 August 2017.

Townsville Mid Term Refresh and HMAS Cairns Mid Term Refresh (grouped as a program of projects), and the HMAS Cerberus Redevelopment.¹⁶

2.25 When announcing the LICP pilot, the Minister for Defence stated:

The pilot projects will require tenderers bidding for major capital facilities projects to state clearly how they have engaged with local industry in providing their tendered solution, and how local industry will specifically be involved in delivering the work packages that underpin the project.¹⁷

2.26 Defence advised that 'guidance to prospective tenderers on local industry participation requirements is provided at multiple points throughout the procurement process'.¹⁸ When responding to a Request for Tender, each tenderer is required to prepare, complete and lodge a draft LICP in Tender Schedule J, based on the following:

- expected economic impact of the works;
- proposed local industry participation in the delivery of the works;
- project contestability; and
- the tenderer's proposed approach for implementing and reporting on the LICP.¹⁹

2.27 The successful tenderer will be required to prepare and submit a LICP to the contract administrator after the award date of the contract. The LICP must be based on the draft LICP provided during the tender process and detail the contractor's approach to the market and intended Australian engagement locally, regionally and nationally for the project.

2.28 The LICP is a project plan that forms part of the contract. Defence will require the contractor to provide a monthly update on the achievement of its LICP.²⁰

2.29 Defence also advised that the LICP will be used by the Commonwealth to:

- determine the extent of the economic benefit to the Australian economy;
- validate engagement and commitment to opportunities for local industry participation in the procurement or the supply chain; and
- identify further opportunities to support and develop Australian industry.²¹

16 Brigadier Matthew Galton, Director-General, Capital Facilities and Infrastructure branch, Defence, *Proof Committee Hansard*, 21 March 2018, p. 16.

17 Senator the Hon Marise Payne, Minister for Defence, *Media release*, 'Strengthening opportunities for local industry', 31 August 2017.

18 Department of Defence, Answers to written questions on notice in advance of 21 March 2018 hearing (received 18 April 2018).

19 Department of Defence, Answers to written questions on notice in advance of 21 March 2018 hearing (received 18 April 2018).

20 Department of Defence, Answers to written questions on notice in advance of 21 March 2018 hearing (received 18 April 2018).

Assessment of the LICP as part of the tender consideration process

2.30 On notice, Defence provided details about the tender evaluation process noting that while a specific weighting is not applied to the LICP, the LICP:

[I]s examined as part of the value for money assessment conducted by the tender board. The Tender is evaluated with reference to whether value for money has been demonstrated by its commitment to local industry participation and will implement appropriate solutions and management strategies to ensure that local industry is given full, fair and reasonable opportunity to participate in the delivery of the Works if it is the successful Tenderer.²²

2.31 The information assessed as part of the tender process includes:

- expected economic impact of the works, (including estimates of employment numbers and description of any initiatives related to Indigenous procurement);
- proposed local industry participation in the delivery of the works, (including description of mechanisms that will be used to ensure local industry will have the opportunity to participate, and how local SMEs will be encouraged to participate in the procurement activities);
- proposed approach to a local supply chain, (including processes for updating preferred supplier lists, assessing potential local businesses and mechanisms to ensure that reasonable opportunity to participate is passed onto subcontractors. If feedback is to be offered to unsuccessful subcontract tenderers, information about the processes which will be undertaken must also be provided);
- standards, (including a description of the standards to be used for the project); and
- project contestability, (including an estimation in Australian dollars of the overall industry participation outcomes by local businesses to site, regional within state or territory and other state or territory as well as a list of goods or services which will be either sourced overseas or locally with imported content).²³

2.32 In relation to defining 'local', Defence advised:

Defence is taking a pragmatic approach to defining 'local', rather than developing a rigid, geographical definition of what local means. Using a rigid definition could result in certain suppliers being arbitrarily excluded.

21 Department of Defence, Answers to written questions on notice in advance of 21 March 2018 hearing (received 18 April 2018).

22 Department of Defence, Answers to written questions on notice in advance of 21 March 2018 hearing (received 18 April 2018).

23 Department of Defence, Answers to written questions on notice in advance of 21 March 2018 hearing (received 18 April 2018).

Additionally, there is no common State and Territory Government model for defining 'local' industry in a geographical construct.²⁴

Local industry engagement

2.33 During Additional Estimates, Mr Steve Grzeskowiak, Deputy Secretary Estate and Infrastructure, explained how Defence is working with possible managing contractors for the projects in the LICP pilot to encourage them to engage with local industry:

What we're doing is, as we go to market looking for tenders for companies to be our primes, whether they be managing contractors or head contractors, we're asking that they engage with the local industry and, as part of their response to us in their tender, we're asking them to explain to us how they will maximise opportunity for local industry to be involved in the process. That doesn't mean that some of those local industry small-to-medium enterprises would definitely get the work, but how will the project be structured to enable them to have the best chance of bidding for the work?²⁵

2.34 At the committee's Canberra public hearing in March 2018, Mr Grzeskowiak advised that Defence expects companies involved in the LICP pilot, 'as part of their discovery process, to understand the local industry and structure the work that they're planning to give those local industries an opportunity to be part of that work'.²⁶

2.35 The LICP pilot actively encourages companies to engage with local industry, however, Mr Grzeskowiak emphasised that Defence is required to assess all bids following the Commonwealth Procurement Rules:

Obviously we do have to follow Commonwealth procurement rules and they require us to look for best value for money. We can't formally give a weighting to a local company over a non-local company, but obviously local companies should be in a good position to bid at competitive prices for work because of the nature of their locale. What this might mean is, for example, as a project is designed, understanding the capacity of local companies and making sure that the design doesn't rule out a local company. A good example is you might be building an aircraft hangar. If you know that locally the largest steel beams that can be galvanised are 20m then you try not to design a hangar that needs 21m long steel beams; you try to keep the design within the capacity of the local industry, so they can at least bid for doing the work. So that's what we're trying to do as well.²⁷

2.36 When discussing the pilot, Mr Grzeskowiak noted the current high percentage of local industry subcontractors:

24 Department of Defence, Answers to written questions on notice in advance of 21 March 2018 hearing (received 18 April 2018).

25 *Proof Estimates Hansard*, 28 February 2018, p. 95.

26 *Proof Committee Hansard*, 21 March 2018, p. 3.

27 *Proof Estimates Hansard*, 28 February 2018, p. 95.

We're not starting from nowhere in this. If you look across the projects in the space we've got at the moment, actually in work, there's about 54 of them. Across that suite of projects, which are all over the country, we're at about 60 per cent of the works subcontracts are placed in local industry. We're a reasonable percentage at the moment but we are trying to increase that.²⁸

2.37 The outcomes from the pilot will inform the development of other Defence policy:

We're running a pilot so we can learn. The idea of the pilot is that the learnings from it will inform the broader Defence policy about local industry capabilities, and we've said that that broader Defence policy is due for release in the first half of this year. So that policy is in the process of being worked up at the moment. We are feeding in, and will continue to feed in, experiences from pilots that we're running at the moment, and what we're learning from these committees.²⁹

Stakeholder views on the pilot program

2.38 The LICP pilot was announced in August 2017, during the period that the committee conducted its inquiry. In February 2018, the committee wrote to witnesses who provided evidence at the Northern Territory and Queensland public hearings seeking feedback on the LICP pilot. The committee received a small number of responses where it was noted that the pilot is positive but it was acknowledged that the initiative is in its infancy with a number of tenders not finalised at the time of writing to the committee.³⁰

Restructuring work packages

2.39 In addition to the focus on local industry engagement of the LICP pilot, Defence is also looking to restructure work packages for Defence contracts. As noted in the committee's third interim report, this initiative was announced by the Minister for Defence:

At present, the typical arrangements are for sub-contracts to be based on 'trade packages'. Defence has considered feedback from Northern Territory enterprises and will instead trial the use of smaller 'work packages' for the upcoming Larrakeyah Redevelopment and Naval Operations in the North projects," Minister Payne said.

Under this approach, buildings or work elements may be tendered separately, rather than by individual trade. It is expected that this initiative will provide greater opportunity to local industry in the Northern Territory.³¹

28 *Proof Estimates Hansard*, 28 February 2018, p. 95.

29 *Proof Committee Hansard*, 21 March 2018, p. 3.

30 Livingstone Shire Council, *Submission 5.1*, p. 3; Capricorn Enterprises, *Submission 40*, p. 1.

31 Senator the Hon Marise Payne, Minister for Defence, 'Strengthening opportunities for local industry', *Media release*, 31 August 2017.

2.40 At Additional Estimates, Mr Grzeskowiak provided further detail about the restructuring of work packages:

We're looking to structure work packages differently. Historically, as we've gone to market through our primes, they would structure a work package to be what is called a trade package, so all of the ground works for a project, all of the electrical works for a project, all of the concrete form work, all of the steelwork. That can tend to make it difficult for smaller local companies to be able to bid. So instead, what we're asking our primes to do is contract for what are called works packages, so if we're doing a lot of work across a base, it might be this small precinct company X gets the subcontract to build that whole precinct rather than doing, for example, the electrical work across the whole base. And small and medium industry have told us that will enable them to better be able to take part.³²

2018 Defence Industrial Capability Plan

2.41 The committee welcomes the release of the *2018 Defence Industrial Capability Plan* on 23 April 2018 and notes that the Plan includes a list of ten initial Sovereign Industrial Capability Priorities. These priorities are focused on areas that are operationally critical, priorities within the Integrated Investment Program over the next three to five years or need more dedicated monitoring, management and support.

2.42 The establishment of Sovereign Industrial Capability Priority Grants will enable SMEs who are contributing to a Sovereign Industrial Capability Priority to apply for grants of up to \$1 million to fund capital equipment purchases and non-recurring engineering costs. Businesses will be required to match funding on a 50:50 basis and total funding for a business over a two to three year period will be capped at \$3 million. Total funding for these grants will be up to \$17 million in a financial year.³³

2.43 The committee notes that Defence provides some reassurance to SMEs who do not contribute to a Sovereign Industrial Capability Priority. It is recognised that there will be opportunities to support the delivery of defence capability across the broader Defence requirements. It is also noted that the priorities will be updated in future reviews of the Defence Industrial Capability Plan.

2.44 It is positive that the Defence Industrial Capability Plan includes a focus on reviewing and updating the Plan. It is recognised that changes will need to be made to align with the defence strategy cycle and capability goals, and defence industry priorities.

2.45 It appears that the Centre for Defence Industry Capability (CDIC) will provide a valuable link to industry and specifically SMEs to ensure that information about progress and reviews to the Plan are published and made available.

32 *Proof Estimates Hansard*, 28 February 2018, p. 95.

33 Australian Government, Department of Defence, *2018 Defence Industrial Capability Plan*, 23 April 2018, p. 153.

Centre for Defence Industry Capability

2.46 Another example of the increased focus on SMEs is the establishment of the CDIC, an initiative foreshadowed in the *Defence Industry Policy Statement*. Based in Adelaide, the CDIC is forming a national advisory network with advisers across all states and territories.³⁴

2.47 The CDIC supports Australian businesses working in the defence industry or those seeking to get involved. The CDIC Advisory Board brings together Australian defence industry leaders and senior public sector representatives to provide guidance and strategic direction for the CDIC.

2.48 The CDIC provides a national network of business advisers with regional expertise to help businesses understand the defence market and to develop their industrial capabilities and ability to work with Defence. The CDIC also assists Defence to better understand the capability of Australian industry.³⁵ The website notes:

Our advisers help businesses navigate the defence market, provide specialist advice on improving competitiveness and accessing global markets, and facilitate connections with other businesses and Defence. We also link Australian innovators, researchers and academic institutions to Defence's two innovation programs - the Defence Innovation Hub and the Next Generation Technologies Fund.

With \$200 billion being invested by Government to modernise defence capability, our task is to work with industry, Defence, and state and territory governments to build a world-class, globally competitive and sustainable Australian defence industry.³⁶

2.49 The committee notes that the CDIC website provides a large range of information for businesses interested in seeking business opportunities with Defence, including a Defence Industry and Innovation information newsletter, and seminars to inform businesses about how to work with Defence.

Defence market seminars hosted by the CDIC

2.50 The committee notes that the CDIC hosted a series of 'Introduction to the Defence Market' seminars in state capitals and regional areas between March — May

34 Australian Government, *About the CDIC*, (updated 9 February 2018), <https://www.business.gov.au/Centre-for-Defence-Industry-Capability/About-the-CDIC> (accessed on 6 March 2018).

35 Australian Government, *Business advice and grants*, (updated 9 February 2018), <https://www.business.gov.au/centre-for-defence-industry-capability/business-advice-and-grants> (accessed on 6 March 2018).

36 Australian Government, *Centre for Defence Industry Capability (CDIC)*, (updated 21 February 2018), <https://www.business.gov.au/centre-for-defence-industry-capability> (accessed on 6 March 2018).

2018. The committee is aware that the seminars were advertised on a variety of defence news websites as well as on other organisations' such as RDAs.³⁷

2.51 Following a preliminary discussion at the Canberra public hearing about the seminars, Defence provided additional information on notice:

The Seminars have attracted a diverse range of small and medium enterprises (SMEs) and the support of local business chambers and incubators that look to support their local businesses in new ventures. In support of the seminars, State and Territory governments and defence industry associations have also been invited to attend and present on local initiatives and the support they have available.³⁸

2.52 As at 28 March 2018, the CDIC has delivered seminars in seven locations nationally: five in Queensland (Brisbane, Sunshine Coast, Townsville, Rockhampton and Cairns), one in Canberra and one in Albury/Wodonga. Ten further seminars were planned for April and May at locations in New South Wales, Victoria, Tasmania, Western Australia, Northern Territory and South Australia.³⁹

2.53 Defence advised that the content of each seminar is tailored for the needs of businesses in each location and where possible and appropriate, each seminar incorporates SME case studies and prime contractor engagement whereby one of the seven prime contractors involved in the Global Supply Chain program is invited to speak about their experiences and the Australian defence market.⁴⁰

2.54 At the Canberra hearing, Defence provided information about some of the CDIC's other initiatives:

...as of February of this year the Centre for Defence Industry Capability has received over 320 applications from Australian companies, of which 302 have been accepted and are being pushed through the various processes. We have received 26 applications for Capability Improvement Grants, of which 23 have been approved, with a total value of \$942,337 in grants so far. There are a number of things inside what the Centre for Defence Industry Capability is doing that are starting to impact upon industry's ability to

37 See for example, Defence Connect, *CDIC Introduction to the Defence Market Seminars*, <https://www.defenceconnect.com.au/events/item/cdic-introduction-to-the-defence-market-seminars-2> (accessed on 19 February 2018) and Regional Development Australia, Far North Queensland, and Torres Strait Inc, *Introduction to the Defence Market*, 13 February 2018, <https://rdafngts.org.au/2018/02/13/introduction-to-the-defence-market/> (accessed on 19 February 2018).

38 Department of Defence, Answers to questions taken on notice, 21 March 2018 (received 18 April 2018).

39 Department of Defence, Answers to questions taken on notice, 21 March 2018 (received 18 April 2018).

40 Department of Defence, Answers to questions taken on notice, 21 March 2018, (received 18 April 2018).

engage with Defence, but I'll get you a more detailed brief and provide that to the committee.⁴¹

Tier 1 contractors

2.55 Another systemic issue examined by the committee is the use of Tier 1 or prime contractors. Typically, Defence will engage a contractor for its major capital facilities and infrastructure projects through either a head or managing contractor contract. Under this contract, the head or managing contractor is 'responsible for seeking, evaluating and engaging its subcontractors and suppliers'.⁴² In addition:

Under the Managing Contract, the contractor is required to tender all construction work as subcontract packages (i.e. it cannot perform the construction work itself). Subcontract works are packaged by contractor, based on their experience and research into the capacity and capability of the sub-contract market. The contractor is required to ensure that all subcontract tender documentation is prepared and all tender processes are conducted consistently with the principles of the CPRs, including the rules in relation to value for money, encouraging competition, efficient, effective economical and ethical procurement, accountability and transparency.⁴³

2.56 As explained by Ms Alice Jones, First Assistant Secretary, Service Delivery, Defence, at the Wodonga hearing, with respect to services delivered at Defence bases, [i]t is the prime's [Tier 1] responsibility to deliver the service and sub out the work as they see fit or desire'.⁴⁴

Ensuring policy intent through Tier 1s

2.57 In order for the intent of government policies such as the White Paper and associated documents to be implemented, and for Defence to have confidence that their contracts are being implemented in accordance with their intended aims, it is important that clear reporting and feedback processes be established. In effect, the head or managing contractor model means that the contracts are being delivered on Defence's behalf. The committee emphasises the importance of a robust reporting framework to ensure that contracts are being implemented in accordance with the terms of contract.

Tier 1 engagement with SMEs

2.58 The committee received evidence about prime contractors who are actively engaged with local businesses. For example, evidence in Port Augusta of prime contractors holding information forums for local businesses to discuss the potential opportunities for subcontracting packages.⁴⁵ In Rockhampton, witnesses provided

41 Mr Marc Ablong, *Proof Committee Hansard*, 21 March 2018, p. 16.

42 *Submission 9*, p. 28.

43 *Submission 9*, pp. 28–29.

44 *Committee Hansard*, 21 November 2017, p. 37.

45 Brigadier Noel Beutel, Director-General, Capital Facilities and Infrastructure, Department of Defence, *Committee Hansard*, 8 June 2017, p. 26.

examples of industry associations and others who are providing assistance to SMEs by either offering training to increase their capability to compete for Defence contracts or providing information about upcoming business opportunities.⁴⁶

2.59 The committee notes the examples of engagement with primes provided to the inquiry, as well as the stated aims of initiatives like the LICP pilot to increase engagement. The committee inquired with Defence about whether there are standard provisions in Defence contracts about engagement with local industry. However, at the time of finalising this report Defence had not provided a response to those questions. The committee recognises the value of the provision of such information by contractors to Defence and also making it available more broadly. The availability of regional information about Defence activity is discussed later in the chapter.

2.60 The committee also received evidence about state government and industry network initiatives that are seeking to 'upskill' SMEs to place them in a better position to tender for Defence contracts.⁴⁷ As noted by Mr Jason Schoolmeester, Executive Director, Defence NT:

...in terms of industry briefings and links to awarded contracts, it is very hard to demonstrate a causal link between attending a briefing and actually getting a contract. But certainly we always say that the more information industry and SMEs have the better prepared they can be to identify the opportunities and compete for the work. I guess the priority here is creating opportunities so that local companies can compete for the work.⁴⁸

2.61 The committee notes there are some synergies between the examples provided in evidence to the inquiry and the work of the CDIC. It is important that ongoing opportunities for collaboration and engagement between Defence, prime contractors and local SMEs are enhanced and maintained.

Tier 1 reporting

2.62 In accordance with their terms of contract, Tier 1 contractors are required to report to Defence on a number of matters. The committee explored the reporting requirements of Tier 1 contractors. Brigadier Noel Beutel indicated that within the projects in capital facilities:

Contractually they are required to provide me with statistics of subcontracts—so total number of trade packages, trade packages let to date, the value of those trade packages, how many have gone to local industry or those subcontractors, and then a percentage value for that.⁴⁹

46 See for example, Capricorn Enterprises, *Committee Hansard*, 12 July 2017, pp. 27–28.

47 See for example, Capricorn Enterprises, *Submission 40*, p. 2; Mr Jason Schoolmeester, Executive Director, Defence NT, *Committee Hansard*, 22 August 2017, p. 11.

48 Mr Jason Schoolmeester, Executive Director, Defence NT, *Committee Hansard*, 22 August 2017, p. 12.

49 Brigadier Noel Beutel, *Committee Hansard*, 22 August 2017, p. 47.

2.63 On notice Defence undertook to provide advice on the level of reporting by contractors across Defence which appears to vary. For capital facilities and infrastructure projects 'Defence's contracts with managing contractors...include the requirement to report on local industry engagement'. Defence highlighted the requirements of the LICP pilot where tenderers will be required to state how they have engaged with local industry. The Australian Industry Capability Program applies to materiel projects of \$20 million and above where 'tenderers are required to provide Australian Industry Capability plans that must address how Australian industry has been engaged in forming the tenderer's proposed capability solution'.⁵⁰

2.64 Tier 1 contractors providing services on Defence bases under Base Services Contracts are also required to report to Defence as part of their contracts. In a response to a question on notice received in February 2018, Defence advised that consideration is being given to amending Base Services Contracts to allow for additional requirements:

Service Delivery Division is looking at ways to capture information from these contractors to identify the local engagement of SMEs, including local contractors and their expenditure. Consideration is being given to amending the Base Services Contracts to include the additional reporting requirements to allow for this level of detail to be captured.⁵¹

2.65 The committee is aware that a 2016 ANAO Report *Design and Implementation of Defence's Base Services Contracts*, includes advice from Defence that 'in response to the internal Defence audit, the Service Delivery Division had initiated a review of its process for performance assessment, reporting and assurance'.⁵² The committee inquired but at the time of finalising the report had not received information from Defence about the progress of the review and how the reporting requirements in Base Services Contracts may change as a result of the review.

2.66 The committee recognises that the information reported by Tier 1 contractors to Defence is valuable and has the potential to assist a range of stakeholders develop a better understanding of the level of engagement with local industry as well as the broader regional impact of Defence activities. The need for an improved system of collecting and reporting on regional information is considered later in this chapter.

Challenges experienced by SMEs with respect to Tier 1 contractors

2.67 As outlined in each of the committee's interim reports, evidence to the inquiry highlighted challenges experienced by SMEs with respect to Tier 1 prime contractors. In preparing for its final hearing, the committee received a submission from Regional

50 Department of Defence, Answer to question on notice, 22 August 2017 (received 27 February 2018).

51 Department of Defence, Answer to question on notice, 22 August 2017 (received 27 February 2018).

52 Australian National Audit Office, *ANAO Report No.29 2016-17, Design and Implementation of Defence's Base Services Contracts*, December 2016, p. 49.

Development Australia Whyalla and Eyre Peninsula (RDAWEP) which provided details about the experiences of businesses operating in the region seeking to secure work on the Cultana Training Area Redevelopment (CTAR) Stage 1 Project. In particular, RDAWEP submitted:

As the initial stages of the project nears completion there is little evidence that local supply chain companies and contractors have been utilised to work on the project. There have been some use of local accommodation, service providers, retailers and local labour, but this has been limited and appears to be a relatively small proportion of the total project budget.⁵³

2.68 RDAWEP explained that 'several medium sized businesses with local facilities and operations in the region bid for work on substantial components of the project (up to \$6 million value)⁵⁴ but were ultimately unsuccessful in being awarded contracts. Further evidence was submitted outlining the experiences of local suppliers, which, in the view of RDAWEP, 'indicate questionable trade practices:

It was reported by 1 local Tier 2 SME that they invested up to \$40,000 in preparing quotes and tender documents for work at Cultana. The company was informed that their quote was used by the EPC to bid for the project. When the EPC bidder was successful, the local company was subsequently advised that they must reduce their final quote by more than 10% in order to secure a contract for the work. Although the local company reduced its price, it was unable to fully meet this demand. The EPC then engaged an interstate contractor for the work who operated on a fly in fly out basis. It is beyond belief that a company incurring substantial travel and accommodation costs for its staff could undertake the same work at a lower cost than a local company with no travel or accommodation costs. This was not an isolated incident as several local businesses reported similar experiences.⁵⁵

2.69 The committee discussed these matters with Defence at the Canberra public hearing who expressed concern about the matters raised. Defence acknowledged that St Hilliers engagement on the CTAR Stage 1 Project was prior to the LICP pilot commencing and undertook to look into the matter raised in the submission.⁵⁶

2.70 Following the hearing, Defence provided the following evidence about St Hilliers engagement with the local community:

Although St Hilliers was engaged prior to the LICP, it has made a concerted effort to engage with the local community, and to provide opportunities to local subcontractors where possible. In July 2017, St Hilliers conducted local industry forums, hosted by the Chamber of Commerce and Industry in Whyalla and Port Augusta, South Australia. The purpose of the forums was to introduce the CTAR Stage 1 Project to the local community and to

53 *Submission 39*, p. 2.

54 *Submission 39*, p. 3.

55 *Submission 39*, p. 3.

56 *Proof Committee Hansard*, 21 March 2018, pp. 26.

engage with local contractors and suppliers in order to maximise opportunities for local industry participation. In March 2018, a further industry forum was conducted with local contractors and suppliers from Whyalla and Port Augusta to advise them of the finishing trades work packages that were going to be released. Attendance for local contractors and suppliers at these forums was high.

In addition to the industry forums, St Hilliers has undertaken the following activities to ensure maximum local participation:

- advertising for subcontractors/suppliers in local newspapers,
- continuing to liaise with local industry networks and the Chamber of Commerce,
- Sourcing materials from local suppliers,
- entering into supply arrangements with local supplier such as hospitality and fuel services providers; and
- managing a project “positions vacant” data base for all project sub-contractors, to facilitate employment opportunities for local residents.⁵⁷

2.71 On the particular experience of specific businesses, the committee, following consultation with RDAWEP, provided Defence with the names of two businesses which had experiences that were consistent with the evidence provided in the RDAWEP submission. At the time of finalising this report Defence was yet to respond.

Feedback to unsuccessful tenderers

2.72 The committee received some evidence about businesses which have been unsuccessful when submitting a quote for subcontracting work to prime contractors and have not received feedback to explain why there were unsuccessful.⁵⁸ Defence advised there are different contractual requirements in relation to the provision of feedback to unsuccessful tenderers. There are some contracts which do not require contractors to communicate with unsuccessful tenderers; it is up to the discretion of the contractor to provide this feedback.⁵⁹

2.73 Further to this, Defence advised that a special condition of contract will be introduced immediately into Defence's traditional head contract to ensure that prime contractors follow guidance in the Commonwealth Procurement Rules on unsuccessful tender debriefs.⁶⁰

57 Department of Defence, Answers to questions taken on notice, 21 March 2018 (received 18 April 2018).

58 Regional Development Australia, Whyalla and Eyre Peninsula, *Submission 39*, p. 3.

59 Department of Defence, Answer to questions taken on notice, 21 March 2018 (received 24 April 2018).

60 Department of Defence, Answer to questions taken on notice, 21 March 2018 (received 24 April 2018).

Commonwealth Procurement Rules

2.74 The Commonwealth Procurement Rules (CPRs) are issued by the Minister for Finance and are the rules for all Commonwealth procurements and govern the way in which entities undertake their own processes. Officials from non-corporate Commonwealth entities such as Defence must comply with the CPRs when performing duties related to procurement.⁶¹

2.75 At the public hearing in Canberra, officials from the Department of Finance (Finance) explained that their department is responsible for the CPRs as the broad high-level procurement framework.⁶²

2.76 Defence explained that their procurement activities are:

...fundamentally driven by value for money considerations. Defence, in line with Government policy, has adopted the use of national large scale contracts and standing offers to achieve the best value for money.⁶³

Consideration of economic benefit

2.77 Finance explained that a clause requiring agencies to consider economic benefits for contracts for specified amounts has been included in the CPRs since 1 March 2017:

The Commonwealth Procurement Rules, as of 1 March last year, include a clause requiring agencies to incorporate a consideration of economic benefits for contracts that are going to be over the value of \$4 million for general procurement, or \$7.5 million for construction procurement...They [the CPRs] establish a framework of principles and we do operate in a devolved framework, so it's really up to individual agencies to determine what constitutes economic benefit and what sort of weighting to give that. The procurement rules do make it clear that that is within the context of considering value for money, so it doesn't override value for money by any means. That's still the core rule.⁶⁴

2.78 Finance explained the setting of these thresholds in a response following the Canberra hearing:

The Commonwealth Procurement Rules (CPRs) sets thresholds for when an open approach to market is generally required consistent with our international obligations. For non-construction goods and services procurements, the threshold is \$80,000 and for construction services the threshold is \$7.5 million. The process for this open approach to market is set out in Division 2 of the CPRs. For construction services the threshold

61 Australian Government, Department of Finance, *Commonwealth Procurement Rules*, 1 January 2018, p. 6.

62 Mr Nicholas Hunt, First Assistant Secretary, Commercial and Government Services, Department of Finance, *Proof Committee Hansard*, 21 March 2018, p. 14.

63 *Submission 9*, p. 33.

64 Mr Nicholas Hunt, *Proof Committee Hansard*, 21 March 2018, p. 12.

requirement for an open approach to market and the requirement for an economic benefit assessment are aligned.

In the case of non-construction goods and services, the \$4 million threshold for an economic benefit test is set above the threshold for an open approach to market because this represents the point at which economic benefits should be able to be assessed, without imposing additional requirements and costs on potential suppliers and agencies, which would be the case for lower value procurements.⁶⁵

2.79 The economic benefit test in the CPRs for contracts over \$4 million is based on the economic impact to the Australian economy and not a particular region.

2.80 In its submission, Defence noted:

Defence is committed to ensuring equitable access to government contracts for Australian businesses, in particular small business as evidenced by the volume and value of contracts awarded in 2015-16. The CPRs reaffirm the Government's requirement for non – corporate entities (of which Defence is one) sourcing at least 10 per cent of procurement by value from small and medium enterprises. Defence has consistently exceeded this target.⁶⁶

South Australian model

2.81 As noted in the committee's first interim report, the South Australian Industry Participation Policy, which has been designed to deliver regional and economic benefits, establishes '...a framework for assessment of economic contribution between rival tenders and grants within a broad value-for-money framework'.⁶⁷

2.82 At the public hearing in Port Augusta, Mr Ian Nightingale emphasised that the South Australian policy 'is not about special treatment or price preferencing but, rather, about recognising the important contribution businesses make to the South Australian economy'.⁶⁸ The model can measure state economic benefit verses regional economic benefit.⁶⁹

2.83 The model used in South Australia has a weighting or a percentage at tender which measures the economic benefit using capital, supply inputs and labour. Currently the weighting is mandated at 15 per cent minimum for all government procurement above \$220,000. In larger projects above \$4 million it can be around 20 per cent. In explaining further how it works Mr Nightingale stated:

Let us take 20 per cent. If 80 per cent are the other components of your tender evaluation, that is still going to dominate the outcome of your tender,

65 Department of Finance, Answer to question taken on notice, 21 March 2018 (received 18 April 2018).

66 *Submission 9*, p. 33.

67 Mr Nightingale, *Proof Committee Hansard*, 8 June 2017, p. 8.

68 *Proof Committee Hansard*, 8 June 2017, p. 8.

69 *Proof Committee Hansard*, 8 June 2017, p. 13.

so you will still get a very competitive tender, but you are measuring a legitimate economic benefit as part of the tender evaluation.⁷⁰

2.84 The committee discussed the SA model further with Defence at the final public hearing in Canberra, noting the 1 March 2017 changes to the CPRs to consider economic benefits. Mr Ablong noted:

It's fair to say that as the changes to the Commonwealth Procurement Rules are relatively recent, we have not yet come to mature methodology for identifying economic benefits. That's one of the things that we are looking at in terms of the pilots: how you amass an economic benefit statement about a local region, how you conduct that economic benefit, and how far into the sort of social licence issues you can take an economic benefit analysis. We're still working those things through to be able to come to a more mature assessment of what the actual value-for-money proposition is. There is a lot of work currently being undertaken to build the economic models that we will use to be able to test those activities out. So, it is certainly something that is being worked through in detail as we start to build the policy.⁷¹

2.85 Defence noted that 'the model the South Australians use is one of the inputs that we're bringing into it'.⁷²

Complexity of procurement process and associated documentation

2.86 During the committee's inquiry, SMEs noted the complexity of the procurement system and in particular the detailed documentation required by Defence when tendering for contracts.⁷³ Finance indicated that specific requirements for documentation for individual tender processes are at the determination of the relevant agency:

We [Finance] are responsible for this broad high-level framework. As I said, there's nothing in the broad high-level framework that requires a particular size or volume of documentation, and often that comes back to the decisions that agencies have made about how to approach a particular procurement. Obviously, larger, more significant procurements have a higher level of documentation.⁷⁴

70 *Proof Committee Hansard*, 8 June 2017, p. 10.

71 *Proof Committee Hansard*, 21 March 2018, pp. 3–4.

72 Mr Marc Ablong, *Proof Committee Hansard*, 21 March 2018, p. 4.

73 See for example: Mr Sam Johnson, Chair, Upper Spencer Gulf, *Proof Committee Hansard*, 8 June 2017, p. 2; Ms Patrice Brown, Company Director, CQC Consulting, *Proof Committee Hansard*, 14 July 2017, p. 17; Foreign Affairs, Defence and Trade References Committee, *Impact of Defence training activities and facilities on rural and regional communities, Third interim report*, October 2017, pp. 20–29.

74 Mr Nicholas Hunt, *Proof Committee Hansard*, 21 March 2018, p. 14.

2.87 Defence advised that following the First Principles Review, a 'slimmed down' version of the Defence procurement manual has been issued.⁷⁵

2.88 The committee pursued this issue at the Canberra public hearing. Mr Grzeskowiak explained that the volume of documentation required for individual contracts will vary depending on the size and complexity of the contract. Large contracts require a range of information including insurance and finance guarantees confirming the viability of the company. Mr Grzeskowiak observed that 'we do understand that parts of industry look at those contracts and find them a bit overwhelming'.⁷⁶

2.89 Further to this, Mr Grzeskowiak provided some additional detail about how contract documentation may differ depending on its complexity:

We've been using—particularly in the capital construction sense—a suite of contracts that has gradually evolved over the last 20 years or so. They're considered robust. We've developed leaner contracts for what we call our medium sized projects, smaller projects, because we do recognise that, clearly, the nature of the contract you enter into, the detail that needs to be provided, and the risk balance between risks we might take and risks the contractor might take need to be scalable to a point. We are always looking at our contract vehicles, looking for improvements we can make for a range of things, one of which would be feedback from industry on how they find our contracts. But—particularly in our bigger contracts—the reason we have the clauses we do comes from experience in dealing over a long period of time in the market sector that we deal in. From a Defence perspective, the contracts have proved robust in terms of us being able to deliver what we need to deliver reliably without seeing too many difficulties down the track. That's not to say there are never difficulties.⁷⁷

2.90 Mr Grzeskowiak noted that Defence does receive feedback about its contracts:

We do hear and understand that new players, particularly, in this space view our contracts as very thorough, and we're attentive to incremental change of those contracts as we go on.⁷⁸

2.91 Following the hearing, Defence advised that they have 'made good progress streamlining and simplifying procurement processes' and regularly engage with 'industry, including SMEs and subcontractors through a range of fora on a range of procurement and contracting issues'.⁷⁹ Defence noted there are a range of initiatives targeting SME engagement.

75 Mr Steve Grzeskowiak, *Committee Hansard*, 8 June 2017, p. 29.

76 *Proof Committee Hansard*, 21 March 2018, p. 14.

77 *Proof Committee Hansard*, 21 March 2018, p. 14.

78 *Proof Committee Hansard*, 21 March 2018, p. 14.

79 Department of Defence, Answer to written question on notice in advance of 21 March 2018 hearing (received 20 April 2018).

Commonwealth contracting suite

2.92 The committee was advised that Defence, in line with requirements from Finance, uses the Commonwealth contracting suite for tenders under \$1 million:

So what we consider low-value, low-risk in a Defence perspective. That's a very streamlined set of tools and templates that we use. As far as I'm aware—and Finance can probably provide more advice—it was developed in consultation with SMEs.⁸⁰

2.93 Mr Hunt provided some additional information about the Commonwealth contracting suite:

[T]he Commonwealth contracting suite, which is something that Finance developed and we did do it in consultation with business. It's designed to minimise the burden on participating businesses, and particularly small and medium enterprises. So it kind of simplifies and streamlines the process, and it provides a standard set of documentation. But it is for lower-value procurements. It's mandatory up to \$200,000, and then it can be used up to \$1 million. It can be used as a basis for developing a contract for larger contracts as well.⁸¹

Consultation mechanisms

2.94 Defence communicates and consults with local communities on a range of matters and via a number of different mechanisms. Evidence to the inquiry highlighted that some consultation mechanisms are working effectively while others could be improved.

2.95 Submissions identified the importance of coordination and consultation between Defence, local, state and territory governments, regional development associations, industry networks and community organisations. For example, the South Australian Government submitted:

Establishing an appropriate communication mechanism within the region, requires a coordinated and concerted effort between local businesses, local government, and state government organisations including Defence SA and the Office of the Industry Advocate and the Department of Defence and Regional Development Australia associations in the USG region. This will ensure that local communities have a full understanding of their requirements and potential investment opportunities.⁸²

Defence consultation with community

2.96 In its submission, Defence noted that it 'sees itself as a member of the communities in which it operates' and that Defence is committed to working with all levels of government and community organisations regarding training activities,

80 Ms Jane Wood, Acting Assistant Secretary, Non-Materiel Procurement, Department of Defence, *Proof Committee Hansard*, 21 March 2018, p. 14.

81 *Proof Committee Hansard*, 21 March 2018, p. 14.

82 *Submission 3*, p. 4.

including exercises undertaken in rural and regional communities.⁸³ Defence advised that it communicates and consults on a range of matters including:

- proactive engagement with state and territory governments about estate planning, logistics, community and encroachment issues;
- communication with local government and community stakeholders such as Indigenous communities, local charities, local councils and sporting associations;
- management of legacy unexploded ordnance;
- consultation with the community about major exercises, including potential environmental aspects and proposed mitigation measures, raising awareness of the exercise, traffic flow, contracting and procurement, local business opportunities and advice about resources that would be required. Engagement mechanisms included social media, newspaper and council newsletter, local TV/radio, open days at some bases and 1800 number for enquiries;⁸⁴
- consultation on use of non-Defence land and facilities; and
- minimising aircraft noise on local communities.⁸⁵

2.97 Local council representatives provided evidence about existing consultation mechanisms with Defence. Forums such as the one used to discuss and consult on emergency management was highlighted as a mechanism that was working effectively.⁸⁶ On notice, Defence noted that 'each local community is unique, and that the level and nature of Defence engagement with a local community varies from base-to-base'. Furthermore:

Defence engages continually with local communities where there is a Defence presence and uses direct engagement, utilises existing functions of local, state and territory governments, industry peak bodies and Tier 1 contractors more broadly to provide information. Mechanisms such as the Centre for Defence Industry Capability have been established to provide a source of information for businesses across Australia about potential procurement opportunities.⁸⁷

83 *Submission 9, p. 23.*

84 *Submission 9, p. 25.*

85 *Submission 9, pp. 25–26.*

86 Mitchell Shire Council, *Submission 38*, p. 4.

87 Department of Defence, Answer to written question on notice in advance of 21 March 2018 hearing (received 24 April 2018).

Relationship between Base Commandant and local community

2.98 Throughout the inquiry the committee heard evidence noting the significance of the local base commandant in ensuring good relationships with the local community.⁸⁸

2.99 While the committee heard positive examples, communities saw the relationship as a key one to build on and were concerned should a base commandant be less engaged with the community. The committee asked Defence how it ensures local commandants are appropriately engaged with the local communities and whether there are any policies in place but at the time of finalising the report the committee had not received a response.

Consultation about business opportunities

2.100 Evidence to the inquiry highlighted that there are differences in the consultation mechanisms utilised to inform and educate local businesses about upcoming business opportunities with Defence. A number of business representatives noted that they are often unaware about Defence business opportunities.

2.101 It was observed that in order for local SMEs to be in a position to provide goods and services to Defence, it is important that 'Defence communicate openly with SMEs regarding upcoming demand for labour and goods and services'.⁸⁹

2.102 As highlighted earlier, some Tier 1 contractors are providing information about upcoming business opportunities with Defence. The committee also heard evidence about the role other organisations (such as local council, chambers of commerce, RDAs, state government departments, industry advocates) have in disseminating information about business opportunities. The committee heard different accounts about the effectiveness of these communication channels.

2.103 The committee sought information from Defence about what formal and informal mechanisms are in place with Defence to facilitate information sharing across the range of organisations outlined above. At the time of finalising the report, a response from Defence had not been received.

2.104 The committee notes that the establishment of the CDIC seeks to provide a national network of business advisers to assist understand the defence market and to develop their industrial capabilities and ability to work with Defence. Assisting and consulting with businesses to ensure they are aware of upcoming opportunities with Defence is another information component of providing assistance to SMEs.

Availability of regional information

2.105 It was widely recognised during the inquiry that Defence training activities and the presence of Defence facilities results in economic, social and environmental benefits for rural and regional communities. Although the overarching benefits were

88 See for example, Councillor Rhonda Sanderson, *Committee Hansard*, 20 November 2017, p. 2, Councillor Anna Speedie, *Committee Hansard*, 21 November 2017, p. 2.

89 Livingstone Shire Council, *Submission 5*, pp. 1011.

accepted, detailed information to quantify and monitor such benefits does not appear to be readily available.

Defence contribution to regional areas

2.106 Defence recognised the contribution that Defence bases make to regional Australia:

Defence makes a significant contribution to regional Australia through the presence of Defence bases and people and by fostering linkages with the communities in which Defence members are based. As at January 2017, the total overall number of Defence personnel in regional centres across Australia was approximately 27,427, which equates to 28 per cent of the total 98,161 Defence personnel.⁹⁰

2.107 While every community that appeared before the inquiry indicated support for Defence presence in their region, there was a strong view expressed for more information to be available about the contribution of Defence to regional areas. Every community was seeking details about what and how Defence money was being spent in their region.⁹¹

2.108 The committee notes that additional information about the regional impact of Defence activities would be beneficial for a range of stakeholders. It is recognised that developing a comprehensive profile of the regional impact may also assist SMEs identify future business opportunities as well as areas that they should be seeking to develop their capabilities and capacity across the Defence supply chain.

Provision of regional information from Defence

2.109 Throughout the inquiry, Defence responses at public hearings and on notice varied on this issue. The Defence submission provided some details of expenditure at Defence establishments as well as expenditure for approved capital facilities by state.⁹² Detail about Defence spending in regions was provided in some answers to questions on notice while other responses have noted challenges with reporting local and regional information.⁹³

2.110 In response to a question taken on notice in Wodonga, Defence stated that they would be 'willing to contribute, through the provision of publically available

90 *Submission 9*, p. 3.

91 See for example, Ms Paula Osborn, Deputy Chief Executive Officer, RDA Far North, *Committee Hansard*, 8 June 2017, p. 15; Councillor Margaret Strelow, Mayor, Rockhampton Regional Council, *Committee Hansard*, 12 July 2017, p. 4; Councillor Kevin Mack, *Committee Hansard*, 21 November 2017, p. 3.

92 *Submission 9*, pp. 38–46.

93 See for example, Answers to questions on notice, 8 June 2017 (received 11 September 2017), Answers to questions on notice, 21 November 2017 (received 13 December 2017).

data, to the conduct of a thesis by another agency, on the economic impact of Defence expenditure on the local community'.⁹⁴

2.111 Following that response, the committee sought additional information from Defence about how this could be achieved to meet the need from the community for regional information. Defence advised:

Where information is available and not commercially sensitive, Defence can work with other agencies to identify how the economic impact of Defence expenditure on the local community may be measured and addressed.⁹⁵

2.112 Defence advised that studies analysing the economic contribution of Defence activities have been undertaken, including an analysis of the RAAF Base Amberley to the local Ipswich, Greater Brisbane and Queensland state economy as well as a socio-economic impact assessment of the Australia-Singapore Military Training Initiative (ASMTI) and the associated benefits for Central and North Queensland.⁹⁶

2.113 Defence also noted that in 2018, economic impact studies will be commissioned for RAAF Base Tindal, RAAF Base Williamtown, RAAF Base Edinburgh, Edinburgh Defence Precinct and HMAS Albatross.⁹⁷

Defence seeking to improve the collection of regional information

2.114 The committee pursued the matter of how Defence can better capture information at a systemic level at the Canberra public hearing. The committee was particularly interested in understanding how the existing financial system could be enhanced or better utilised to capture information about the economic benefits of Defence activities at the regional or local level.

2.115 Mr Grzeskowiak reiterated that currently Defence's systems 'are not gathering data in a granular enough way in all cases for us to be confident about figures'.⁹⁸ It was noted that although detailed information is not currently readily available, Defence is doing some work to improve its data collection processes.

2.116 Mr David Spouse, First Assistant Secretary, Financial Services, Department of Defence explained that Defence's financial systems are largely designed around paying suppliers:

That fundamentally means that whoever the contract's with, and whatever their billing address and banking arrangements are, is the system that we

94 Department of Defence, Answers to questions on notice, 21 November 2017 (received 13 December 2017).

95 Department of Defence, Answer to question on notice in advance of 21 March 2018 hearing (received 17 April 2018).

96 Department of Defence, Answer to question on notice in advance of 21 March 2018 hearing (received 17 April 2018).

97 Department of Defence, Answer to question on notice in advance of 21 March 2018 hearing (received 17 April 2018).

98 *Proof Committee Hansard*, 21 March 2018, p. 4.

use to pay those people, and that's the way that it's always been. That also means that, whilst it may be that the majority or even the vast majority of a payment is spent in that local area, particularly where you're dealing with prime contractors or tier 1 contractors that may operate right across Australia or internationally, there's no specific information in that payment necessarily about where the goods were delivered or where the service was provided. What is happening as part of the procurement reform framework is that, internally, all of the contracts and purchase orders that we raise will be required to relate to the postcode, if it's in Australia, where the goods and/or services are going to be provided. That will give us a better picture.⁹⁹

2.117 Under new requirements, when contracts or purchase orders are put into the system for payment, the postcode where the majority of the goods and services will be provided must be included:

Let's assume I'm a Melbourne based tier 1 contractor. When the contract's raised or the purchase order's raised, the parts of the purchase order, or the goods that are delivered to particular locations, where we're aware of those, would be identified against those postcodes. So, if I have a Melbourne based head office but all of the work's done in 5084, 5084 would be identified as the key location for the goods or services to be provided. Now, I wouldn't argue that that's a 100 per cent solution, but I think it would take us a lot further than we can currently provide.¹⁰⁰

2.118 Mr Spouse further explained that under the current requirements, as part of the development of the contract or the procurement document, detailed information about the location of a business engaged to deliver a particular part of the project are not required. In addition:

It's an enhancement to our systems internally, and probably to our procurement requirements, that we would have to take on board. Then there's a question of the amount of effort involved in doing that, and back again into the value-for-money sort of equation. Undoubtedly, that sort of information is available, but it needs to be right at the start of the process rather than as part of what the financial system can represent out of the current specifications.¹⁰¹

2.119 The committee notes the importance of Defence continuing to review and refine the information it collects as the provision and regular reporting of this information will assist the local community and it will also allow Defence to clearly articulate the economic benefit being provided by Defence to communities.

99 Mr David Spouse, First Assistant Secretary, Financial Services, Department of Defence, *Proof Committee Hansard*, 21 March 2018, p. 5.

100 Mr David Spouse, *Proof Committee Hansard*, 21 March 2018, p. 5.

101 Mr David Spouse, *Proof Committee Hansard*, 21 March 2018, p. 5.

