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SENATE

FOREIGN AFFAIRS, DEFENCE AND TRADE
LEGISLATION COMMITTEE

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SENATE

FOREIGN AFFAIRS, DEFENCE AND TRADE LEGISLATION COMMITTEE

Monday, 3 June 2002

Members: Senator Sandy Macdonald (*Chair*), Senator Hogg (*Deputy Chair*), Senators Bourne, Chris Evans, Ferguson and Payne

Senators in attendance: Senators Bartlett, Brandis, Calvert, Collins, Conroy, Cooney, Evans, Faulkner, Ferguson, Forshaw, Hogg, Sandy Macdonald, McKiernan, Payne, Schacht and West

Committee met at 9.06 a.m.

DEFENCE PORTFOLIO

In Attendance

Senator Hill, Minister for Defence

Department of Defence

Portfolio overview and major corporate issues

Portfolio overview (including implementation of White Paper)

Dr Allan Hawke, Secretary of the Department of Defence

Admiral Chris Barrie, AC, Chief of the Defence Force

Lieutenant General Des Mueller, AO, Vice Chief of the Defence Force

Mr Lloyd Bennett, Chief Finance Officer

Budget summary and financial statements

Improvement initiatives (efficiencies, Commercial Support Program, customer-supplier arrangements)

Mr Lloyd Bennett, Chief Finance Officer

Mr Rick Martin, Acting First Assistant Secretary Financial Services Division

Mr Joe Roach, Acting First Assistant Secretary Business Strategy Division

Capital budget: major capital equipment and major capital facilities projects (questions on Defence Materiel, including on materiel reform, and infrastructure projects)

Mr Mick Roche, Under Secretary Defence Materiel

Mr Shane Carmody, Deputy Secretary Corporate Services

Major General Peter Haddad, AM, Commander Joint Logistics

Rear Admiral Kevin Scarce, CSC, RAN, Head Maritime Systems

Dr Ian Williams, Head Land Systems

Air Vice Marshal Ray Conroy, AM, Head Aerospace Systems

Mr David Learmonth, Head Industry Division

Ms Shireane McKinnie, Head Electronic Systems

Air Vice Marshal Norman Gray, AM, Head Airborne Surveillance and Control

Ms Ann Thorpe, Head Materiel Finance

Mr Michael Pezzullo, Acting Head Infrastructure

Air Commodore Noel Schmidt, Director General, Technical Airworthiness

Responses to questions on notice from 2001–02 additional estimates hearing.**Defence outputs****Output 1—Defence operations**

Rear Admiral Chris Ritchie, AO, Commander Australian Theatre

Mr Kevin Pippard, Director Business Management Headquarters Australian Theatre

Output 2—Navy capabilities (Navy Group issues)

Rear Admiral Brian Adams, AM, RAN, Deputy Chief of Navy

Mr Les Wallace, Director General, Navy Business Management

Rear Admiral Kevin Scarce, CSC, RAN, Head Maritime Systems, Defence Materiel Organisation

Mr Mark Gairey, Director General Submarines

Output 3—Army capabilities (Army Group issues)

Lieutenant General Peter Cosgrove, AC MC, Chief of Army

Mr Lance Williamson, Director General Corporate Management and Planning—Army

Output 4—Air Force capabilities (Air Force Group issues)

Air Marshal Angus Houston, AM, Chief of Air Force

Mr George Veitch, Assistant Secretary Resources Planning Air Force

Air Vice Marshal Ray Conroy, AM, Head Aerospace Systems

Output 5—Strategic policy (including Defence Cooperation Program)

Dr Richard Brabin-Smith, AO, Deputy Secretary Strategic Policy

Air Vice Marshal Alan Titheridge, AO, Head Strategic Command

Ms Myra Rowling, First Assistant Secretary Strategic International Policy

Output 6—Intelligence (including Defence Security Authority).

Mr Ron Bonighton, Acting Deputy Secretary Intelligence and Security

Mr Stephen Merchant, Acting Director Defence Signals Directorate

Ms Margot McCarthy, Head Defence Security Authority

Business processes**Defence Science**

Dr Roger Lough, Acting Chief Defence Scientist

Dr Tim McKenna, CSM, First Assistant Secretary Science Policy

Ms Chris Bee, Assistant Secretary Science Corporate Management

Inspector General (including portfolio evaluations)

Mr Claude Neumann, Inspector General

Public Affairs

Ms Jennifer McKenry, Head Public Affairs and Corporate Communication

Mr David Spouse, Acting Director-General Communication and Public Affairs

Corporate Services (including management decision support (information systems))

Mr Shane Carmody, Deputy Secretary Corporate Services

Mr David Kenny, Head Information Systems Division

Mr Ken Moore, Head Service Delivery Division

Mr Michael Pezzullo, Acting Head Infrastructure

Mr Ian Clarke, General Counsel Defence Legal Service

Mr Patrick Hannan, Chief Information Officer

People**Defence Personnel (recruitment and retention, recruiting advertising)**

Rear Admiral Russ Shalders, Head Defence Personnel Executive

Mr Felix Bleeser, Deputy Head Defence Personnel Executive

Commodore Louis Rago, Director-General Personnel Plans

Ms Bronwen Grey, CSM, Director Equity Organisation

Department of Defence

CHAIR—Good morning. I declare open this meeting of the Senate Foreign Affairs, Defence and Trade Legislation Committee. I will shortly be welcoming Senator Hill, the Minister for Defence; Admiral Barrie, Chief of the Defence Force; Dr Hawke, Secretary of the Department of Defence; and officers of the Defence organisation. The committee will consider particulars of proposed expenditure for the Department of Defence, the Defence Housing Authority and the Department of Veterans' Affairs. The committee has before it the particulars for proposed expenditure for the service of the year ending 30 June 2003—documents A and B—and the portfolio budget statements for the Department of Defence. The committee will first consider the portfolio overview and major corporate issues. We will then move on to the outputs, business processes and people.

When written questions on notice are received the chair will state for the record the name of the senator who submitted the questions. The questions will be forwarded to the department for answer. The committee has resolved that the deadline for the provision of answers to questions taken on notice at these hearings is Thursday, 11 June 2002. I remind colleagues that the Senate Finance and Public Administration Legislation Committee is continuing to monitor the format and contents of the portfolio budget statements. If you have any comments you wish to make about these documents, please place them on the public record during these estimates hearings or direct them to that committee.

Witnesses are reminded that the evidence given to the committee is protected by parliamentary privilege. I also remind witnesses that the giving of false or misleading evidence to the committee may constitute a contempt of the Senate. The Senate has resolved that there are no areas in connection with the expenditure of public funds where any person has a discretion to withhold details or explanations from the parliament or its committees unless the parliament has expressly provided otherwise. An officer of a department of the Commonwealth shall not be asked to give opinions on matters of policy. However, you may be asked to explain government policy, describe how it differs from alternative policies and provide information on the process by which a particular policy was selected. An officer shall be given every opportunity to refer questions asked of that officer to a superior or to the minister. The minister has not yet arrived, so I cannot ask him whether he wishes to make an opening statement. Dr Hawke, do you wish to make an opening statement?

Dr Hawke—No, Mr Chairman.

CHAIR—We will now move to questions for the portfolio overview.

Senator COONEY—I have a question to do with the DSD. It is in respect of a very courteous letter from you, Dr Hawke, a very spirited press release by Senator Hill and a very interesting report from Mr Blick on the gathering of intelligence from communications emanating from PILCH. I am wondering whether this is the time to do it or whether I should wait until DSD comes on board. I was originally told that this matter would come on quite early, but I have now been told that DSD is down the line a bit.

Dr Hawke—We could get the director of DSD to come straight over.

Senator COONEY—No, I will wait my turn. Would it be more convenient to wait until later?

Dr Hawke—We can get him over during the course of the morning, Senator, and deal with it then. We will get him to come over now.

Senator COONEY—We would need Senator Hill to be here as well.

Dr Hawke—Yes.

Senator COONEY—Do you know the material? I suppose you do.

Dr Hawke—I signed the letter as a result of the report of the Inspector-General of Intelligence and Security, Mr Blick. There was a recommendation in that report that I should write to a number of people apologising for the incidental collection—

Senator COONEY—This is the one that was sent to PILCH, the Public Interest Law Clearing House?

Dr Hawke—Yes.

Senator COONEY—I would have to declare an interest, by the way. The communication emanated from my daughter-in-law. Mr Chair, what would be the best thing to do?

CHAIR—I would very much like to cooperate in any way that I can. We have a very large program ahead of us. It is output 6, and I am sure there will be other questions on output 6. Are you proposing to be here for the next couple of days?

Senator COONEY—Yes, I will be here. It is just that I was told that it would be on this morning.

CHAIR—I am in the hands of the committee, but my personal feeling is that we should start by going over the portfolio overview. We will make sure that we contact you when we get to output 6.

Senator COONEY—Thank you very much, Mr Chair. Thank you very much, Dr Hawke.

CHAIR—I think that is the best way to approach it, Dr Hawke.

Senator CHRIS EVANS—Dr Hawke, perhaps the starting point, from my point of view, would be to ask for your response to the ASPI Defence budget brief and the comments they made about accountability and the adequacy of the Defence budget information. Would you like to make some opening remarks about how you see that?

Dr Hawke—That ASPI report was released while I was overseas, and I have not had time to study it in detail. I gather it is about 150-odd pages in its own right so, if it was meant to explain the Defence budget in a simpler way, I expect they would have had as much trouble with it as we have had. It is unclear to me what their recommendations actually mean. I saw a list of about four or five points, but there is no explanation from them about what they would do differently in an endeavour to overcome those points. I thought one particular comment was rather gratuitous, and that was the comment about the Defence outcome. If Defence is not there to defend Australia and its national interests, I would like them to tell me what it is there for. So I take exception to that point. As far as the rest of it goes, you can cut the figures in different ways—we have, Treasury has and so have they. I guess that is because there is still some uncertainty about the presentation of this material.

I say that because I am aware that some little time ago the management advisory committee, which is a group under the Public Service Act chaired by Mr Moore-Wilton—it comprises all secretaries and a number of statutory agency heads—looked at some of the issues across the Australian Public Service and the Commonwealth sector and decided that there should be a review of the accrual budgeting framework. Quite a lot of work had gone into that prior to the election, but on the back of the election and the changes in secretaries Dr Ian Watt, who is the Secretary of the Department of Finance and Administration, is reviewing that material before it comes back to the management advisory committee. So I expect there to be some recommendations from that dealt with by secretaries and they probably will go forward for consideration by the government, and it may include the way in which information is presented in the portfolio budget statements.

Senator CHRIS EVANS—You have seen enough of the report to be able to take offence at parts of it, obviously, Dr Hawke. One of the more general concerns it raised was the amount of information and what it says is the lack of description of the Army, Navy and Air Force outputs, in particular the lack of detailed information—information that was in the 1998-99 budget papers about each of the forces, their targets, flying hours and those sorts of things that are not in the more recent documents. From a senator's point of view, we find the outputs a bit skimpy as well. Is that one of the areas that has been considered?

Dr Hawke—There is a series of balances to be struck here. One balance is the size of the document itself, which is already that size. It was not clear what ASPI was suggesting should be provided additionally, but if you would like further information of that nature I am sure the minister would be prepared to consider looking at the addition of that material in the future.

Senator CHRIS EVANS—I guess I have the advantage in that I just put questions on notice and seek it out anyway, but certainly it raises a concern about the information under the Army, Navy and Air Force outputs and it may be something this committee would like to discuss at the end of this estimates process. Is that any reason why some of these figures that used to be in the budget are no longer included?

Dr Hawke—No, there is no reason at all. We will go back to the minister, and it would not be a big problem or concern for us to have that material included if the committee and the Senate would like that.

Senator CHRIS EVANS—What about the capital projects issue?

Senator Hill—You have to be precise, though, about what you want.

Senator CHRIS EVANS—Some of the criticisms in the ASPI budget brief were really aimed at the point that information that was in the budget two or three years ago is no longer in the budget, particularly the outputs of each arm of the Defence Force, and that less information is available about what the money is spent on.

Senator Hill—I have not read the report yet, but that is a complaint made by every estimates committee and, in most instances, it relates to changing over to accrual budgeting. I do not think you can just ask us to produce what was produced in the past. If there are specific questions you want answered, then we will get answers.

Senator CHRIS EVANS—I did not do that. I raised in general with the secretary—you were not here at the time—the criticisms raised in the ASPI report and asked what Defence's attitude and response to that was.

Senator Hill—The answer to that is that we have not considered it yet.

Senator CHRIS EVANS—The conversation flowed from that. I was not saying I was denied particular information; I was raising the concern they raised, which I also have, that there is a lot less information than there was in previous budgets about what the money is spent on.

Senator Hill—That is because it is accounted for differently these days.

Senator CHRIS EVANS—Is that the reason, though?

Senator Hill—It has been the reason in every other committee.

Senator CHRIS EVANS—It has been the reason used in every other committee.

Senator Hill—I am only surmising, but I have said that if you, from your examination of previous budgets, nevertheless want further specific information from us in relation to this one, let us know what you want and we will seek to get it for you.

Senator CHRIS EVANS—What I want to do, though, in the first place is to have a general discussion about what is included in the budget papers and why information that used to be included is no longer included. To be frank, I do not think accrual budgeting is the reason for that.

Senator Hill—I do not know.

Dr Hawke—I think that it actually is the reason for what has happened but, as I mentioned to you just before the minister came in, Dr Watt is reviewing the approach to accrual based outcome budgeting. My guess is that, in association with that, he will be looking at the nature of material presented in the portfolio budget statements. We would expect some consideration of that between now and the next estimates period.

Senator CHRIS EVANS—Perhaps, for your information, I will mention a couple of things—for instance, budget papers used to include the targets for flying hours for naval aviation, days at sea for patrol boats et cetera and whether or not Defence met those targets. Those are no longer included. Those are the sorts of things that probably flesh out better what is happening inside the portfolio and what the money has been spent on.

Dr Hawke—The other balance to be struck here, of course, concerns information which is classified. We are trying to get enough material to show you what is going on, but certainly not to reveal the intimate inner workings of the ADF. I am sure that you would not expect us to do that.

Senator CHRIS EVANS—That is why I started with information that you used to put in your budget papers, which clearly was not classified and which you used to be able to produce. I think that is a reasonable starting point for that discussion.

Dr Hawke—What I am unsure of is whether that was associated with the cash based approach. But if there are indicative issues there of the use of the ADF assets then certainly we could have a look at that and provide a recommendation to the minister.

Senator CHRIS EVANS—I just get a bit sceptical—a new accounting system seems to be an excuse for everything these days. I think people do that partly because they know I do not understand the new system. Can I ask you about the Defence management of finance plan. Senator Hogg tells me that he understands this, but can you just give me a brief explanation of how that plan works?

Dr Hawke—It was a requirement of the white paper that Defence produce an annual Defence management and financial plan which goes to the minister. Following his

consideration, the amendments that he might require and his approval, it then goes to the government and to the Expenditure Review Committee for consideration in the budget context each year.

Senator CHRIS EVANS—Where would I find that plan?

Dr Hawke—It is classified.

Senator CHRIS EVANS—It is a classified document?

Dr Hawke—Yes.

Senator CHRIS EVANS—How is it used, then, within Defence?

Dr Hawke—It is used by the government in deciding how we are going in terms of the management reforms and the financial planning and pressures for consideration in the Expenditure Review Committee—decisions on which, of course, are reflected in the budget and in the PBS.

Senator CHRIS EVANS—So this does not have any public accountability feature about it, then?

Dr Hawke—The public accountability finds effect through the portfolio budget statements.

Senator CHRIS EVANS—So the plan is only used by very senior officers inside the defence department and the minister?

Dr Hawke—And the government. The other part of the accountability mechanisms is the annual report, which you also receive as a public document.

Senator CHRIS EVANS—Thanks for that. Can I ask about the issue of costing election promises that was raised with DOFA last week. I presume that despite your travels you have been briefed on that discussion, Dr Hawke.

Dr Hawke—I am vaguely aware of that.

Senator CHRIS EVANS—Can someone tell me the process and what information Defence provided to DOFA regarding Defence costs and the impact on their preparation of the election documentation, the Charter of Budget Honesty?

Dr Hawke—Yes. I will come back to that. Perhaps I should start by telling you that I provided the authority of advice about the cost pressures and the like to the new Minister for Defence on 4 December, but it is true that there were discussions between Defence and Finance officials before that over a period of time. Those issues did not receive final approval within Defence for going to the minister until I signed the submission to the minister on 4 December.

Senator Hill—Rather than just speaking vaguely about what might have been discussed last week, if you put the specific question at least I will understand what you are talking about.

Senator CHRIS EVANS—It was really just a point of reference for Dr Hawke. There was a debate at DOFA estimates about the whole Charter of Budget Honesty process and the costings for the election. You might recall, Minister, that there were no extra costings in the DOFA papers, as I understand it, for the deployments to the Middle East and—

Senator Hill—This is at the time of the election.

Dr Hawke—That is correct, because there were no decisions associated with that at that time. It was always our intention to put forward for government consideration in the additional estimates context the additional moneys required for a range of activities. Because of the ongoing nature of those activities, like the war on terrorism and the interception of unauthorised boat arrivals, they were dealt with in the budget for next financial year. So those figures were not accumulated or presented to government for decision until after I wrote to the minister on 4 December and then they went into both the additional estimates process for our current financial year and into the separate ERC process for the 2002-03 budget year.

Senator CHRIS EVANS—I accept that, Dr Hawke. But it is also true you did not wake up on 4 December and say, ‘Gee, this is going to cost us a lot of money and I did not know about this before.’

Dr Hawke—That is correct.

Senator CHRIS EVANS—What I am trying to understand is what your understanding earlier in the piece was about the cost of these operations and whether Defence was going to absorb them or not. Clearly, by February we worked out it was going to cost us \$339 million and that Defence needed that money. What was your understanding prior to that—that you were just going to have to absorb those costs?

Dr Hawke—We did not have an understanding because these issues were not considered before the caretaker period and of course would not have been considered during the caretaker period.

Senator CHRIS EVANS—Why would they not have been considered before the caretaker period?

Dr Hawke—They just weren’t.

Senator CHRIS EVANS—No-one thought about what these deployments were going to cost us before the caretaker period?

Dr Hawke—Well, we may not have calculated them but my recollection is that they were not an issue.

Senator Hill—For this coming year we have included a figure because we are engaged and we are better able to assess what the likely cost is going to be. That said, it is still a guesstimate in many ways. If there is a shortfall, we hope that that will be recognised by government as a whole and that it will be supported at the next appropriations. Certainly, in relation to the war against terrorism, I think that is not surprising.

Senator CHRIS EVANS—At the time of the decision to deploy there was no consideration of costs?

Senator Hill—I do not know the answer to that. Do you mean in terms of—

Senator CHRIS EVANS—In terms of how we are going to pay for it.

Senator Hill—There was no decision. I was not part of the NSC then but I think the Treasurer made some comments that he believed that the costs could be funded internally. Certainly, when we got to the additional estimates situation late last year we bid for a sum of money which we argued was a reasonable contribution to the additional costs to Defence that we had incurred. Out of the process of negotiation we received some additional support.

Dr Hawke—As the minister says, the approach was to seek the net additional costs. That is important because the net additional costs mean that, had those assets not been doing what

they were doing in relation to the war on terrorism or the interception of illegal immigrants, we would have been using them for training or something like that. So we netted off those costs in order to provide the ask to the government at the time.

Senator CHRIS EVANS—I understand that, Dr Hawke. Perhaps we should go back a stage. Traditionally, when we deploy, what general funding arrangements are made in terms of Defence? Do you have to carry the cost or do you seek extra appropriations? How does it normally work?

Dr Hawke—I think we have now established a principle that Defence will be supplemented for the net additional costs of these operations. You can see that in terms of East Timor, Bougainville, interception of illegal immigrants and the war on terrorism. It depends: I guess if it was not seen to be a significant sum of money the NSC might say, 'Our view is that Defence can absorb that amount of money.' There is no hard and fast rule, but on the bigger deployments that is the principle and the approach that the government has been taking.

Senator Hill—East Timor, because it was an ongoing process, was included in the last budget; the war against terrorism, which was a new process during the course of the financial year, was not.

Senator CHRIS EVANS—I understand that. I am just trying to go back to the process. So there is a general understanding that Defence will be supplemented for the cost of overseas deployments—or Dr Hawke likes to hope that the principle has been established, as I am sure secretaries would. There is a precedent for that occurring. What I am trying to understand is what decision, then, was made. Clearly when we committed to these overseas deployments, the war on terrorism et cetera, there must have been some understanding that a cost went with that.

Dr Hawke—No. You will recall the minister said that, at that stage, the Treasurer was of the view that the costs associated with that might be able to be absorbed within the total Defence budget—that is, the Defence costs; there were other costs, of course, to other departments like Immigration.

Senator CHRIS EVANS—I was more interested in what Defence's view was. Was that your view as well?

Dr Hawke—We put a view to the minister that we were not able to do that. We put a view to the minister about what we thought was fair in the circumstances. He supported that and took it to the government.

Senator CHRIS EVANS—When did you first put that view to the relevant minister?

Dr Hawke—On 4 December.

Senator CHRIS EVANS—So you did not make any approach to your minister prior to that about the costs of the war on terrorism?

Dr Hawke—No; 4 December was when we provided advice. I wrote the submission to the minister.

Senator CHRIS EVANS—I just want to be clear: I am not only asking about Minister Hill; I am asking about his predecessors.

Dr Hawke—The advice went to Senator Hill as the new minister on 4 December.

Senator CHRIS EVANS—So when we committed to the war on terrorism there was no advice from Defence to cabinet or the Prime Minister about the cost of that?

Dr Hawke—There was no decision taken, to my recollection.

Senator CHRIS EVANS—Was there any advice about what this might cost?

Dr Hawke—I do not recall that. I am not sure there was.

Senator CHRIS EVANS—No-one actually asked what the cost was going to be?

Dr Hawke—We would not have done the figure work or had an idea at that stage about the likely cost.

Senator Hill—The government made a decision on the deployment and accepted, obviously, as part of that decision that it would have to be paid for. What we are really talking about this morning is how that is to be accounted for. It seems that issue was not dealt with at that time possibly because of uncertainty over what the additional cost would be. Additional costs in Defence are not easy to calculate, in any event.

Dr Hawke—If the point is that these figures should have been included in the Charter of Budget Honesty, I am a bit puzzled because we had not done the work on what the costs were and we were not in a position to put those costs forward. I not sure how Finance or Treasury would have gone about costing that in a separate way to us—if that is the issue.

Senator CHRIS EVANS—I am keen to understand how it works. Suddenly on 4 December it was a major issue and, with all respect to the minister, there was a bit of work done explaining to the public the issue of how much pressure Defence funding was under.

Dr Hawke—There was a new minister and we provided the new minister with a range of briefing material to assist him in coming in as the new Minister for Defence. One of those things obviously of considerable importance to him and us was the funding situation then, and what it was likely to be in the future.

Senator CHRIS EVANS—Sure. Maybe it is my lack of understanding but I am a little surprised, I suppose, that the issue of the cost of all this would not have been raised with the relevant minister prior to then.

Dr Hawke—It is just part of the normal additional estimates and budget cycle. We were just proceeding along the normal lines. I think the additional estimates cycle this year was changed as a result of the timing of the election campaign itself.

Senator CONROY—When the announcement was made to deploy the troops, the ship and the planes, did Defence do any costings?

Dr Hawke—I do not think we did. I would have to check that but my recollection is that we did not do those things at that time.

Senator CONROY—On 17 October—that is the date, I think, from my questioning of the DOFA officials last week—the Treasurer certainly and, I think, the Prime Minister indicated that there would be no extra costs for the rest of the financial year.

Dr Hawke—My recollection is that the Treasurer said that he thought the additional costs associated with these issues could be absorbed within the Defence budget, that is true, but when he and his department came to consider the detail of that at additional estimates time he was, as was the government, convinced that there were net additional costs that needed to be supplemented.

Senator CONROY—So when on 17 October—and do not hold me to the exact date—the Treasurer stands up publicly during an election campaign and says that these costs can be absorbed, you are saying that Defence had done no costing whatsoever of our commitment?

Dr Hawke—Defence had then put in place what we would do if we had to absorb those costs, and we continued along that path until the outcome of the additional estimates process. It would not have been prudent for us to do anything other than that, in my view.

Senator CONROY—So you had no correspondence with the government of any kind after the Prime Minister and the Treasurer indicated that there would be no additional costs?

Dr Hawke—Not that I recall.

Senator Hill—When?

Senator CONROY—I think it was 17 October.

Senator Hill—Obviously, if I put a bid in the additional estimates—

Senator CONROY—This is before your—

Senator CHRIS EVANS—You were still concerned with the environment at the time.

Senator CONROY—You were still hugging trees at this point, Senator Hill. Were you aware of the Prime Minister's and the Treasurer's statements that there would be no additional costs from the expenditure?

Dr Hawke—Absolutely. That is why we planned on the basis that we might have to absorb those costs. It would not have been prudent for me or Defence to make any other assumption given what the Treasurer had said.

Senator CONROY—There had been a lot of discussion earlier when we invoked the ANZUS commitment after September 11 and it was first indicated by the Prime Minister that the President had been on the phone and that our position was that we would support the war against terror within our means. Are they the key words that ring a bell?

Dr Hawke—I do not recall.

Senator CONROY—Was it something along those lines? I will happily get the quote and come back to you if you are unfamiliar with the Prime Minister's major commitment in Defence over the last six months. I will track that quote down for you exactly. From recollection it was something along the lines that we would help in the war against terrorism within our means, within an already tight budget.

Dr Hawke—That is not necessarily what the Prime Minister may have meant, Senator. He may have meant within the means of our capability and the range of other operational activities that the government had committed the ADF to.

Senator CONROY—I probably agree with you that that is what he meant. When I use the words 'within our budget' I encapsulate all of those things you have just described. There had been a fair bit of comment publicly that we were stretched. We had a full, important commitment in East Timor and we had ships patrolling in the Middle East as part of the blockade against Iraq and we were not sure what we would be able to contribute to the war on terror.

Dr Hawke—That is correct.

Senator CONROY—So it was generally considered that Defence was working away under fairly tight conditions.

Dr Hawke—I would not necessarily say ‘tight’. If you ask the people in the ADF, I think they would tell you that this is what they joined the ADF to do.

Senator CONROY—I am not disagreeing with that at all; I think it is a commendable approach. Of course, everyone will always do what they can with the available resources but there was a lot of media and public comment that we were committed in a number of fields.

Dr Hawke—Correct; we were, and are.

Senator CONROY—And it would be only a limited contribution that we could make to the war on terror. That was the general view and no-one disagreed with it. We have a substantial commitment in East Timor and in policing the blockade in the Middle East. So when the Prime Minister indicates that it will be within available resources, that must have got you scratching your head and thinking, ‘Well, we are pretty well engaged in a lot of different places at the moment and here is the war on terrorism and it is going to be no net cost to the Department of Defence.’

Dr Hawke—If there is no net cost, we do not have a problem.

Senator CONROY—You are the person in the best position to judge whether that is actually feasible.

Dr Hawke—And I did, and I presented the case to the minister and when he was satisfied with that case he took his position to the government. In terms of the ADF assets, the government will basically decide on what sort of military response options it wants to put forward, and it does that in consultation with CDF as the principal military adviser. He basically does that in concert with his US colleagues. He provides the advice to the government and it made the decision about the range of capabilities that we would offer to the United States and what was agreed and what was then deployed in support of the war on terrorism.

Senator CONROY—Sure. But when you go from your normal peacetime role—defence exercises and those sorts of things—when you step up from a peace footing to a war footing, commonsense would say that you are going to be doing a bit more than you were doing previously. Is that fair?

Dr Hawke—Yes, that is correct.

Senator CONROY—And doing a bit more than previously would probably involve spending a dollar more than was spent previously?

Dr Hawke—Exactly. But it is quite within the confines of government and their resourcing strategy for them to require us to absorb some or all of that cost. Our job is to explain to the minister, and through the minister to the government, what the implications of that might be. So, if it was a considerable sum of money, we might have had to stop recruiting or we might have had to stop other operations and training in order to fund what the government considered to be the priority. That is the way in which we handle that sort of issue.

Senator CONROY—On 17 October the Treasurer says, ‘We are going to deploy these extra resources, we are going onto a war footing and there is no net cost to Defence.’ At this point, as you said, presumably you have to start drawing up the areas in which you are going to reduce your activity to accommodate the Prime Minister’s and the Treasurer’s commitment. Is that fair?

Dr Hawke—Yes, we were putting plans in place as to how we would meet the government’s commitments and absorb those costs.

Senator CONROY—When the announcement was made on our troop deployment, what was Defence's best estimate of how long that deployment would be in place? Was it for the weekend; was it for three months?

Adm. Barrie—The answer to that question is that it depends. It has to be recognised that the initial cost of a deployment in the ADF is not all that high. The real cost drivers inside Defence come from building rotation forces to replace troops already committed in the field and for the cost of sustainment—that is, the logistics effort, depending on the intensity of the operations being conducted. In the period we are describing, we had an election result due on 10 November, so the initial commitment made by the government was quite low cost. What was of concern and what had to be put to a new government was: what would be the costs of an ongoing commitment of the ADF along those lines? I think that is quite properly what the secretary said was brought to the minister later.

Senator CONROY—Thank you, Admiral Barrie. Can I just come back to the announcement on 17 October. You mentioned the election on 10 November. Presumably, when the Prime Minister made the announcement on 17 October, you believed there was going to be an ongoing commitment? I read a quote last week—and, again, I am happy to track it down—that this would not be a short—

Adm. Barrie—The answer to that question is that nobody knew. The sort of commitment we ended up making in the first instance was one that suited the coalition leader, the United States. We were very much mindful that, as operations began, we would not know with any precision where this would go. But, in all those circumstances, Australia's initial contribution looked very reasonable at the time.

Senator CONROY—I am not questioning the level of the contribution; I just want to know—and you are the CDF—what was in your mind on 17 October. You were involved in putting together what our contribution would be—as I think Dr Hawke and you have said. How long did you think our contribution would be committed for?

Adm. Barrie—I think that is an open-ended question and one that I am not able to answer simply because—

Senator CONROY—Did you think it was going to be—

Senator Hill—The PM made an original commitment of 12 months, didn't he? It may be that the government initially decided that the full costs would be borne from within Defence. In the end, they did not decide that; they allowed a certain supplementation. But prudent planning means that, if you have not been given extra money, you plan to fund it internally.

Senator CONROY—Thank you, Senator Hill. I do not remember hearing about the 12-month commitment. Admiral Barrie, does what Senator Hill said ring a bell with you? Was it your belief that it was going to last 12 months?

Adm. Barrie—No, it does not ring a bell with me. But everyone is entitled to their view, and the fact of the matter is that we do not know.

Senator Hill—It is not a question of how long we will be involved in this. In fact, we think we are going to be involved in some form or other for years. The PM made certain commitments—and I am going from memory too; it is true that at that time I was hugging trees—for 12 months.

Senator CONROY—Admiral Barrie, did you believe that our forces and our contribution would be completed on 10 November, or did you believe it would be longer than that?

Senator Hill—On 10 November? Last year?

Senator CONROY—Yes; that is the election. So we go from 17 October to 10 November—did you believe our contribution would be concluded by then?

Adm. Barrie—No.

Senator CONROY—Did you believe it would be concluded by 4 December?

Adm. Barrie—That depended on the new government. It is the government that makes this decision, not me. An option for any new government coming in after the result of the election is to bring our forces home after the initial deployment.

Senator CONROY—Sure. Was the Labor Party's position well known to you, the fact that we supported the war on terrorism?

Adm. Barrie—That does not matter. The fact of the matter is that I advise the government and the government would have been in a position to make its own decision after the result of the election.

Senator CONROY—When the Prime Minister announced that there was going to be a long-term commitment—which the opposition, the alternate government, committed to support—did you believe that the contribution by our troops would still be going by Christmas?

Adm. Barrie—Yes.

Senator Hill—With great respect, that is a silly question.

Senator CONROY—Thanks for your opinion, Senator Hill. I think you are at the day for estimates.

Senator Hill—I hope we are not going to sit here all day listening to silly questions.

Senator CONROY—Thanks for your contribution, Senator Hill. If you had been paying attention when you were sitting in the chair last week at the DOFA estimates, you would actually remember the conversations that took place, Senator Hill. The reason that I am asking this is that DOFA indicated to us last week that Defence used the phrase 'short term' when it was having discussions with DOFA. You might remember, Senator Hill, I had a lengthy chat with Dr Watt about what 'short term' was and I am just looking to gain an understanding from Admiral Barrie what a military definition of 'short term' is.

Adm. Barrie—'Short term', for me, means you make an initial deployment for a certain period of time and if you get to the end point you bring the forces home; that is short term. Sometime during that period, if you decide to replace those forces you then incur all the costs of rotation. And in my view, the decision about ongoing commitments would have been made by a new government after 10 November.

Senator CONROY—So when you say that in your view there was the initial short-term deployment, what did you believe that short-term deployment was?

Adm. Barrie—Whatever it was we announced for the various forces we committed at the time. I think we have various time frames but, broadly speaking, four to six months.

Senator CONROY—That rings more of a bell than the 12 months. I do not remember the 12 months coming from the Prime Minister, which Admiral Barrie does not remember either.

Adm. Barrie—You have to differentiate between the two things, Senator. That was the initial deployment of forces.

Senator CONROY—Please, you do not have to worry. It was Senator Hill that contributed the 12 months, Admiral Barrie, not me.

Senator Hill—I was trying to be helpful.

Senator CONROY—There was no trap here. Senator Hill had suggested the 12 months. When you prepared the initial deployment, you were thinking in terms of four to six months. Dr Hawke, did you do calculations based on a four- to six-month commitment?

Dr Hawke—I am not sure what we did at that stage.

Senator CONROY—Did you not chat with the Admiral?

Dr Hawke—No. This would have been going on in the chief financial officer's area to prepare these estimates and there certainly would have been discussions at officer level between them and the department of finance, if not the Treasury. The point is that I put forward to the minister the authoritative advice on 4 December. I might just add something to Admiral Barrie's comments. The government do, of course, review our commitment to the war on terrorism and other operations on a very regular basis and they do that quite often in terms of the individual capabilities and the totality of the capability. The rollover of the Special Air Services Regiment, the decision to bring the FA18s home, the rotation of the ships on station there et cetera are considered on quite a regular basis. Each time, informed by CDF, they make a judgment about whether that will continue, in what form and until what next review point.

Senator CONROY—I appreciate that. I am really just trying to get an understanding of what Defence's view was of how long we were likely to be committed to the war on terrorism. The Prime Minister has said it will be a long-term fight because it is not a simple one. Admiral Barrie has indicated that after the election on 10 November anything was possible, notwithstanding the alternate government saying that they were committed to the war on terror. I know you were overseas or possibly on leave or a combination of the two, Dr Hawke.

Dr Hawke—When DOFA approached us?

Senator CONROY—Yes. DOFA indicated last week that they approached you to test the costings as part of the Charter of Budget Honesty and that they approached and had iterations and conversations prior to 7 November.

Senator Hill—Who spoke with whom?

Senator CONROY—I think Dr Watt indicated that DOFA had formally spoken with Defence. Just so you understand the process: the government and the opposition submit their costings for their policies. On 7 November DOFA released a document verifying that on their best calculations there was no net cost for Defence. A zero dollar commitment was listed in the Charter of Budget Honesty statements on 7 November, a couple of days before the election.

Senator Hill—It has taken a long time to get to it, but the question is: do you know of being approached by DOFA?

Dr Hawke—No, I do not.

Senator CONROY—If I could actually ask the question and perhaps Dr Hawke—

Senator Hill—Yes, but you are taking hours.

Senator CONROY—could respond to my question rather than yours, Senator Hill. You can chat with him later.

Senator Hill—Yes, but why don't we get to the point and we will save a lot time?

Senator CONROY—I just wanted to get to the point of what Defence's understanding of a short-term commitment was. DOFA indicated in testimony to the Senate last week—

Senator Hill—No wonder the estimates are taking so long.

Senator CONROY—that upon receiving the government's policy documents they costed them. I think their words were: 'Where do you go to test the veracity of the assumptions in the policy documents? Well, we went to the experts. We went to Defence, and Defence assured us, in the period leading up to 7 November, that there were no extra costs to be incurred.' So did DOFA approach you?

Dr Hawke—I am unaware of that approach. I will have to ask Dr Watt about that. He was not even there at that time.

Senator CONROY—I understand that. But Dr Watt and the entire department of finance were sitting about where you are.

Dr Hawke—I understand the point you are making. But I am certainly unaware of that.

Senator CONROY—You were away during some of the period?

Dr Hawke—No, I was there.

Senator CONROY—You were there in that period.

Dr Hawke—But I do not know every little thing that happens in the organisation. It is quite usual for there to be discussions at officer level.

Senator CONROY—I was just wondering if you might be able to inquire for us and come back at some stage during the day as to whether or not DOFA did approach you in that Charter of Budget Honesty process.

Dr Hawke—We will ask.

Senator CONROY—And you will give us the answer?

Dr Hawke—Yes.

Senator CONROY—Okay. Thank you. At some stage during the day you will be able to check it out?

Dr Hawke—We should be able to do that.

Senator CONROY—Thank you very much. DOFA indicated that the Department of Defence signed off—

Senator Hill—Get the answer from Dr Hawke and then we will follow it up.

Senator CONROY—I am just giving him some more information to help him with his search. DOFA indicated that Defence had agreed that there was no net cost as part of that process.

Senator Hill—No net cost, or Defence did not have a right to expect additional funding?

Senator CONROY—I think what DOFA indicated—and the testimony is on the public record, so—

Senator Hill—Of course there is a net cost.

Senator CONROY—I am sorry: no additional net cost. Can I put the word 'additional' in there, just to make you happy?

Senator Hill—Of course there is additional net cost if you take on extra deployments.

Senator CONROY—Tragically, that is not what the Treasurer, the Prime Minister and the department of finance—and, the department of finance claim, the Department of Defence—said by 7 November, three days before the election.

Senator Hill—What the Treasurer said was that it had to be paid for by Defence.

Senator CONROY—No, I said ‘additional’. If you are able to come back to us, Dr Hawke, as part of that process, that would be much appreciated. I will pass back to Senator Evans, as I have jumped in here.

Senator CHRIS EVANS—I had a couple of questions about that process but, Dr Hawke, if you are going to take some advice on what occurred between DOFA and Defence, it is probably best if we come back to that when you are forearmed with that information rather than we bat on now in that area.

I wanted to ask some broad questions about the Defence budget. Last time I asked your then chief financial officer about what the figure was that we could take to be the Defence budget. As you are aware, probably far better than I, there are a whole range of different global figures given as the Defence budget. I think on his definition he agreed with ASPI that the \$14.6 billion this year would be a fair call as being the Defence budget. Is that your view as well?

Dr Hawke—That is not my view and I do not think he would have agreed with that.

Senator CHRIS EVANS—Well, he took me through what he thought the definition of the—

Senator Hill—What you are now trying to do is disaggregate from the accrual figures. Having gone through the tortuous process of getting to accrual budgeting you are now asking us to try and give you a cash figure.

Senator CHRIS EVANS—I am actually just seeking enlightenment.

Senator Hill—This is one of the reasons people become very confused about these things.

Senator CHRIS EVANS—All we are doing is seeking understanding and enlightenment, Minister.

Senator Hill—Yes, I know. And there are a number of different figures because it depends on by which system you wish the figure to be calculated.

Senator CHRIS EVANS—That is why I wanted a discussion—so we had a joint understanding.

Dr Hawke—What figure would you like to deal with, Senator?

Senator Hill—It is not correct to say, ‘What is the correct figure?’ You tell us the basis of calculation and we will give you the figure.

Senator CHRIS EVANS—I am trying to get an understanding of what the department feels is the best way to describe the Defence budget—what headline figure one would describe as the budget for Defence for the year and why. There is nothing tricky in this. I am just trying to understand what you say the budget for Defence is.

Dr Hawke—We even have a difference of view with the Treasury about this matter. That is dealt with at table 1.1 of the budget, where we believe that the Australian accounting standards should be used and the Treasury prefers to use government finance statistics. As I

mentioned to you earlier, I think these sorts of issues will be resolved in the review that Dr Watt is overseeing right at this moment. If I might answer your previous question, we are not aware of any approach by DOFA to Defence during the Charter of Budget Honesty process.

Senator CHRIS EVANS—I might come back to that because Senator Conroy wanted to pursue it with you as well, rather than do it twice.

Dr Hawke—There is not much you can pursue, if we do not know. I do not know what Senator Conroy wants to do.

Senator CHRIS EVANS—I just thought, rather than you and I have the conversation and then Senator Conroy come and do it twice—

Dr Hawke—Yes, okay.

Senator Hill—He might provide us with further and better particulars.

Senator CHRIS EVANS—Yes. Perhaps as a starting point I will ask: what would Defence say is the best, most realistic figure to look at to describe the Defence budget?

Dr Hawke—The figures are set out there in table 1.2, according to the way in which the accounts are structured. I am still a bit unclear about what your question is.

Senator CHRIS EVANS—All right. Perhaps we will start with some of the detail. You would say to me that the budget for Defence for the year 2002-03 is the \$21,940,482,000 figure?

Dr Hawke—That is the total resourcing; that is correct.

Senator CHRIS EVANS—Would you say that is the Defence budget?

Dr Hawke—No.

Senator CHRIS EVANS—That is probably why I asked you the previous question. What would you say the Defence budget is?

Dr Hawke—It depends on whether you are looking at this in cash or accrual terms.

Senator CHRIS EVANS—In accrual terms.

Mr Roach—There are various ways of looking at the budget. It would probably help if I took you through the different presentations. They are all correct, but they represent different things. As the secretary said, the total resourcing for the Defence portfolio in 2002-03 is \$21.9 billion. In talking about the activities of Defence and the Defence Force's capabilities and operations, we would usually exclude the administered items, which are mainly superannuation and a few other things. They are shown in table 1.2 as \$2.2 billion. It is usual to remove the capital use charge if you want to try to get down to a figure that more closely represents a cash figure. It is not a cash figure; it is simply taking out the capital use charge.

Senator CHRIS EVANS—That is \$5 billion, is it not?

Mr Roach—That is correct.

Senator CHRIS EVANS—We are not talking about small change. That is \$5 billion of the total.

Mr Roach—That is correct. That \$5 billion represents a charge on our net assets. We are fully funded for that and we return it to government.

Senator CHRIS EVANS—It is a straight in and out transaction?

Mr Roach—Correct.

Dr Hawke—That is one of the issues that we have about the way these things are structured at the moment. My hope is that Dr Watt will include that in the issues he is dealing with, because you are absolutely right: it gets added on and then taken off.

Senator CHRIS EVANS—I suggest to you therefore that the figure of \$21.9 billion looks inflated by the \$5 billion which comes in and goes straight out.

Dr Hawke—I understand that. You are now getting towards what the actual cash position is, compared to the accrual position.

Senator HOGG—Under table 1.1 the note states:

... the acquisition of specialist military equipment is accounted for as an expense rather than capital investment.

Mr Roach—That is under the Treasury government financial statistics framework, which I understand is an international accounting convention, as opposed to the one applied to government departmental accounts.

Senator HOGG—But I presume it is not a position that you necessarily agree with?

Mr Bennett—We are required to account under Australian Accounting Standard 29, whereas Treasury use the international approach.

Senator Hill—Just to make it easy to follow.

Senator HOGG—That is my worry. I will come back to that.

Senator CHRIS EVANS—I reread the *Hansard* and then try to understand all this stuff. That is why I am trying to get on top of it. So when the \$1.1 billion increase reported in the budget papers is used to describe an increase in the Defence budget, that includes funding for the capital use charge which is then returned straight to the government; is that right?

Mr Roach—Yes.

Senator CHRIS EVANS—What about the proceeds from asset sales?

Mr Roach—I want to check the \$1.1 billion figure.

Senator CHRIS EVANS—It is my understanding that the \$1.1 billion includes both the capital use charge and the asset sales which, again, are returned straight to the government. I will let you take that on notice. If you could confirm that for me, that would be useful.

Mr Roach—If you are referring to the total increase of \$1.123 billion, that is an increase calculated on figures which include the capital use charge.

Senator CHRIS EVANS—So my understanding is that, in terms of additional funding actually retained by Defence, the best figure to use is the \$400 million—is that right?

Mr Roach—Are you referring to the \$428 million?

Senator CHRIS EVANS—Yes.

Mr Roach—For new measures and other adjustments not including offsets, yes.

Senator CHRIS EVANS—New measures and other adjustments not including offsets—is that the same as real money?

Mr Roach—It represents our funding on an accrual basis.

Senator CHRIS EVANS—Is it fair to say that it represents the additional real funding to Defence?

Mr Roach—You would also have to take into account the offsets that we have been required to make.

Senator CHRIS EVANS—How do you mean?

Mr Roach—Again, it might help if I take you through the figures.

Senator CHRIS EVANS—You mean the cost offsets?

Mr Roach—The \$428 million for new measures and other adjustments in 2002-03 does not include the offsets that we have also had to make, which brings the total net increase down to \$150 million.

Senator CHRIS EVANS—To \$150 million or to the \$107.3 million figure?

Mr Roach—The difference between \$150 million and the \$107 million is that you just quarantine the new measures, the new operations and the like from simply funding adjustments—for example, the special-purpose aircraft transfer.

Senator CHRIS EVANS—All right.

Mr Roach—If you take the \$428 million figure, there are four offsets that bring the total funding increase down. There is the \$150 million repensed from 2002-03 to 2003-04 for the capital program—the defence capability plan; there is a further offset of \$20.9 million for the purchase of high priority explosive ordinance—that offset is also found within the capital budget; there is a saving of \$97 million, made up of a three per cent decrement to our non-operational suppliers fund, which is called the administrative saving in the budget papers; and there is a further \$10 million from advertising. That \$428 million plus those offsets leaves us with additional funding of \$150 million.

Senator CHRIS EVANS—Of the \$1.1 billion?

Mr Roach—No. The \$1.1 billion includes all of the adjustments at a portfolio level, including the capital use charge and a range of other things. The \$428 million relates to the new measures announced in this budget, but that \$428 million does not take into account the offsets which were also announced in this budget.

Senator CHRIS EVANS—So, in layman's terms, the \$428 million is not new money because part of it is actually funded from savings in other parts of the portfolio?

Mr Roach—We have had to make offsets and redirect our funding according to the priorities, yes.

Senator CHRIS EVANS—So would you say that the real new funding figure is the \$150 million?

Mr Roach—That is the net increase to our bottom line for those things.

Dr Hawke—You would have seen, from table 1.1, for instance, the rescheduling of the major equipment acquisition—the minus \$150 million. That is an adjustment just for this year's budget. The money has been added back for the following year's budget, as you will have seen in the next column. So there were a couple of issues like that in order for the government to balance decisions on defence against the total budget approach.

Senator CHRIS EVANS—I appreciate that. I want to go through some of those cost offsets with you in a little while, but I want to get some of this macro stuff clear in my head first.

In table 1.2, I see on the appropriation line that from 2004-05 to 2005-06 it actually falls from \$19.381 billion to \$19.377 billion. That seems to indicate that the total cost of outputs would fall over those two years. Can someone explain that to me?

Mr Roach—Senator, it is a misconception that the white paper funding is a smooth and upward slope; it is actually not. Particularly in the defence capability plan, there was a lot of money in the early years, and that was laid out when the white paper was announced. Similarly, there is a significant ramp-up towards the end of the white paper funding which is to do with some of the very large major capital equipment replacement projects. In the mid years of the decade, the rate of increase in fact drops off. What you are seeing in those two years is essentially a flat part of that curve.

Senator CHRIS EVANS—So that drop-off is explained by lower white paper expenditure than in the previous years?

Mr Roach—The rate of increase is not as great.

Senator CHRIS EVANS—It has nothing to do with the withdrawal of funding for East Timor?

Mr Roach—That appears in 2004-05, and what you see there is effectively the deployment part of those costs coming out of our budget as we plan to wind up the deployment.

Senator CHRIS EVANS—So that would also count for part of the drop in 2004-05?

Mr Roach—In 2004-05 relative to 2003-04, yes.

Dr Hawke—The minus \$150 million is also associated with the fact that the government will be doing an annual strategic review of the circumstances facing Defence this year. In association with that, they are also going to review the defence capability plan. That is the principal reason why that \$150 million was taken out this year. The government wish to have a review of the defence capability plan, both in the immediate and in the longer term, against any change in our strategic circumstances. That process will occur over the course of this year, with conclusions reached, I am sure, by the end of the year to feed into the following year's budget.

Senator CHRIS EVANS—In layman's language, does mean that you decided not to spend the \$150 million because you might change your mind?

Dr Hawke—No, the government wanted to have a relook at the capability plan itself. The issues that you are pointing to here in the out years may well change as a result of government reconsideration of the capability plan over the course of this calendar year.

Senator CHRIS EVANS—I always treat projections for three years hence with some scepticism—as I am sure we all do. What would that \$150 million have been spent on, Dr Hawke?

Dr Hawke—Mr Roach would be able to explain that.

Senator CHRIS EVANS—We will deal with that when we come to it. I have a question on indexation of the Defence budget. I want to again come to terms with the macro issues. I gather it is indexed against a GDP deflator. Is that right?

Mr Roach—Yes.

Senator CHRIS EVANS—For 2002-03, what estimate did you use for that index?

Mr Roach—It is the non-farm GDP deflator.

Senator CHRIS EVANS—Do you know what that was?

Mr Roach—Yes, but I am not sure whether that is publicly available information.

Dr Hawke—That issue was settled in the white paper context, and as you probably know the second issue relates to Defence pricing. The first issue is prices, as you rightly identified, and the second one is exchange rate variations. I think the Treasurer made an announcement about that in the last week, while I was away. But the government made a decision to continue with the existing arrangements that Defence has had for some years, which are presented basically in what is called a no loss, no gain agreement, where Treasury strikes a rate for the Australian currency against a basket of other currencies. If the Australian dollar fluctuates in one particular way against those currencies, Defence returns the windfall gain to consolidated revenue. If it goes the other way, then Defence gets supplemented for the exchange rate variation. That arrangement has been in place for a considerable period of time and has recently been re-endorsed. So, where you read in various reports that Defence has lost this money because it does not hedge, it is absolute nonsense. Because it is not an issue for Defence; it is treated at a whole-of-government level. There has never been any point in or prospect of Defence hedging, nor is it correct to say that Defence has lost this money because of those arrangements.

Senator CHRIS EVANS—So you are basically saying that it is a matter for Treasury and Finance, not for you, because of that arrangement?

Dr Hawke—It is essentially handled by those two agencies, but I am not precisely clear on which one of them does it or how they do it. Other than that, the government did decide, in the light of the relevant National Audit Office report and additional research that the government itself requested, to go ahead with the arrangements that the Treasurer announced, I think, in the last week or so.

Senator CHRIS EVANS—I take it that means that what looks, on first blush, in the books as a significant increase in Defence expenditure in the last couple of years, because of the fall in the Australian dollar, is in fact not so. It is a no win, no loss situation?

Dr Hawke—That is right. It maintains our purchasing parity, so Defence has not lost as a result of those exchanges. I do not fully understand how they strike the benchmark prices. But I did offer to the former Secretary of the Treasury that, if he wanted to, we would be amenable to taking that risk on board in Defence at whatever the prevailing currency rate was at the time, which was about 50c, I think. He was not amenable to that approach at that time, either.

Senator CHRIS EVANS—You can only try, Dr Hawke. From my figures, Mr Roach, it looks like, from 2001-02 to 2002-03, almost \$740 million has been allocated to Defence for foreign exchange and price movements. Again, they are big dollars in the budget but in real terms it does not mean anything in terms of Defence purchasing?

Dr Hawke—It does mean something: it means that parity is maintained.

Senator CHRIS EVANS—But the \$740 million did not buy you \$740 million more outputs; it maintained the purchase of outputs.

Dr Hawke—But it is a real hit on the budget.

Senator CHRIS EVANS—I am trying to understand what it means in terms of what we get in Defence.

Mr Roach—Were the figures you mentioned the figures over two years?

Senator CHRIS EVANS—Yes.

Mr Roach—This year the exchange is \$351 million.

Senator CHRIS EVANS—Over the two years it is \$740 million, but that is a no win, no lose basis and zero dollar gain for Defence. Is that right?

Dr Hawke—It could come back the other way in the second year too, because of the appreciation of the Australian dollar.

Senator CHRIS EVANS—I am just trying to establish that it does not actually have any impact on Defence at all.

Dr Hawke—It maintains our real purchasing power.

Senator CHRIS EVANS—Are you telling me you cannot give me the GDP deflator because it is a classified figure?

Mr Roach—I would like to check. The forecasts, as you know, are sensitive but I will check the 2002-03 figure to see whether I can provide it for you.

Senator CHRIS EVANS—Let me know whether that is a state secret or not. That indexation factor represents the amount of funding effectively needed to maintain the value of the Defence budget. Is that fair?

Mr Roach—That and the exchange mechanism are the mechanisms that have been agreed.

Senator CHRIS EVANS—They have always been projected into the Defence budget?

Dr Hawke—We did not always have the present price arrangement. That price arrangement was settled in the context of the white paper by a government decision.

Senator CHRIS EVANS—Was it?

Dr Hawke—Prior to that, we had a basket of price variations which were more Defence specific, and there was some work done about whether we should go with the one deflator or whether we would continue with the basket approach. It was agreed that we would go with the present one. That was announced in the white paper, I think.

Senator CHRIS EVANS—Is it fair to say that they are unrelated in the sense that you always had an indexation measure, you have just changed the measure?

Dr Hawke—Yes. We have changed by agreement with Treasury.

Senator CHRIS EVANS—But the methodology for Defence is the same; you are just using a different—

Dr Hawke—Yes, and that was decided by government.

Senator CHRIS EVANS—Is it fair to say that that is unrelated to the white paper in the sense—

Dr Hawke—No, it was a specific decision as part of the white paper, when price and exchange arrangements were discussed.

Senator CHRIS EVANS—I am just trying to understand the connection with the white paper process.

Dr Hawke—If I am right, it is the non-farm GDP deflator. That was decided as a replacement for the previous mechanism which relied on a whole basket of price changes,

some of which were quite specific to Defence. We will use that as the means of adjusting defence for future price variations.

Senator CHRIS EVANS—I appreciate that; you keep putting it in the context of the white paper. I do not understand.

Dr Hawke—The decision was made as part of the white paper.

Senator CHRIS EVANS—Why is that?

Dr Hawke—Because we looked at price and exchange arrangements when looking at the financial underpinning of the white paper.

Senator CHRIS EVANS—But it could have been a separate decision, because it affected the whole of the Defence budget not just the white paper.

Dr Hawke—That is right. It is just that it did happen in that context because underpinning the white paper, of course, is the finance to give effect to what the government wants to put in place.

Senator CHRIS EVANS—Mr Roach, what is the impact of that deflator on the budget from 2001-02 to 2002-03?

Mr Roach—In terms of the change from the additional estimates to budget 2002-03, the changes in the parameters have resulted in us handing back \$55 million as the papers show, but that is on top of a parameter we got at additional estimates for our forward estimates, which was higher. So effectively the parameter is just decorative.

Senator CHRIS EVANS—What is the indexation impact between the two years?

Mr Roach—From budget to budget as opposed to additional estimates?

Senator CHRIS EVANS—Yes.

Mr Roach—I would have to find that for you.

CHAIR—I think we will take a short break.

Proceedings suspended from 10.29 a.m. to 10.47 a.m.

Senator CALVERT—Minister, I was reading an article the other day about the UK structure where the government, industry and the department are working together to improve export earnings for their defence industries. Do we have anything similar to that or are we thinking about having a program that rewards our export oriented companies that produce defence equipment here in Australia?

Senator Hill—We have similar processes. We have a number of people here who can give you the distinctions between our processes and the British procurement processes.

Mr Roche—We have an Industry Division responsible for industry policy and for working with Australian industry to ensure that they get an opportunity to tender for defence business both in Australia and overseas. We support Australian industry through facilitating visits by overseas defence manufacturers who are looking for Australian suppliers either for general reasons or as part of an acquisition which requires some Australian industry involvement. We also lead and facilitate industry delegations to the various trade shows which provide the opportunity for them to display their wares. We try also to publicise the good news stories that there are from Australian industry that can get involved in defence industry.

Senator CALVERT—But you do not have a program as in the UK where the government and the department of industry get together to see where they could improve export earnings

or improve government-industry relations? Do you have a structured committee that does that?

Mr Roche—We have a number of forums. The highest level forum is the Defence Industry Advisory Council, and there are forums underneath that that do involve pretty much constant discussion between Defence and industry both in relation to the way that we work with industry in Australia—that is the DMO—and in relation to export opportunities. The trick of it is in making sure we identify all of the people who, potentially, can take part in this because some of it is not very obvious. It is down there at the SME level.

Senator CALVERT—What is this Defence Industry Advisory Council? Could you tell me a little bit about it?

Mr Roche—The Defence Industry Advisory Council has a membership of about a dozen representatives from major defence companies operating in Australia and some representatives from the groups that represent SMEs. Chaired by the minister, it canvasses a range of issues to do with industry policy and the relationship between the DMO and the Australian industry.

Senator CALVERT—Do we have any programs where we reward our export companies for excellence in Defence industry like the industry awards that we attend every year for exports and whatever? Are you placing any priority on trying to promote export sales and that type of thing in Defence? It is in Australia's interests, surely, to have more defence work being produced here in Australia, because if you have that you obviously reduce the cost of our own budget.

Mr Roche—I have just been reminded I omitted to mention the defence exporters council, which is specifically aimed at exports and trade shows. That is a departmental level council. It includes industry and also has state government representation on it. We do not have a formal awards scheme as such, but we do, as I said earlier, give publicity to those people who are doing it well. We certainly try and spread through all of these forums that we attend examples of successful Australian participation in defence industry. In some respects, that has been helped by the tack that we are taking on defence industry policy, announced by the government last year and again in their election commitments, and that involves greater involvement in international supply chains rather than focusing on simply assembling something in Australia because we can do it here—looking at a more sustainable involvement by industry with a market that has a significantly greater volume. I suppose I could explain it by saying that I think I would rather make the tail rotors for every Black Hawk worldwide than assemble 36 Black Hawks in Australia. We are seeing evidence that that sort of thing can be done. There are a number of contractors working on the AEW&C project. There is one contractor, for example, that is providing wiring looms for the AEW&C project in Melbourne, and I think there is a pretty fair chance that they will get follow-on work for other AEW&C aircraft to be sold to Turkey and other countries.

Senator CALVERT—What prompted my questioning was a visit our defence committee had to Edinburgh the other week. We were shown some of the very productive work being done there for other agencies overseas and testing their equipment. Whilst it is not a big thing, if we are doing that in other areas, why are we not taking advantage of the skills we have and perhaps producing income that we normally would not have?

Mr Roche—We certainly are doing what we can. The British, with their Defence Export Services Organisation, are doing pretty well and we have had a good, hard look at how they

do it and are prepared to borrow whatever ideas we can. That is an organisation of some 600 people, I think, and it is significantly sponsored by industry as well as by government. We have always had some difficulty in Australia getting an industry-side contribution to that, possibly reflecting the number of quite small enterprises that are involved on the Australian side.

Senator CALVERT—It would be fair to say that, in purchasing defence equipment that is reasonably new and is cutting edge technology, perhaps we are doing a bit of groundwork for other countries. With the C130J Hercules, I believe the RAF are getting some expertise from our Air Force on the teething problems they have had with those—is that right?

Mr Roche—It is certainly the case that DSTO in particular has a very good reputation overseas for a lot of its work, particularly in relation to fatigue. As I understand it, it has been doing work on vibration in the C130Js. I suppose they would be right up there in whatever is happening worldwide in F18 fatigue work.

Senator CALVERT—That is what I am getting to. We are dealing with that problem. That is just an example. Do Lockheed come out here and have input? Do they actually get a benefit from Australia's expertise or do they make any allowances on the cost of these particular aircraft because you have had to iron out a few of the problems?

Mr Roche—I guess that all of these companies come to Australia when they have to—when they have to achieve a certain level of Australian industry involvement in a project. We are trying to persuade them that the work that can be done here is of a quality and at a price that is attractive to them worldwide. Certainly we are seeing some initial positive reactions from companies in relation to software development, where Australian quality and price is right up there. Lockheed were out just recently on a mission to do with their interest in the Air 6000 project—the replacement of the FA18s and the F111s. They went to most capital cities. I think they had individual discussions with some 48 companies, covering an enormous range of capabilities from cabling right through to software systems and so on. I know that Rafael have done a similar thing and BAe are looking at it. These companies are coming out and they are aware of what is out here.

You would be aware of the work that is being done at an Adelaide facility, where GM Defence are now manufacturing turrets for ASLAVs worldwide. Rather than simply assembling ASLAVs for Australia only, we are now moving to build turrets for them worldwide. That is the sort of work we are trying to get.

Senator CALVERT—I am sure you would be very much aware of Lockheed's record over some time now: they have had more than 33 cases covering overcharges in government contracts and I think they have been fined over \$145 million for bad practice. I am sure you would take all that into account when you are looking at the F35 strike fighter, wouldn't you?

Mr Roche—Indeed.

Dr Hawke—I will add one point to Senator Calvert's line of questioning. The department of industry is doing some sectoral work, which we are engaged in. The first sector they are looking at is aviation. Defence officials and defence industry people have been involved in that. I think I am right in saying that Mr Ken Peacock from Boeing Australia is the chairman of that committee, but the industry department is pursuing through that sectoral approach the sorts of issues that you raised.

Senator CALVERT—It is commonsense to make the best of what we are doing.

Dr Hawke—Yes, and they are involving us in that process.

Senator FAULKNER—Dr Hawke, I would like to follow up a matter that I raised at the PM&C estimates. I do not know whether or not you are aware of it. It relates to the access by former Defence Minister Reith to cabinet and other documents from the department since he left office. Could you indicate to the committee whether ex-Minister Reith has had access to any Defence documentation?

Dr Hawke—I am not aware that he has sought or had access, but I will get you a definitive answer on that.

Senator FAULKNER—I have a number of questions to follow up on this. One issue was raised at the Department of the Prime Minister and Cabinet estimates about whether that department had had any inquiries from Defence about access for Mr Reith. Ms Belcher from PM&C thought there may have been and took that on notice.

Dr Hawke—Ross Baker, who is the head of our ministerial and parliamentary area, has just told me that we have no record of any requests from, or access by, Mr Reith.

Senator FAULKNER—So I can be satisfied that there has been no access by Mr Reith to any departmental records?

Dr Hawke—Subject to me correcting the record in the next day or so, yes.

Senator FAULKNER—Are you aware whether Defence sought advice from the Department of the Prime Minister and Cabinet on guidelines?

Dr Hawke—Which guidelines?

Senator FAULKNER—Guidelines in relation to access by former ministers to such material.

Dr Hawke—No, I am not aware of that. The division head who would most likely be concerned, Mark Cunliffe, is not here, so I will check with him.

Senator FAULKNER—What about access to the former minister's email account?

Senator Hill—What about it?

Senator FAULKNER—I am asking specifically about the former minister's email account.

Senator Hill—Has the former minister sought access to the email account?

Senator FAULKNER—Has there been any access and what are the arrangements? As you know, Senator Hill, this is a similar issue to one I pursued in the estimates of the Department of the Prime Minister and Cabinet. I thought that might have meant that someone would be forewarned, because it was suggested that it might be progressed at this committee. Being diligent, that is exactly what I am doing.

Senator Hill—I do not think I suggested that. The question is whether Mr Reith has sought access and, if so, whether it has been given. A sort of supplementary question is whether there are any guidelines.

Senator FAULKNER—If you are drawing a distinction between seeking access and having access, I will ask the question in a slightly different way. Has former Minister Reith had access to such material?

Mr Hannan—No. He has neither had nor to our knowledge sought access.

Senator FAULKNER—Does a former minister's email account close as soon as he leaves office?

Mr Hannan—Yes.

Senator FAULKNER—Is that what happened in this instance?

Mr Hannan—That is correct.

Senator FAULKNER—Could you give me the date, please, when that occurred?

Mr Hannan—I do not have it with me, but I will get back to you on the exact date.

Senator FAULKNER—Dr Hawke, if one of your officials could flag with the committee secretariat when you come back about that, I would appreciate it so that I can, at a minimum, listen in to the responses.

Dr Hawke—Yes, certainly.

Senator FAULKNER—I would imagine you ought to be able to do that within the next day or so?

Dr Hawke—Yes.

Senator FAULKNER—Thank you very much for that—I will await those answers. Thank you for your cooperation on those matters. A second matter I would like to raise was also touched on in the examination of the Prime Minister and Cabinet portfolio. It goes to the question of the \$20 million to the PNG defence force, the details of which were finalised in a meeting on 8 October last year. Dr Hawke, I wonder if you could give me some background, just briefly, because I know that you were personally involved in this—

Dr Hawke—I was personally involved.

Senator FAULKNER—Yes. I said I wonder if you could give me some background because I know that you were personally involved in this.

Dr Hawke—I thought you said I was not, I am sorry.

Senator FAULKNER—No, I know that you were personally involved in it and, in fact, I know that you were at the meeting on the 8th because that evidence was extracted at estimates hearings last week. Can you just indicate to the committee very broadly—I do not think we need a thesis on this, just a broad brush indication—what the background to the meeting on the 8th was and the planning that had gone into that in the lead-up to those matters being finalised on that date?

Dr Hawke—My recollection of this is that there was a discussion between Prime Minister Morauta and Prime Minister Howard quite some time ago which led to the formation of the Eminent Persons Group under the sponsorship, I think, of the Commonwealth. This group then did some work on PNG Defence Force reform. Before that submission could be decided by the Papua New Guinea government, I think a copy of it was leaked and it did not receive favourable reception in PNG. This led the PNG government to commission its own 'home-grown review', I think they called it, of the Papua New Guinea Defence Force and reform issues.

On the back of that, I suspect there were discussions between the two Prime Ministers which then led the secretary of the Chief Minister's Department to come to Australia for discussions with Mr Moore-Wilton, me and the Australian High Commissioner, Mr Nick Warner. I think, but I am not absolutely sure, that a division head from Prime Minister's,

Michael Potts, was also present at the meeting, which occurred in Sydney on the morning of 8 October. The discussion essentially ranged from a draw-down in the numbers in the PNG Defence Force, the numbers of those people, a time frame for it, the way in which the accountability arrangements would be established to the funding.

There had already been some discussion at government level which had agreed to a sum of money that could be made available to Papua New Guinea if we were able to reach agreement on the reform package. That agreement was reached on the morning of 8 October. My recollection is that the high commissioner may have written a letter which confirmed the agreement, and that led to a sum of \$20 million being provided for what was quite clearly regarded as the first tranche of PNG defence reform.

Senator FAULKNER—When was the copy you spoke of leaked?

Dr Hawke—The original Eminent Persons Group? I would have to go back and find that out. My guess is six months or more—it was certainly last year. But I could get you a date for that.

Senator FAULKNER—Was there a suggestion that that was a leak from Defence?

Dr Hawke—No, this happened in PNG; this was not in Australia. I do not know—I am not even sure they would know.

Senator FAULKNER—That is what led, in your view, to the home-grown review approach being adopted by PNG?

Dr Hawke—I am absolutely convinced that was the connection.

Senator FAULKNER—Do you know when the meeting date of 8 October was determined?

Dr Hawke—I don't actually. My guess is some time the week before. The arrangements were made to have that meeting some time the week before, from memory. I can check my records.

Senator FAULKNER—I would appreciate it if you would. Did you see the meeting as in any sense out of the ordinary?

Dr Hawke—I did not see it as out of the ordinary, other than that, if this was going to be done, my view was it would need to be done by this government before the issue of the writs and, if that had not occurred, there would need to be discussion between probably the Prime Minister with the Leader of the Opposition about the issue. But the matter was finalised quite clearly on the morning of Monday, 8 October to the satisfaction of both sides.

Senator FAULKNER—When you talk about the issue of the writs, it is after the issue of the writs—well after the issue of the writs.

Dr Hawke—Sorry. You are right.

Senator FAULKNER—Are you making a point about the caretaker conventions?

Dr Hawke—Yes. If it had not been concluded by I think it was around lunchtime that day, when the caretaker conventions came into effect, then there would have needed to have been some discussion—

Senator FAULKNER—Did you seek advice on that issue?

Dr Hawke—No.

Senator FAULKNER—You just knew that was the case?

Dr Hawke—It was in my mind, yes.

Senator FAULKNER—Why was it in your mind?

Dr Hawke—Because it was going to come into effect at lunchtime that day and we had been preparing to issue—we may have already issued within the department—the guidelines for the caretaker period. That is why it was uppermost in my mind.

Senator FAULKNER—This I appreciate is not directly a Defence responsibility in a sense—the high commissioner does not work for you, does he?

Dr Hawke—He certainly does not.

Senator Hill—He is very supportive of us.

Senator FAULKNER—I am not suggesting he is not.

Senator Hill—And we are supportive of him. I do not want it to be misinterpreted.

Dr Hawke—He clearly belongs to the Department of Foreign Affairs and Trade and acts as an agent for the total Commonwealth government including Defence, so our defence attache up there clearly works for him.

Senator FAULKNER—Are you saying that in the high commissioner's letter the arrangements about the detail of expenditure and other arrangements about the \$20 million was contained within—

Dr Hawke—My recollection is yes, that was the case.

Senator FAULKNER—So it is a fairly important piece of correspondence from Defence's point of view, isn't it?

Dr Hawke—Yes, we would have a copy of it.

Senator FAULKNER—You would have a copy of it?

Dr Hawke—Yes. I had understood what was going to be in it and agreed with it.

Senator FAULKNER—Give me that background. Could you explain to me how that happened?

Dr Hawke—It was principally to do with paying out allowances and redundancies for a significant number of PNGDF personnel. But there are a number of—and I cannot recall them now—what Secretary Igara called 'show stoppers' and we agreed that some of the funding could be used for those purposes. I cannot bring that to mind, but they were small amounts of money in the general context of the \$20 million.

Senator FAULKNER—When were these show stoppers developed?

Dr Hawke—That was Secretary Igara's view. He was acting on behalf of the Papua New Guinea government, putting that position to us. He raised them on the morning.

Senator FAULKNER—So when did you give approval to the high commissioner's letter?

Dr Hawke—That morning. We discussed and agreed the thing between the parties that morning.

Senator FAULKNER—So when did you first see the high commissioner's letter?

Dr Hawke—I think I saw it that morning.

Senator FAULKNER—Did you take any notes of this meeting?

Dr Hawke—I do not recall; I would have to check.

Senator FAULKNER—Was there a minute-taker or note-taker at the meeting?

Dr Hawke—Mr Potts from the Prime Minister's department I think was there.

Senator FAULKNER—He may have been there. I could turn up who was there, but I was told—

Dr Hawke—If Potts was not there—I am a bit unclear about that—Nick Warner would have taken the record of what happened and that would be reflected in the letter that he provided.

Senator FAULKNER—Fair enough, but you would accept it is very important that a record was kept?

Dr Hawke—My recollection is that there was. It is reflected in the letter.

Senator FAULKNER—I asked Mr Potts who was the minute-taker or the note-taker at the meeting and Mr Potts said there was no formal record, and I said—

Dr Hawke—No formal record?

Senator FAULKNER—Yes. He said no-one did take any notes.

Dr Hawke—The formal record is contained in the high commissioner's letter, which confirmed the agreement and arrangements.

Senator FAULKNER—Just a moment ago you were telling me that there was note-taking at the meeting.

Dr Hawke—Warner was taking notes; that is correct. But did he type those up and produce a formal record? I do not think so. He drew on those notes to provide the letter of arrangement and agreement between the two governments.

Senator FAULKNER—Was there a draft of the letter when you came to the meeting?

Dr Hawke—No.

Senator FAULKNER—The letter was created at the meeting?

Dr Hawke—Yes.

Senator FAULKNER—Who typed it up?

Dr Hawke—I don't know that.

Senator FAULKNER—It is typed up while the meeting is going on, is it?

Dr Hawke—No, at the end of the meeting.

Senator FAULKNER—Does this \$20 million come from the Defence budget?

Dr Hawke—I am actually not sure about that, because there was an argument about supplementation relating to this. I will have to find that out.

Senator FAULKNER—Surely someone there knows whether the \$20 million came from the Defence budget. It is not peanuts.

Dr Hawke—That is why I do not want to mislead you.

Senator FAULKNER—And I do not want you to mislead me, but I do think that if I ask you a question whether the \$20 million came from the Defence budget—

Dr Hawke—We will know; we will get an answer for it.

Senator FAULKNER—Could we get that answer now? The answer ‘I don’t know’ to that question is not acceptable.

Dr Hawke—I am saying I don’t know, but we will find out and provide it. The answer is that it came from the Defence budget. It would have come from the Defence Cooperation Program.

Senator FAULKNER—Are we certain about that?

Dr Hawke—It is in the additional estimates book at page 8. At page 8 it says:

- assistance for the reform of the Papua New Guinea Defence Force (\$20m).

Senator CHRIS EVANS—That is certainly what you told me at the last estimates.

Senator Hill—It is my understanding too, that we were supplemented \$20 million and that it was funded through an increase in the Defence Cooperation Program with PNG.

Dr Hawke—And it is also reflected at page 12, where it says:

The Government has provided \$20m in assistance to the commencement of a Papua New Guinea Defence Rebuilding Program.

... ..

Defence has met this new initiative through internal reprioritisation of spending.

Senator FAULKNER—How much of this \$20 million is going to redundancies for the PNG—

Dr Hawke—We are not finished. It is a current year activity; it is happening now.

Senator FAULKNER—So what is the plan?

Dr Hawke—Quite a significant number of those people are to go out by 30 June. There was a review of this just recently—and, again, I will have to get you the details that were in an exchange of letters between the chief secretary and the high commissioner. It is of the order of 1,100 people, from memory.

Senator FAULKNER—Yes.

Senator Hill—As I understand it, money was put in a trust account administered by Deloitte, and rules were agreed upon to cover the circumstances in which the trust account could be drawn down. The predominant draw-down is to pay benefits to facilitate a reduction in the size of the PNG Defence Force. That is part complete, but I do not have the figures on the full number who have been paid out.

Senator FAULKNER—That is helpful about the process, Senator Hill, but I was asking Dr Hawke this question: what proportion of the \$20 million either has gone for PNGDF redundancies or is planned to go for PNGDF redundancies?

Dr Hawke—This would move every day.

Senator FAULKNER—Give us a ballpark figure. It may move every day, but is it \$10 million; is it \$15 million?

Dr Hawke—It is not being done here; it is being done in PNG.

Senator FAULKNER—I know that.

Dr Hawke—We will have to ask PNG to find the answer to your question.

Senator FAULKNER—But it is the main proportion of it, isn't it, that is going on the redundancy package?

Senator Hill—Yes.

Dr Hawke—Absolutely.

Senator FAULKNER—Can you give me an indication, at least in broad measure, of the proportion?

Dr Hawke—I will get the figure for you.

Senator FAULKNER—How appropriate do you think it is, Dr Hawke, for the Defence cooperation budget to be used for redundancies?

Senator Hill—It is not for Dr Hawke to say. In the government's view, this is an entirely appropriate contribution.

Senator FAULKNER—All right. If the government believes it is—

Senator Hill—The PNG Defence Force is an institution that is critical to the stability of PNG. As we all know, there have been significant problems in that regard in recent years. As a result of detailed analysis, the government has decided that one way to contribute to a PNG Defence Force that can be relevant and capable according to the original plan would be to reduce it in size. It is an aged force in terms of military. That is inhibiting younger, better educated people from getting the chance to join and to contribute. Therefore, for Australia to assist PNG in restructuring that force so that it can better contribute to PNG's national goals seems, in the opinion of the government, a perfectly proper thing to do and a very sensible investment.

Senator FAULKNER—When was the priority for redundancies established?

Dr Hawke—That was a key part of the Eminent Persons Group report and, in turn, it became part of the PNG's home-grown solution to PNGDF reform.

Senator FAULKNER—Yes, their home-grown solution. Senator Hill has said that that is the government's view and policy. That is fair enough, if he can properly outline that. Historically, has the Defence cooperation budget ever been used for redundancies?

Dr Hawke—I do not know the answer to that, either.

Senator FAULKNER—There must be someone here who has a bit of an idea?

Dr Hawke—We will find out, but with 100 years in the organisation it is not an easy answer.

Senator CHRIS EVANS—I do not think you have been there 100 years, have you?

Dr Hawke—No, I have not.

Senator Hill—It certainly has not been a principal part of the cooperation program but there may be instances in the past where it has occurred.

Senator CHRIS EVANS—Was this policy reviewed after there was some rioting—as I recall—by some of the affected troops?

Dr Hawke—The rioting was associated with the Eminent Persons Group report.

Senator CHRIS EVANS—No, more recently than that. Wasn't it early this year that there was further dissatisfaction with the propositions which we are funding and some arms went

missing and there was some disobedience by soldiers? Has there been a review of the proposal as a result of that sort of activity?

Senator Hill—In our view the events that occurred this year only emphasise how important this project is.

Senator CHRIS EVANS—So it is part of the bargaining process?

Senator Hill—No, it is not part of it but it reflects an ongoing problem within the PNG Defence Force which we believe can be at least in part addressed through retiring a considerable number of people. PNG is unable to afford to do that itself and Australia is therefore giving it some assistance.

Senator CHRIS EVANS—Is there the equivalent of an industrial negotiation going on about rates and packages? Is that the process?

Senator Hill—There certainly has been an issue of the quantum of the payouts. Australia is contributing only part of it, and part is to be paid by the PNG government. The quarrel at Moem Barracks did not relate to the size of packages but certainly the quarrel illustrated unsatisfactory behaviour within the PNG Defence Force which if not addressed would lead to more serious problems down the track.

Senator FAULKNER—But the prioritisation of these funds—the \$20 million—actually occurs on the morning of 8 October. Is that right, Dr Hawke? Is that when you get the first detail of it?

Dr Hawke—Yes, that is when we agreed it.

Senator FAULKNER—They are actually whistled up on the day of the meeting? You do not know anything about it beforehand?

Dr Hawke—I knew we were meeting with them to discuss—

Senator FAULKNER—Do you know when you knew you were meeting?

Dr Hawke—Yes, I do now. It was 4 October.

Senator FAULKNER—How was that communicated to you?

Dr Hawke—It was a message that there would be a meeting in Sydney with Robert Igara on that morning.

Senator FAULKNER—Who did that message come from?

Dr Hawke—That came to me from Ken Baxter, who was working with the Chief Secretary, Mr Igara.

Senator FAULKNER—Did that particular note tell you what matters would be discussed at the meeting?

Dr Hawke—It said that it was about ‘momentum in reducing the size of the Papua New Guinea Defence Force and achieving the reforms’, but in a different way from what was envisaged under the eminent persons group report.

Senator FAULKNER—What did it say? Are you reading the notice of the meeting? Is there any reason why you could not table that?

Dr Hawke—I would be reluctant to because it involves the PNG government. I would be happy to seek their agreement to doing so.

Senator FAULKNER—This is a parliamentary committee of the Commonwealth of Australia.

Dr Hawke—Absolutely. I am not sure that we would want to reveal a position of another government here, which may not be—

Senator FAULKNER—You might tell me what is on the agenda, anyway. You can take that on notice if you like, but tell me what was on the agenda that you received.

Dr Hawke—I will read it again: ‘reducing the size of the Papua New Guinea Defence Force and achieving the reforms’.

Senator FAULKNER—Was there anything else on the agenda for that meeting?

Dr Hawke—No.

Senator FAULKNER—That is the one item?

Dr Hawke—Yes, that was the item.

Senator FAULKNER—‘Reducing expenditure’—and?

Dr Hawke—‘Reducing the size of the Papua New Guinea Defence Force—

Senator FAULKNER—Sorry, ‘reducing the size’—

Dr Hawke—and achieving the reforms’—that is, the reforms that the PNG government wanted to pursue following the Eminent Persons Group report and their view about what they wanted to pursue.

Senator FAULKNER—Of course, this is a meeting about the expenditure of, in total, \$54 million worth of taxpayers’—

Dr Hawke—Not that I am aware of. The meeting I was at was about \$20 million for the PNG Defence Force—

Senator FAULKNER—But you left before the end of the meeting, didn’t you?

Dr Hawke—Well, I finished at this meeting. I am not sure I follow you, Senator.

Senator FAULKNER—When did you leave the meeting?

Dr Hawke—I do not actually recall.

Senator FAULKNER—Do you remember when the meeting ended?

Dr Hawke—I think it was roughly around 11.30 or something like that.

Senator FAULKNER—That is lucky.

Senator Hill—Dr Hawke has spoken to the agenda item that he was certainly involved in.

Senator FAULKNER—Yes, I know.

Senator Hill—If you are arguing that there were other agenda items that he was not involved in, it hardly seems to be appropriate to be asking him about them.

Senator FAULKNER—Senator Hill, even you would have to accept that what occurs on this morning before the caretaker conventions kick in at 12 o’clock is crucial. You were there until 11.30, Dr Hawke, were you?

Dr Hawke—I think the meeting finished at around 11.30, from my memory. I will have to go back and check whether I have a record of that, but my recollection is that it finished at around that time.

Senator FAULKNER—We have heard evidence that in the broad supports that. Tell me if there were any other agenda items apart from reducing the PNGDF and achieving those reforms. Were there any other agenda items?

Senator Hill—I thought he answered that question.

Dr Hawke—There may have been, but I was only involved in this one, so I do not think I can answer that question.

Senator FAULKNER—When you say the meeting ended, what happened? Did everyone just get up and leave?

Dr Hawke—We sat around having a chat and, yes, I think we left.

Senator FAULKNER—When did the discussion turn to asylum seekers?

Dr Hawke—At the completion of our arrangements on the PNGDF reform issues. But that has nothing to do with me.

Senator FAULKNER—That is what I am asking: were you present for those?

Dr Hawke—I was present when the issue was raised.

Senator FAULKNER—Well, that is another item on the agenda.

Dr Hawke—No, it was not on my agenda. I was not part of that meeting and it had nothing to do with me.

Senator FAULKNER—But you were present.

Dr Hawke—I was present when the issue was raised.

Senator FAULKNER—Was it raised before the end of the meeting or after?

Dr Hawke—It was raised at the end of the meeting on PNGDF reform. We completed that meeting and then there were separate discussions between Mr Moore-Wilton and Mr Igara, from my memory.

Senator FAULKNER—But you were present while they took place?

Dr Hawke—I was present when they started. I think I was sort of in the sidelines while they were discussing that matter.

Senator FAULKNER—You were there having a cup of coffee a minute ago.

Dr Hawke—I did not say I was having a cup of coffee.

Senator FAULKNER—You said you were still there.

Dr Hawke—I was still there, but it was nothing to do with—

Senator FAULKNER—You are either still there or you are not still there.

Dr Hawke—I was taking no interest or part in that discussion.

Senator Hill—You have had to say that several times. You should not have to say that several times.

Senator FAULKNER—We have established that Dr Hawke was there. Can I establish from Dr Hawke at what point the meeting turned its attention to the issue of asylum seekers?

Dr Hawke—I do not remember. All I remember is that we had completed the meeting on PNGDF reform before that discussion occurred. The two were unrelated.

Senator FAULKNER—Really! Was it the same meeting and a brand new agenda item, or was it two separate meetings?

Dr Hawke—I do not think there was an agenda item.

Senator FAULKNER—No, I do not either. I am sure that \$34 million was spent without an agenda item existing; we have established that.

Dr Hawke—It arose after completion of this meeting, then in discussion between Mr Moore-Wilton and Secretary Igara.

Senator FAULKNER—Who raised it?

Dr Hawke—I do not recall that. Frankly, I was not interested; it had nothing to do with me.

Senator Hill—Again, you have said that several times. Dr Hawke's evidence is that he went there to deal with a particular matter and he dealt with that particular matter. If other parties went there to deal with another matter, so be it. But that is not Dr Hawke's concern. That is the subject you sought to pursue in another committee where it was actually more appropriate to pursue it.

Senator FAULKNER—Senator Hill, Dr Hawke was there and, because Dr Hawke was there, I thought he may well be able to assist us, and I think he has been able to assist somewhat in this. I am just trying to nail down when this took place. How can I be confident that this all occurred before midday on the 8th, which you would accept is very important, wouldn't you, Dr Hawke?

Dr Hawke—I do, and I said so in the select committee. This issue arose in the select committee, as you may recall.

Senator FAULKNER—Yes. So I am asking what time you believe the agenda item on the PNG Defence Force ended and the discussion on asylum seekers started.

Dr Hawke—My recollection is that the whole meeting was completed by about half past 11—the whole thing.

Senator FAULKNER—But you were there, you see.

Dr Hawke—Yes, but I still do not follow you. My part in this meeting was completed before then.

Senator FAULKNER—Before when?

Dr Hawke—Before half past 11.

Senator FAULKNER—And when do you think the whole meeting completed?

Dr Hawke—Around half past 11.

Senator FAULKNER—So how long did the discussion on asylum seekers take?

Dr Hawke—I do not think it took very long at all.

Senator FAULKNER—How long?

Dr Hawke—I do not know, about 15 minutes.

Senator FAULKNER—And you did not say anything in that part of the meeting?

Dr Hawke—No, it was none of my business.

Senator FAULKNER—Do you recall who was present for that part of the meeting?

Dr Hawke—It would have been the same people, I think.

Senator FAULKNER—Again, you were there; I was not there.

Dr Hawke—I did not take a record of it. Frankly, it was not of interest to me. I know who was there for the part that I was directly involved in.

Senator FAULKNER—For the whole time you were there and what you were listening to—which was the whole of the meeting on both issues—was the question of the application of the caretaker conventions mentioned?

Dr Hawke—No, not to my recollection.

Senator FAULKNER—Thank you.

Dr Hawke—I can answer one other question you raised earlier—that is, we have no record of any Defence approach to PM&C with regard to guidelines for the handling of requests by former ministers for access to documents.

Senator FAULKNER—But, in relation to the matters we have been discussing, were there discussions with the government division of PM&C on the application of the caretaker conventions more generally?

Senator Hill—In relation to what?

Dr Hawke—In relation to this issue?

Senator FAULKNER—Yes.

Dr Hawke—No.

Senator Hill—What is this issue?

Dr Hawke—You are talking about PNGDF reform and the separate conversation?

Senator FAULKNER—Yes.

Dr Hawke—No.

Senator FAULKNER—Why not? You were confident that that was not a matter—

Dr Hawke—Confident and conscious that, if this arrangement was going to be reached in that way, it would have to be done by then and, if it was not, there would need to be discussion with the leader or between government ministers.

Senator FAULKNER—What about the other issue of asylum seekers?

Dr Hawke—Again, I will tell you that is not my business. But clearly the same issue would apply.

Senator FAULKNER—What do you mean by ‘the same issue would apply’?

Senator Hill—The caretaker provisions apply across the board.

Dr Hawke—I have a very clear recollection that that arrangement was agreed at or around the same time. And PM&C would probably be able to confirm that.

Senator FAULKNER—What was the approval process then for the \$20 million from the Defence Cooperation Program?

Dr Hawke—It was considered by a cabinet meeting and there was an extant cabinet decision which authorised the expenditure of that money, prior to the meeting.

Senator FAULKNER—Can you tell me the time frame for that?

Dr Hawke—When the sum was agreed? I can find out for you.

Senator FAULKNER—I am sorry—‘When the sum was agreed’?

Dr Hawke—Are you after when the government considered it and decided?

Senator FAULKNER—I am just wondering what the approval process was for the diversion of these funds from the Defence Cooperation Program.

Dr Hawke—There was a discussion in the National Security Committee, a decision was taken and then the amendments were made at additional estimates time.

Senator FAULKNER—When was cabinet approval given?

Dr Hawke—I will have to find that out for you. But it was some little time before the meeting.

Senator FAULKNER—We can explore that a little bit later, Dr Hawke.

Dr Hawke—It should not take long to get you the answer.

Senator FAULKNER—If it will not take time, that will be good. I will come back to it in a few moments.

Senator CHRIS EVANS—We will go back to inflation and such things. Mr Roach, were you able to get me the indexed increase between the Defence budget 2001-02 and 2002-03?

Mr Roach—I got some figures over the break. I can give them to you now, but I would like to confirm them and give them to you in writing. The total price increase in 2001-02 is \$231 million and the total increase in price in 2002-03 is \$293 million.

Senator CHRIS EVANS—That is a bit higher than I thought. That is the total price increase in the Defence budget driven by the GDP inflator index. Is that right?

Mr Roach—Yes.

Senator CHRIS EVANS—And will you have to kill me if you told me—

Mr Roach—No. Let us say around two per cent.

Senator CHRIS EVANS—Does that mean that it is two per cent or—

Mr Roach—It means that the figure published in Budget Paper No. 1 is two per cent.

Senator CHRIS EVANS—About what about for the out years, Mr Roach?

Mr Roach—I would not wish to disclose forecasts.

Senator CHRIS EVANS—Two per cent looks to be a fairly good guide for the out years. Are you saying that you cannot confirm or deny—

Mr Roach—I am not able to disclose the Commonwealth’s forecasts for these things, but if you look at our budget you can see that it increases by something like that.

Senator CHRIS EVANS—If we are looking from last year’s budget to next year’s budget, \$293 million of the increase is driven by that inflation figure.

Mr Roach—Along with all the other effects that are built into the budget.

Senator CHRIS EVANS—As you are aware, there is quite an increase in cash reserves being held by Defence over the next few years. I have seen a couple of public explanations about being more liquid, but it is quite a startling difference from the years when you are

holding around \$60 million to now holding about \$600 million. Could someone take me through the rationale for what has changed here?

Mr Bennett—In principle, it is to make sure that we have appropriate funds at hand to deal with our fortnightly spends and also to recognise our accrued liabilities so that we can deal with them as they arise.

Senator CHRIS EVANS—Does that mean that you have not had funds at hand before and that you have not been able to pay your bills?

Mr Bennett—No. At no stage have we not paid bills. It is a move to make sure we are better aligned to a reasonable practice.

Senator CHRIS EVANS—Could you be a bit more forthcoming? If you were moving from \$60 million to \$100 million, people would say that was understandable, but you are talking about tenfold increases in cash from a couple of years ago to next year. It is quite a significant change. You are talking about \$600 million held in cash. It is not a minor adjustment in your accounts, is it?

Mr Bennett—No; as the numbers stand, it is not a minor adjustment. What we are doing is certainly in line with good commercial practice. In a statement of accounting terms, the number as at last year was perhaps a bit lower than you would otherwise think, because some appropriations were provided for in the following year, but under the accounting treatments we could not recognise them.

Dr Hawke—My recollection is that it is the \$60 million that is more unusual. A series of circumstances led to us having very little cash on hand at that time.

Senator CHRIS EVANS—Looking back over previous years, it seems to have been a fairly consistent picture.

Dr Hawke—Do not forget there was a change from cash to accrual accounting at around that time.

Senator CHRIS EVANS—I never forget that. It is raised at every opportunity when something else is otherwise unexplainable.

Dr Hawke—It is a fundamentally different way of looking at the accounts.

Senator WEST—It is a great way of hiding anything from us.

Senator Hill—It is supposed to be to the contrary. It is supposed to give you a more useful picture.

Senator WEST—That is your story, Minister—stick to it.

Senator CHRIS EVANS—I do not understand why Defence needs \$600 million cash at hand.

Mr Bennett—In a lot of other departments there are administered expenses so that they can draw down, and the money is straight in and straight out. We are in a different sort of business from a lot of the other government departments.

Senator HOGG—So why is the \$600 million necessary? Give me an idea of the range of debts that you would want to pay off on a fortnightly basis with that amount of money.

Mr Bennett—There are employee expenses; there are contracts as they fall due. We typically have a variation of over \$500 million in a fortnight.

Senator CHRIS EVANS—But you have managed that in the past without these cash reserves.

Mr Bennett—Again, I think it is a matter of the timing of the appropriations and what we are expected to manage ourselves.

Senator HOGG—So your credit cards are not valued anymore out there?

Mr Bennett—I cannot comment on credit cards, in my time at Defence.

Senator CHRIS EVANS—This financial year you have budgeted for \$500 million cash at the end of the year. Sorry, that was not the right rate, but I see that the cash at hand is projected to increase over the next few years. Are you aiming to have \$600 million, \$700 million, \$800 million or \$1 billion in cash?

Mr Bennett—In the current framework, yes, we would expect to grow the cash at hand in line with the nature of the growing business.

Senator HOGG—Do you use a formula to work out the cash at hand that you need?

Mr Bennett—To predict the amount that we would like to have on hand?

Senator HOGG—Yes. Is there a certain percentage?

Mr Bennett—It is not a high percentage, but we are trying to align that to the short-term liquidity requirements and the accrued liabilities that we have. If you look at our percentage compared to BHP, we are probably lower. Perhaps we are closer aligned to a retailer like Coles Myer. We are not dissimilar to other government agencies that have a similar type of funding.

Senator HOGG—So the amount would rely upon a cash-flow chart that you do, in effect, rather than on a recurring percentage on a weekly basis?

Mr Bennett—Yes, it would tend to more align with the cash that we think we would need.

Senator HOGG—Where is this money held? Is it held in some form of daily cash management investment and drawn down?

Mr Roach—It is held in the Reserve Bank, and we earn interest on that money.

Senator HOGG—Yes, you are earning interest on that money on a daily basis. Where is that interest reflected in the accounts, and does that mean that the interest that will be earned by Defence as a result of higher holdings of cash will be greater in the forthcoming years?

Dr Hawke—While Mr Roach is finding that information, perhaps I could give you some examples of the cash balances of other organisations. BHP's tends to be about 5.4 per cent of its annual cash requirements; Coles Myer's is about 2.2 per cent; Health and Ageing's is about 5.9 per cent; Family and Community Services's is about 3.9 per cent; and, in Defence's case, it is equivalent to about 3.5 per cent. For instance, BHP would have around \$1 billion of cash on hand at any particular point in time and Coles Myer would have \$580 million or so.

Senator HOGG—I understand, but Coles Myer is a completely different business operation.

Dr Hawke—That is right—and so are we. That is the point I am making.

Senator CHRIS EVANS—But you were holding only \$20 million a couple of years ago. I suspect that the big Australian and Coles Myer were holding about the same as they are holding now.

Dr Hawke—Yes, because they have been on an accruals framework for a lot longer than we have. That is one of the differences. They range from 2.2 per cent to 5.4 per cent, the two Commonwealth agencies of Health and Ageing and Family and Community Services are at 5.9 per cent and 3.59 per cent respectively and we are at 3.5 per cent.

Senator HOGG—You were going to answer my question about the interest.

Mr Roach—Yes. If you go to page 60 and look at table 3.1, which is the budgeted statement of financial performance, under ‘Revenues’ you will see a line for interest. The amount budgeted for 2002-03 is \$20 million. That amount grows across the forward estimates in line with the projected cash holding, and we would use that revenue to fund Defence activities.

Senator CHRIS EVANS—What interest rate is the Reserve Bank paying you on that?

Mr Roach—I would have to get you that figure, Senator.

Senator CHRIS EVANS—Is it an investment account or is it just a normal sort of cash balance account?

Mr Bennett—We would have to provide you with the details, because they are different accounts.

Senator CHRIS EVANS—Is it invested or is it just held like your Commonwealth savings account? I know that we are talking about much bigger numbers.

Dr Hawke—Mr Martin might be able to answer that question.

Mr Martin—The rate of interest we are paid depends on our own investment performance. We nominate an amount of money and the period we want to invest it for—for a couple of days or for a few months—and the interest rate is based on commercial rates.

Senator CHRIS EVANS—How much of the \$600 million would you have invested at any one time?

Mr Martin—We do not have \$600 million at the moment. That is our budget for the end of that particular year. It depends on where we are in the draw-down cycle. Every fortnight we draw down somewhere in the order of \$600 million.

Senator CHRIS EVANS—At the end of this financial year—that is, by the end of next month—you are supposed to have \$500 million.

Mr Martin—I would hope we would invest nearly all of it. Depending on what our short-term liquidity requirements might be in those first few weeks of July, I would hope that we have invested the majority of that money. I should clarify: we determine how much for a notional investment; Treasury certainly continues to manage the whole of Commonwealth government financial reserves.

Senator CHRIS EVANS—I am not trying to get from you the exact amount, \$372 million at three per cent or whatever; I am just trying to get a sense of how this is managed. Would you have some of it on a three-month, six-month or a year-long period?

Mr Martin—That is correct. As has been indicated before, we turn over almost \$600 million a fortnight, so we have always got to make sure we are prepared for that sort of turnover. We would spend a lot of that on draw-down day because it coincides with salary payment day. We might put some away for a week or so within that draw-down period but, as you have noted, of the balances of \$500 million that we expect to have at the end of this year

we are certainly leading up to putting the majority away for a more substantial period of three, six or even 12 months.

Senator CHRIS EVANS—What would be the longest period for which you have invested part of that?

Mr Martin—It is a notional incentive scheme for us really, so it depends on what notional interest rates are offered to us by the government. My recollection of the recent performance or recent indications is that the interest rate we were offered flattened out after three or six months. There is no incentive for us to nominate it for any longer than that because we would have to break the investment, and notional penalties are imposed on us for breaking an investment.

Senator CHRIS EVANS—But some of that money would be invested for as long as six months to maximise your returns?

Mr Martin—That is correct. We would like to make sure that we take the benefit of the highest interest rate offered, which tends to be for a longer period; but, as I said, because of the flat yield curve and the interest rate in recent years there is no real incentive for us to put it in the bank for, say, two years or anything like that. Having said that, the moment that that investment might expire we would reinvest it again.

Senator HOGG—Do you get to keep the interest that is earned on these investments or do you have to return it to Finance?

Mr Martin—We retain the interest from our investments. Of course, that is taken into account in our overall budgeted financial statements. So that is just one source of funding for Defence.

Senator HOGG—In the annual report from last year, I note that under the heading ‘Interest and dividends’ in 1999-2000 there was roughly \$31 million and in 2000-01 roughly \$33 million. I do not know what other matters are mixed in by way of dividends which might be separate from interest, but it would seem that the figure you are estimating for this year, \$20 million, is substantially lower than what one would think would be the interest component of the interest and dividends in those two years and yet you are increasing the amount of money that you are going to have invested over any period of time up to \$500 million or \$600 million. Can you explain that to us?

Mr Martin—Our investment performance for 2000-01 and again for the current year certainly has been based on having a lot less money in the account and lower interest rates. Both are going up in the next year and certainly across the forward years, so at this stage we have made an estimate. We round the estimate.

Senator HOGG—I accept that. Have you changed your strategy, though? You have obviously changed the amount; have you changed the strategy as well?

Senator CHRIS EVANS—Senator Hogg’s point is that, on the face of it, you are going to earn less with a lot more money invested.

Mr Martin—We will not be earning less. I would have to look at the breakdown of interest and dividends, but I can assure you that the budget—

Senator HOGG—Can you get back to us on that?

Mr Martin—interest for the next financial year is higher than what we expect to get this financial year.

Senator CHRIS EVANS—But, according to those figures, while you have been earning \$30 million on a lot less than \$600 million, you only expect to earn \$20 million to \$25 million on \$600 million.

Mr Martin—Table 3.1 on page 60 does show steadily increasing interest returns over the forward period from that projection in the current financial year—

Senator HOGG—That is not my point, though.

Senator CHRIS EVANS—Senator Hogg's point is that you have done better than that in the past.

Senator HOGG—My point goes back to page 151 of the annual report. You may well need to disaggregate the interest and dividends and tell us which component is interest and which is dividends, given that we are looking at a substantially lesser cash amount than you say you have been investing over that time.

Mr Martin—Yes, I take your point.

Senator CHRIS EVANS—So we have got a lot of this money invested and returning to you. Do you make those decisions about how much you invest in consultation with Finance or is that purely a prerogative of Defence?

Mr Martin—One of our responsibilities is to manage our overall budget, including our cash reserves. We consult across our own department to make sure we understand where the cash requirements are. We look at our balance sheet to look at the longer term—both short-term and long-term—liquidity issues. It is an area in which we are improving. We do have a way to go at this stage, and that reflects one of the reasons why we have moved on from the \$58 million last year to the higher amounts in the bank now.

Senator CHRIS EVANS—I understand DOFA last week, when explaining this, made the suggestion that you had had a bit of a cash crisis at the end of 2000-01. Is that right?

Mr Martin—Liquidity is a function of a lot more than cash at bank. We also need to look at our receivables, for instance. In the first month of the current financial year, we did go into a small overdraft a number of times in making sure we paid our bills, but we did have a large amount of money—as reflected in our additional estimates—which was forthcoming from the government as a result of costs incurred in the previous year.

Senator CHRIS EVANS—When did Defence go into overdraft—July 2001?

Mr Martin—In July 2001, we went into overdraft by a small amount. We certainly did not not pay any bills because of any shortages of available funding.

Senator CHRIS EVANS—Was that overdraft arrangement with the Reserve Bank?

Mr Martin—In the same way that we can invest money, we can go into overdraft with the Reserve Bank. We might have money put in a cash deposit or a term deposit and we may choose not to break that deposit rather than go into a short-term overdraft.

Senator CHRIS EVANS—What was the extent of the overdraft?

Mr Martin—It was somewhere around \$50 million, for a few days.

Senator HOGG—What were the rates on that?

Mr Martin—I might have to check on that.

Senator HOGG—Were they commercial rates?

Mr Martin—They are based on commercial rates, yes.

Senator CHRIS EVANS—Why was that time particularly difficult? I am just trying to put it in context. The deployment pressures obviously came later in the year. What would have brought the pressures on at that time of the financial year?

Mr Martin—The government made a number of decisions in 2000-01 in relation to accelerating Defence spending. Because we still had cash available at the end of the year—these decisions were made subsequent to that year's additional estimates so there were no adjustments to our appropriation—the government decided to give us that money in additional estimates 2001-02, and they were detailed in the portfolio additional estimates statements at the time.

Senator CHRIS EVANS—So that was in fact money for operations in the year 2000-01 that had been unfunded to that stage?

Mr Martin—None of those decisions related to operations in the military sense.

Senator CHRIS EVANS—What were those other decisions then?

Mr Martin—They were detailed at additional estimates time. They included the acceleration of some capital projects work from 2001-02 into 2000-01 and some balancing of some East Timor payments.

Senator CHRIS EVANS—I will just go through that. You brought forward some capital works? Which were they?

Mr Martin—I would not be able to articulate which exact projects, but it was very public at the time.

Senator CHRIS EVANS—I am just trying to put it into context. What was the situation with East Timor payments?

Mr Martin—We used some East Timor money to balance some delays in the sale of our IT assets. We had some delays in the sale of our IT assets in that particular year; therefore there was a potential funding problem. We brought forward money from the future year into that year. The net effect was that we had appropriations forthcoming in 2001-02 to meet costs we incurred in 2000-01. So, yes, while we did have a short-term liquidity problem there, we had the comfort of knowing that there was an appropriation forthcoming.

Senator CHRIS EVANS—When DOFA talked about a cash crisis, would they have been referring to that period? I do not have the *Hansard* in front of me, so that may not be their term. I am not trying to put words into anyone's mouth. They referred to a problem Defence had with liquidity—cash et cetera.

Mr Martin—Whatever the words they might have used, yes, they were referring to that period.

Senator CHRIS EVANS—So this was not about the pressures that were on the Defence budget while waiting for the additional estimates in February?

Mr Martin—It was in relation to the money we got in the additional estimates, but not in the more public operational issues that have occurred since then. These issues occurred in July 2001.

Senator CHRIS EVANS—But was there another squeeze in January-February?

Mr Martin—No, not that I am aware of—not in cash funding terms.

Senator CHRIS EVANS—So you did not need overdraft facilities or whatever on that occasion?

Mr Martin—Not that I am aware of, no.

Senator CHRIS EVANS—Because, as you know, some directives et cetera went out about—

Mr Martin—They were more in the sense of the whole-year budget.

Mr Bennett—We were waiting for additional funds in the AE, so we had to control our rate of spend.

Mr Martin—We were waiting for the government's decision.

Senator CHRIS EVANS—Control the rate of spend—that is a nice way of putting it, Mr Bennett. I did not want to draw the crabs by saying you had to tighten your belt or not pay your bills for a while, but you had to control your rate of spend—and that was in the January-February period?

Mr Roach—Yes. I would probably just change the wording of that a little bit. At that point, before the additional estimates were through, we had on one hand a commitment to actually delivering the new operations that government wanted us to perform and we were bent on doing that. In order to do that, we were having to move money from other areas of the budget to support those operations. So, in those areas not connected with operations, yes, we had to manage funding very tightly, but the money was not lost and it was not a liquidity issue; it was just that the money was being redirected to higher priorities. Then the additional estimates effectively came through and we have been able to rebalance since then.

Senator CHRIS EVANS—So, effectively, you sent out a series of directives about spending to non-operational areas—is that correct? I think the one I saw was in the DMO, but it was more generally to the non-operational tasks. Is that right?

Mr Roach—I do not know about directives, certainly from the CFO organisation. But, in a sense, we were seeking to get the operations up and going and, to the extent that we needed to find money for specific things for those operations, it had to be taken from existing budgets. Those other areas were constrained at that time. That is simply directing the funds to the government's priorities.

Senator CHRIS EVANS—What did that mean, though? Obviously that put some pressure on some of your other things, but were you not paying bills?

Mr Roach—No, it was not a liquidity issue.

Mr Martin—It was about the whole-of-year budget. Dr Hawke made a reference before to the fact that government policy following the election was that we may have to absorb this. We put in place contingencies. We leave it up to our own groups and services to manage the pressures that they might be feeling. But, certainly, we looked at different options as far as putting in place contingencies for funding those operations.

Senator CHRIS EVANS—But you did have absorb some of the costs anyway, didn't you? I will come to them, but were there cost offsets?

Mr Roach—For the additional estimates 2001-02, yes, and in this budget.

Senator CHRIS EVANS—So you got a partial result—you got funded for some of it but not all of it. Is that the fair summary?

Mr Roach—That is correct.

Senator CHRIS EVANS—I think Dr Hawke gave evidence before that you were not exactly sure what you would get out of additional estimates, so I suppose you had to plan for the fact that you might get nothing at all.

Mr Roach—That is correct.

Senator CHRIS EVANS—Following the good news that Senator Hill had come through and done his job—

Senator Hill—It is nice of you to say so.

Senator CHRIS EVANS—All of those press briefings of December had paid off—and the additional estimates were there, that meant you were able to loosen the strings again in February. Is that right?

Mr Roach—It meant that we were able to adjust group budgets to fund those pressures. That meant we were able to move some money back to other areas.

Senator CHRIS EVANS—Some of those areas would have been told that they had been cut and would then have been told that they had only been cut half as badly after additional estimates. Is that the sort of message they got?

Mr Roach—That sort of message, I think.

Senator CHRIS EVANS—I am not talking about the words; I am just trying to understand the process. They would have been told to cut their cloth accordingly, and then you had some slightly better news for them after the additional estimates, or were the cuts proceeded with in whole in some areas and not in others?

Mr Roach—I could not speak for how individual groups managed their particular priorities, but in essence once the additional estimates came through we were able to provide money to groups and they were able to redirect that to their next highest priorities, if you like.

Dr Hawke—I am in a position to respond to some of the earlier questions, if you would like to have those answers. They are responding to Senator Faulkner's questions.

Senator HOGG—We might get Senator Faulkner, if you would just hold on a bit.

CHAIR—Why don't we do that when we come back after lunch and we can arrange for Senator Faulkner to be here.

Senator CHRIS EVANS—Is that all right with you, Dr Hawke?

Dr Hawke—Sure.

Senator CHRIS EVANS—That way I can organise for Senator Faulkner to be here. Otherwise we might do it twice: he will come back in and go over it again.

CHAIR—I think that is the way to handle it, Dr Hawke.

Senator CHRIS EVANS—Could I ask some questions about employee costs, on page 60.

Senator HOGG—Could I just go back. Seeing we have a number of people from the finance sector, it might be appropriate to go back to the question I asked earlier, under table 1.1. I heard your explanation about the special military equipment being accounted for as an expense. Does that mean that that special military equipment is not a part of your depreciation costs?

Mr Martin—No, it does not. That is a specialised treatment for International Monetary Fund type purposes, for government finance statistic purposes. It does not affect the way we have presented this budget.

Mr Roach—In fact, if you look in table 1.1, we have laid out the measures according to the accounting standard that supports the Defence financial statements. In the next section, which starts two pages over, headed ‘Budget measures’, the measures are laid out essentially as you find them in the Treasurer’s budget papers. There is a little bit of formatting change, but essentially one is the Defence views that put—

Senator HOGG—Yes. It was just the footnote that threw me off. I understood that the military equipment was taken into account in terms of depreciations costs that will be found elsewhere throughout the accounts—whereas you do not normally depreciate an expense hike.

Mr Roach—Correct.

Senator HOGG—But this is in consistency with a particular accounting standard rather than impacting on the rest of the Defence accounts. Is that a correct way for me as a layman to explain that?

Mr Roach—Yes.

Senator CHRIS EVANS—That is the layman’s explanation!

Senator HOGG—Yes, I am a layperson in this area. I have never laid claim to having any expert knowledge.

Senator CHRIS EVANS—Am I right in saying that you had overestimated employee costs in 2001-02 by about \$186 million, from the additional estimates?

Mr Roach—Our current estimate is that we will be, in cash terms, \$186 million over in terms of our estimation.

Senator CHRIS EVANS—Why is that?

Mr Roach—There is no simple explanation. We are having some difficulty in coming up with good estimates for all of our employee expenses. It is not so much the salary and wages that are a problem but the non-cash items. At the same time, because of the way our financial systems are actually working at the moment we are not able to get really good data and good projections.

Senator CHRIS EVANS—Again, to the layman, I would have thought salaries and employee costs was one of the few things that you would have had a good handle on. I can understand other areas of the Defence budget would be much more difficult to predict. I am a bit surprised by that. You say it is the non-cash items that are giving you difficulty?

Mr Roach—In fact, there are several things, but they are all captured in that number. One is that we have not actually had the work force that we thought we had and budgeted for. We have fewer military people than we originally expected to have. We have slightly more civilians, and that has also affected the estimates.

Senator CHRIS EVANS—I know that you are below your military targets. You are actually in excess of your civilian numbers, are you?

Mr Roach—That is correct.

Senator CHRIS EVANS—By how many?

Mr Roach—From memory, I think we were budgeting at the start of the year at around 16,300 civilians. I can get you the exact number. For 2002-03 we are looking at around 17,300.

Senator CHRIS EVANS—You are 1,000 over where you thought you would be in civilian numbers?

Mr Roach—We are 1,000 over the start point, but again there are explanations as to why that number is growing. Partly it relates to civilianisation. Partly it relates to planned increases in various Defence groups. Those are the major contributors.

Senator CHRIS EVANS—It appears, on my reading of the budget papers, that you have been allowed to keep that money, the excess of employee costs. Is that right?

Mr Roach—It is all one budget. We move the dollars in order to meet our priorities. For example, there is going to be some movement between the suppliers expense and employee expenses as we reduce our contractors and PSPs.

Senator CHRIS EVANS—By effectively the \$186 million that was overestimated is to be retained by Defence?

Mr Roach—That is correct. That is a cash number.

Senator CHRIS EVANS—Mr Chairman, do you want to do the responses to Senator Faulkner's questions now, given that he has arrived?

CHAIR—Are you happy to do them, Dr Hawke?

Dr Hawke—Yes. There are a number of points. It appears from pages 11 and 12 of the additional estimates that the \$20 million for PNFDF reform did not come out of the Defence Cooperation Program as I thought. There was a specific provision for it. That is set out at 11 and 12 of the 2001-02 additional estimates. In terms of the Eminent Persons Group report—

Senator HOGG—Could you just draw our attention to that?

Dr Hawke—It is specifically mentioned on pages 11 and 12 in the summary table 1.4. You will see the reference at page 12 to the specific rebuilding program.

Senator HOGG—That is \$20 million of new money?

Dr Hawke—Yes. It depends on how you look at this, but you can rightly interpret that as a specific recognition of that \$20 million.

Senator FAULKNER—If you go down to the bottom of page 12—

Dr Hawke—Yes, the reprioritisation.

Senator FAULKNER—The last sentence.

Dr Hawke—Yes, that is correct. But that is why I say it depends on how you interpret it. My understanding is that, if you go back to the top of this table to the lease-back of sold accommodation, that figure would have originally been minus \$36 million. It was offset by the \$20 million for the Papua New Guinea Defence Rebuilding Program. That is the understanding I have of what happened. That is the way in which it is presented in the papers.

Senator FAULKNER—Lease-back of sold accommodation?

Dr Hawke—Yes, because we did not sell that accommodation at that time and therefore we did not require the supplementation for the lease-back. So we would have returned that to consolidated revenue.

Senator HOGG—I can accept that, but why would you not therefore show that figure for lease-back of sold accommodation as minus \$36 million?

Dr Hawke—I will have to ask the experts.

Senator HOGG—That does not seem to reflect a true picture of the position. I can understand the net outcome—

Dr Hawke—I do understand clearly what you are saying.

Mr Roach—I am sorry, Senator, I missed the question.

Senator HOGG—To some people, it is called a hospital pass. The question was, in view of the secretary's comment, the lease-back of sold accommodation was minus \$36 million. That is not the way it was represented. It was represented as minus \$16 million, and the other \$20 million was shown as being the 'Papua New Guinea Defence Rebuilding Program'. Why wouldn't you show the true situation as it happened in terms of the lease-back of sold accommodation and then address the other matter in a different way?

Mr Martin—In the additional estimates statements at that time, you will notice that there is a net reduction figure, at the end of that long list of initiatives on page 8. It was certainly just an oversight not to specifically distinguish that \$20 million as a reduction lease-back. We have the \$16 million offset for reductions in rent; it certainly should have been \$36 million.

Senator HOGG—You referred me to page 8. Whereabouts on page 8?

Mr Martin—On page 8 of the additional estimates statements. In the top dot point, the fifth dash refers to a reduction in rental of \$16 million.

Senator HOGG—That is correct, but the figure was really \$36 million.

Mr Martin—I agree with you, Senator.

Senator HOGG—Yes; I think that is sloppy.

Mr Martin—There was a lag between the preparation of this and the decision in relation to the \$20 million.

Senator Hill—It seems I did not do as well as I thought I did.

Senator HOGG—No; you will have to go back to hugging trees.

Senator FAULKNER—You say on page 12:

Defence has met this new initiative through internal reprioritisation of spending.

Just so that we can be clear, what in its totality is the 'internal reprioritisation of spending'?

Dr Hawke—The point is that the figure in table 1.4, on page 11, should have been minus \$36 million—that is, lease-back of sold accommodation. Then the \$20 million was added back to the Papua New Guinea Defence Rebuilding Program. We have presented the net \$16 million. It may be that it is covered by the figure at page 8, where it says:

- a net reduction in other spending (-\$68m)

I do not know whether that is the way we covered it for the purpose of these accounts.

Senator FAULKNER—So the previous evidence that this came from the Defence Cooperation Program is not true.

Dr Hawke—Yes, it is not true; I want to correct that. It was then added to the Defence Cooperation Program and discharged through the DCP.

Senator FAULKNER—The \$20 million?

Dr Hawke—Yes. So I need to add that.

Senator HOGG—I think that, when it comes to the annual report, you will need to explain this matter, for transparency reasons alone.

Dr Hawke—Yes. One of the additional issues you were interested in, Senator Faulkner, was what happened with the EPG and the subsequent consideration. As I understand it, the Eminent Persons Group report was finalised around the end of 2000, and then considered by the Papua New Guinea government in March. That was what led to the subsequent demonstrations by the defence force up there. The Eminent Persons Group report was put aside and PNG began working on its own reform package. The National Security Committee of cabinet considered this matter in May and agreed to the provision of the funding. That was done in advance of the two Prime Ministers meeting in July 2001, when this was an item they discussed.

Of the \$20 million, 80 per cent was to go towards redundancies and 20 per cent towards what were called reform stoppers and morale issues. This involved paying some old allowances, fixing up some of the barracks accommodation and some repairs to aircraft and ships. As of 31 May, some \$17 million of the \$20 million has been spent and about 15 per cent of that has been spent on the reform stoppers; the rest has been spent on redundancies.

Senator FAULKNER—What has been the pattern in the retention rate in the PNGDF over the longer term?

Dr Hawke—I would not know.

Senator FAULKNER—I reckon I know.

Adm. Barrie—This is just a view of mine but the average age of the PNG Defence Force is about 47, and the long-term retention rate has been almost 100 per cent, and that is the problem.

Senator WEST—Unlike Australia's retention rate.

Senator Hill—That is a difference between a developing and a developed country. The picture is similar in most developing countries where a job in the armed forces tends to give you the best security possible.

Senator FAULKNER—What is our current retention rate?

Mr Roach—It is about 12½ per cent.

Senator FAULKNER—And PNG's would be and has been consistently—

Adm. Barrie—Very high, and that means that there has not been recruitment and refreshment of the force. That is one of the reasons why the PNG government has been pursuing these reforms.

Senator FAULKNER—It is not a new issue at all. This has been a long-term problem in the PNGDF, hasn't it?

Adm. Barrie—It has.

Senator Hill—What we are saying is that in the last few years the problems have become particularly manifest in terms of behaviour.

Senator FAULKNER—You might be saying that, but it is the same as the budget pressures that they face. Is the PNG budget still organised on a calendar year basis?

Dr Hawke—I do not think it is. I think they have moved to some other arrangement where it is on an October to October basis. I do not know why they would have moved that way, but I will find that out for you.

Senator FAULKNER—This arrangement on 8 October happened at what stage of their budgetary cycle?

Dr Hawke—I do not know.

Senator FAULKNER—If it was October to October—

Dr Hawke—Yes, but it was not relevant to what we were doing, so it was never a factor. I can confirm from Nick Warner that the meeting concluded at 11 o'clock on that morning.

Senator FAULKNER—Did he take notes?

Dr Hawke—I have not asked him. My recollection is that he did have some notes and that that is how he constructed the letter.

Senator FAULKNER—You might ask him. You cannot assist me with the budgetary cycle and how these particular pressures—

Dr Hawke—No, but we can get it quickly for you over lunch. Are there any other outstanding issues?

Senator FAULKNER—I will wait to see what you are able to report back after lunch.

Dr Hawke—Okay.

CHAIR—We will break for lunch.

Proceedings suspended from 12.30 p.m. to 1.34 p.m.

CHAIR—Dr Hawke, I understand you have some answers for Senator Faulkner.

Dr Hawke—In response to your question, it still is a calendar year in PNG. High Commissioner Nick Warner confirms that he took notes of the meeting. Regarding the costings during the caretaker period in the Charter of Budget Honesty, the log of the costing unit in Finance does not show any contact with Defence on the cost of the war on terror. Defence Cooperation Program money has not been used before for redundancies. When Mr Hannan turns up, he will be able to answer the one additional question that we had hanging over.

Senator FAULKNER—Which one was that?

Dr Hawke—There was a further issue that you asked about relating to email. Mr Hannan has gone away to investigate that.

Senator FAULKNER—Do you have the time of the cabinet committee decision making in relation to the \$20 million expenditure?

Dr Hawke—It was in May 2001.

Senator FAULKNER—Are you able to say what terms that decision was in?

Dr Hawke—I did have something on that here, if you will bear with me. The decision was that the government is committed to assisting the PNG Defence Force, including the provision of funding to assist with a program of redundancies, to permit a planned reduction in the

Defence Force to sustainable levels. The exact timing of the payments was somewhat uncertain. They may or may not occur in the 2001-02 financial year. The details were to be worked out.

Senator FAULKNER—Have you had any contact with Secretary Halton over evidence that either you or she gave to the Senate Select Committee on a Certain Maritime Incident?

Dr Hawke—Yes. I wrote to her about her testimony in response to questions from you, where it seemed to me that she was expressing some puzzlement over why I or other people whom she knew very well had not rung her to cast a different light on the ‘children overboard’ issue. I wrote to her about that, saying that I thought that was the impression she had conveyed and that she needed to understand why I had some difficulties with that.

Senator FAULKNER—Is that the only contact you have had with her?

Dr Hawke—In writing, yes. We spoke about the matter. Within a few days of me writing to her, I ran into her at a function in the Great Hall and we had a very brief discussion about that. She said that she would write back to me to clarify what she had meant rather than what might be interpreted from what was in the *Hansard*.

Senator FAULKNER—Has she written back to you yet?

Dr Hawke—Yes, she has.

Senator FAULKNER—Would you be able to make available copies of that correspondence?

Dr Hawke—I understand that that has already been asked for in the PM&C estimates hearing.

Senator FAULKNER—I did ask some questions about that.

Dr Hawke—My understanding is that the Department of the Prime Minister and Cabinet are going to table them. The reason they were holding off was that I felt I should also write to Senator Cook about the matter, in the light of that exchange of correspondence. I will have to ask Ms Halton but I assume, since she is comfortable for it to be tabled in the other committee, or I understand that she is, that there is no problem about the correspondence being tabled here as well. We will do so within the next day or so.

Senator FAULKNER—Thank you very much. I was going to ask you about one or two comments Ms Halton made in her evidence, but it may be best for me to look at the correspondence and follow it through later in the week when those documents are tabled—although you are not going to be here, Dr Hawke.

Dr Hawke—If the committee requires it, I will be here.

Senator FAULKNER—I do not want to delay the committee. I will look at the correspondence and follow it through later. If you are able to do that within the next 24 hours or so, that would be appreciated. The committee secretary will no doubt let me know when that material is provided by Dr Hawke.

CHAIR—We will do that, Senator Faulkner.

Senator CHRIS EVANS—Mr Roach, before the break we were talking about employee costs. It seems to me that, on page 60, your projections for employee costs seem to be running at quite a high level, with an average increase of 4.8 per cent on my figuring. Is that right?

Mr Roach—If you look at employee expenses in terms of the change between 2001-02 and 2002-03, it is six per cent. If you want to look at it in per capita terms, which is probably a better way because we are in fact planning to grow our numbers, the increase is about 4.9 per cent.

Senator CHRIS EVANS—That is obviously faster than the annual growth of the Defence budget and proportionally a quicker rise in employee costs. Why is that? I notice in your annual report there is a concern about the growth in employee costs. I am just trying to understand what is driving this.

Mr Roach—There are three elements that drive our employee expenses. The first is the planned increase in numbers that the white paper sets in train. The second is just the normal growth in wage and salary costs that we have to deal with, as does everybody else. The third is that we include a number of items in our employee expenses that are non-wage and salary such as medical costs, fringe benefits tax and things like that. Those costs have traditionally grown—and I expect will still grow—at faster rates than just normal wage and salary costs. So, effectively, our budget takes all those things into account.

Senator CHRIS EVANS—Isn't this growth in employee costs long term going to put pressure on the overall Defence budget?

Mr Roach—It will to an extent. It is a problem that we always have to manage. But, again, we were able to get recognition in the white paper that, if we wanted to grow the ADF and the Defence organisation as government intended, we needed some extra money to do that, and that was provided through the white paper. It starts in 2004-05 and is built into our budget from then.

Dr Hawke—Where the government has taken specific decisions that have manpower implications, it has also recognised that additional funding on the personnel side is required. That has been provided in respect of the Incident Response Regiment and the Tactical Assault Group.

Senator CHRIS EVANS—I was going to bring you to those now.

Dr Hawke—So the 26,000 figure that was originally in the white paper as the number for the permanent Army will increase as a result of those decisions.

Senator CHRIS EVANS—So the TAG and IRR are going to add to that total?

Mr Roach—Yes, they will.

Senator CHRIS EVANS—Do you have the numbers for those?

Mr Roach—Not off the top of my head.

Dr Hawke—Could we deal with that when we come to the Army program? Army will have the details.

Senator CHRIS EVANS—Sure. As a rough guess, I thought there would be 100 in one and 500 in the other. Will that be added to the 26,000 target?

Mr Roach—Yes, whatever the numbers are.

Dr Hawke—We will confirm the numbers for you when the Army program is up.

Senator CHRIS EVANS—Can someone explain to me how the two per cent growth driven by the white paper is going to work?

Mr Roach—It started in the year beyond the forward estimates. At that point in time a wedge of funding was added which would effectively allow the organisation to grow its total employee bill with the aim of actually reaching a total permanent ADF of about 54,000 by 2010. That money is in our estimates now.

Senator CHRIS EVANS—So the two per cent real growth is to provide for extra employees?

Mr Roach—It is to provide a level of funding which will enable us to grow the numbers of people and to pay them what we believe is a reasonable amount on a sustainable basis.

Senator CHRIS EVANS—But the two per cent does include, as part of its charter, as it were, meeting the increases in numbers?

Mr Roach—I think we might be getting confused over different two per cents. There are two in this context. The first two per cent is the price indexation that we will expect to get year on year. The second two per cent is effectively the white paper provision to top up our budget.

Senator CHRIS EVANS—That is the one I am referring to—I am trying to get an understanding of how that works.

Mr Roach—It is a wedge of funding added to the Defence budget, starting in 2004-05 and continuing until 2010.

Senator CHRIS EVANS—So you do not get any of that two per cent real growth from the white paper until 2004-05?

Mr Roach—That is correct.

Senator CHRIS EVANS—Are some of these personnel measures that were announced recently—I think Mr Vaile was talking about a child-care initiative—part of that funding?

Mr Roach—No, they are not. The money that is being set aside for recruiting and retention initiatives—there are others who can speak about the specifics of those—is money that also came, effectively, from the white paper. Around \$100 million was set aside each year in order to proceed with those initiatives.

Senator CHRIS EVANS—So there is \$100 million each year for recruitment and retention initiatives, which is separate from the two per cent real growth?

Mr Roach—Yes.

Senator CHRIS EVANS—That \$100 million per annum started from last year, is that right?

Mr Roach—This current financial year: 2001-02.

Senator CHRIS EVANS—But that is a flat new \$100 million each year?

Mr Roach—It is \$100 million each year going forward. It is not \$100 million, \$200 million, \$300 million; it is \$100 million.

Senator CHRIS EVANS—How will the initiatives you fund with the \$100 million this year be funded in the out years?

Mr Roach—The \$100 million?

Senator CHRIS EVANS—Yes.

Mr Roach—We do not have \$100 million for new initiatives every year.

Senator CHRIS EVANS—You have got \$100 million which will be funded each year, but it is to meet \$100 million worth of initiatives et cetera?

Mr Roach—Yes, and that would also get approximate indexation.

Senator CHRIS EVANS—That was very inelegantly expressed by me, but that is right. So the two per cent real growth cuts in in 2004-05. What is the logic of the two per cent? How did we come to the two per cent figure?

Mr Roach—As part of the white paper development process we did some work to look at the trends in our personnel costs. As you would be aware, we have basically shed a lot of people, on both the military and the civilian sides, over the last two decades. Actually growing the organisation represents a major departure from that trend. We recognised, and the government recognised, that we needed funding to actually reverse that and grow.

Senator CHRIS EVANS—Obviously there is some science, but there is no pretence that there is any particular science to the two per cent—it was a judgment decision about providing some extra funds to allow the growth to occur. Is that correct?

Mr Roach—The basic logic is that we have to be an employer of choice. Our work force, virtually everywhere you look, needs to be more highly trained and more skilled than in the past so we have to be in a position to attract those people. We have to have competitive wages and conditions. If you look around in the market we are competing in, with the indexation and the two per cent together we are in a position to compete. It is effectively allowing for something like 4.5 per cent per annum growth.

Senator CHRIS EVANS—I will come back to the TAG and IRR in the Army program, but please explain to me about the \$32 million to be spent in 2002-03. I think it is on page 20 of the budget documents. How is that to be spent? Is that the personnel costs? There is 'Enhancement to Defence's tactical response capability' and 'Tactical Assault Group' et cetera. The funding of \$32 million in next year: is that to be spent on personnel costs?

Mr Roach—A small element of it is but the personnel numbers and expense you see there on the expenses line actually grow over time as the capability is transitioned to a permanent independent force.

Senator CHRIS EVANS—What is that money for, then? Is that additional money to go into the personnel budget to pay for this? Is that how it works?

Mr Roach—The expenses money includes some money for personnel, which grows over time, and supplies expenses for equipment stores and that sort of thing. There will be some depreciation. Then in the capital line you have basically got the new specialist military equipment and the new facilities.

Senator CHRIS EVANS—That is only half a million.

Mr Roach—It will take a while to progress the capital works associated with that.

Senator CHRIS EVANS—Yes. That is a significant expense in the year after. But not much of the \$30-odd million is for personnel. The personnel costs of these units will be met out of your gross personnel budget?

Mr Roach—What is happening at the moment is that we have an interim capability—Army knows more about this—which is based on people who are in 4RAR, the commando battalion. Over time we will restore 4RAR to its full commando role—

Senator CHRIS EVANS—I can see I am taking you into the area of Army expertise, which is not my intention, so I will come back to that later.

Mr Roach—Let me confirm the basic point: that measure does contain within it the dollars for personnel who will in fact form the permanent unit which is in addition to our present force structure.

Senator HOGG—Does it also include establishment costs where there might not have been infrastructure that would be needed?

Mr Roach—Do you mean facilities?

Senator HOGG—Yes.

Mr Roach—That is in the capital line.

Senator HOGG—Is it in that figure there on the second line?

Mr Roach—It is in the \$24.7 million. There is also some specialist military equipment in there as well.

Senator CHRIS EVANS—Roughly how much of the \$32 million is going to be personnel cost?

Mr Roach—My memory is that in 2002-03 it is relatively small. It would be better if I got you the breakdown.

Senator CHRIS EVANS—Yes. I am just trying to get a sense of it rather than the breakdown. From what you are telling me, it is probably quite small because you actually will not be replacing those people in the other units for a while, and it will take some time for that build-up at Kapooka—

Mr Roach—It is a wedge.

Senator CHRIS EVANS—I would like to ask some questions about asset sales. Has there been a change in policy in relation to asset sales and how they are handled? As I understand it, Defence has traditionally kept one per cent of its budget as proceeds from asset sales; is that right?

Dr Hawke—That issue would be best dealt with when we come to the corporate support program. We have now agreed between departments, principally Defence and Finance—and then the ministers decided—on the approach to the whole asset sales program. I think the Infrastructure Division will probably have most of the information related to that. Would you prefer to wait for that program?

Senator CHRIS EVANS—I always take guidance from the chairman, but I am happy to do it under the correct program. If you think it is best dealt with under corporate support, that is fine.

Dr Hawke—They will have the answers.

Senator CHRIS EVANS—In general, though, could you confirm for me that there has been a change in policy?

Dr Hawke—There has.

Senator CHRIS EVANS—Does that apply from this budget?

Dr Hawke—It might have applied from the additional estimates.

Senator CHRIS EVANS—I am unsure of whether it applied from additional estimates or from this budget.

Senator Hill—I think it is from this budget.

Senator CHRIS EVANS—Okay. If you are unsure, I think we will do it when we get to corporate support.

Senator Hill—I am reasonably confident.

Senator CHRIS EVANS—Yes; I am sure you have your head around it, Senator Hill. We will do that in corporate support.

Dr Hawke—In the unlikely event that the minister is wrong, we will let him know.

Senator CHRIS EVANS—I want to cover other budget type measures. I see you have a budget measure for 2002-03 to do with CHOGM. Can someone explain that to me? Is that just for historical interest?

Dr Hawke—Whereabouts are you, Senator?

Senator CHRIS EVANS—On page 19.

Senator HOGG—It is the second last item on page 19, under ‘Commonwealth Heads of Government Meeting’.

Senator CHRIS EVANS—It is listed as a budget measure and I wondered why. There does not seem to be any expenditure.

Mr Martin—You may recall that we listed the initiative in our additional estimates statements. Government budget paper convention is that any new initiative approved by the government in the whole-of-government context, since MYEFO, is reproduced in this year’s budget.

Senator CHRIS EVANS—So it is just a trick position to confuse us.

Mr Martin—It is not our trick, Senator.

Dr Hawke—It is just to record the fact that, since the mid-year estimates, that actually happened in the current financial year and that there are no expenses or costs in the out years.

Senator CHRIS EVANS—There are no provisions in the out years for the ‘Enhanced Protective Security’ measure. Can someone explain that to me?

Mr Roach—The reason there is no provision is that, essentially, we do not know what the security situation is going to be in 2003-04 and beyond. We are currently at a state called ‘Bravo’, which is an elevated level of security. Were we to remain at that level and need a level of security that reflected that, we would need to look at the provisions in the out years.

Dr Hawke—The government decided it would provide the cost just in the next budget and would then review the need for continuing provision in next year’s budget context.

Senator CHRIS EVANS—So that is not, then, to indicate—

Dr Hawke—That there will not be money; that is right. There may be but, at this stage, there is not, and the government wants to revisit that in next year’s budget context.

Senator CHRIS EVANS—So at the moment we only have enhanced protective security for the coming financial year?

Dr Hawke—Yes.

Senator CHRIS EVANS—I see that \$13 million is obviously for capital. What is the \$27.9 million for other expenses to be spent on?

Mr Roach—I can give you plenty of detail, but essentially it is the extra guarding and patrolling required around Defence's bases. I think there are about 800 bases, but not all of those would have that level of protection. That is in place for 2002-03.

Senator CHRIS EVANS—So the majority of the enhanced protective expenditure, non-capital, is actually on the hire of contract security firms to patrol Defence establishments. Is that right?

Dr Hawke—I think we have APS guarding at a large number of our places.

Senator CHRIS EVANS—Is it a payment to APS?

Dr Hawke—It probably reflects increased costs there. We would have some private security firms. Mr Bonighton may be able to help us.

Mr Bonighton—The majority of services are to do with guarding, but there is also signage and additional warning measures that have been put up around bases. We can certainly get you a more detailed breakdown on just how that was spent.

Dr Hawke—There are some physical protection measures too, I think.

Mr Bonighton—Indeed.

Senator CHRIS EVANS—Fencing and the like?

Dr Hawke—Yes.

Senator CHRIS EVANS—That is the capital, I presume. But, in terms of the \$27.9 million largely for guarding, is that guarding done by APS or by private security firms?

Mr Bonighton—It would vary. We did a risk assessment based on the particular circumstances on each base, and we then looked at what was needed to bring the security up to that level.

Senator CHRIS EVANS—I presume you already had guard services in place for many of them?

Mr Bonighton—For some of them, certainly. But there were upgrades and extended guarding periods. There was increased guarding because we changed the perimeter requirements.

Senator CHRIS EVANS—How do you determine whether you use APS or a private security firm? Is there a risk assessment?

Mr Bonighton—I would have to get you the detail of that. Perhaps we could do that under the intelligence and security program.

Senator CHRIS EVANS—Okay, if it is better done then. But am I safe to conclude that the majority of that money is going to go on increased guarding costs, basically?

Mr Bonighton—Yes. As I said, we can give you a more complete breakdown when we do the intelligence and security program.

Senator CHRIS EVANS—Thank you very much. In terms of the 'Incident Response Capability' initiative, can someone tell me whether we had a similar unit formed during the 2000 Olympics?

Adm. Barrie—We certainly did, Senator, but straight after the Olympics we returned those people to their normal jobs. We raised a special unit to deal with Olympic security. When the Olympics were over, they went back to normal tasks.

Senator CHRIS EVANS—So that was disbanded at the end of the Olympics?

Adm. Barrie—Yes.

Senator CHRIS EVANS—Is what we are forming here a very similar group?

Adm. Barrie—It is certainly based on the basic concepts. It will be slightly different, in the sense that there will just be one organisation as headquarters staff and two actual incident response teams.

Senator CHRIS EVANS—Have you decided where they are going to be located?

Adm. Barrie—I think in Sydney, but I would have to confirm that.

Senator CHRIS EVANS—So both teams are going to be in the one spot?

Adm. Barrie—Yes.

Senator CHRIS EVANS—Do you have an indicative view of the size of the Incident Response Regiment?

Adm. Barrie—I do not have the figure for the number of people allocated to it but I am sure the Chief of Army will have a very good idea.

Lt Gen. Cosgrove—The Incident Response Regiment will number 302 but, of those, pre-existing, there are soldiers who were part of the Olympic capability who were released back to units and who have now been regathered. The actual growth in numbers would be about 117 for the Incident Response Regiment, over and above what Army anticipated after Defence white paper 2000.

Senator CHRIS EVANS—I do not quite understand that, Lieutenant General Cosgrove, in the sense that, if you have sent them back to the regiment, haven't they been absorbed back into the numbers already?

Lt Gen. Cosgrove—That is right, and they are part of the requirement in growth. So we actually have a regiment that is forming now by regathering those people. Part of the growth will be to go up in number to absorb the additional people who were dispersed but who are still in the same roles.

Senator CHRIS EVANS—So you are telling me you will not end up with 302 new staff.

Lt Gen. Cosgrove—No. I am saying that the actual growth involved is 117.

Senator CHRIS EVANS—So you will absorb the other 200 owed you currently—

Lt Gen. Cosgrove—They were in what we might call 'bibs and bobs', but in the same sorts of roles throughout Australia. They have been brought together.

CHAIR—Where will they be based?

Lt Gen. Cosgrove—They will all be based in Sydney.

CHAIR—At Holsworthy?

Lt Gen. Cosgrove—Yes.

Senator HOGG—So where will the 117 be drawn from?

Lt Gen. Cosgrove—The 117 will be grown, so to speak.

Senator HOGG—So they will be new recruits, in a sense.

Lt Gen. Cosgrove—Yes.

Senator CHRIS EVANS—You are saying that some of those other 200-odd are actually performing those tasks but are attached to other regiments.

Lt Gen. Cosgrove—That is right.

Senator CHRIS EVANS—What sorts of people are we talking about?

Lt Gen. Cosgrove—Explosive ordnance demolition folk, high-risk search troops.

Senator CHRIS EVANS—So they are actually operating as a small sub-unit within another regiment.

Lt Gen. Cosgrove—And we retained a chemical, biological and radiological response company, or squadron, which also forms the nucleus of the IRR.

Senator CHRIS EVANS—Where are they currently?

Lt Gen. Cosgrove—They are in Holsworthy.

Senator CHRIS EVANS—So they are all going to be brought together in the new regiment?

Lt Gen. Cosgrove—That is right.

Senator CHRIS EVANS—Thanks for that.

Senator WEST—I will just go back to the 117 new personnel. You had 302, so does that indicate that the original group was 302 and you have lost 117 in less than two years?

Adm. Barrie—No, I think it is an enhanced capability we are talking about. What we had dispersed through Army units all over Australia was a basic level of capability. After September 11, we now need a more concentrated capability to deal with the consequences of any action in Australia.

Senator WEST—I do not think you understood what I was asking. In September 2000 we had the Olympic Games and we had a group. What was the number in that group?

Adm. Barrie—It was a pretty similar sort of number.

Senator WEST—Was it 302?

Adm. Barrie—No, it was a bit more than that.

Lt Gen. Cosgrove—It was larger; it was 500, I think.

Senator WEST—So, of that 500, 117 have presumably moved out of the Defence Force; they are not available to you.

Lt Gen. Cosgrove—I do not know whether you could construe that, Senator. That is the actual growth needed above the 26,000 ceiling. So, in the pluses and minuses of reorganising the Army to meet the 26,000 cap mentioned in the white paper, the additional growth above the 26,000 that the government has agreed to out of the IRR initiative comes to 117.

Senator CHRIS EVANS—How is the increased munitions war stock to be funded? In one place it is shown as costing zero dollars and that the funding will come from the white paper; yet at page 14 it states that the cost will be offset by cancelling \$20.9 million worth of military equipment.

Mr Roach—Table 1.1, which is the Defence presentation against the accounting standards applying to us, shows this as an additional cost of \$20.9 million, and we have been directed to find the dollars for that. We are finding them out of the capital program, so we also show the offset there from specialist military equipment. We are basically reprioritising in order to buy those higher priority explosive ordnance items. The Treasury table nets it off.

Senator CHRIS EVANS—There is no additional funding; it is taking \$20 million out of the military equipment budget?

Mr Roach—We are reprioritising within that budget.

Senator CHRIS EVANS—What is the budget for military equipment?

Mr Roach—It is \$4.72 billion from memory—it is in table 3.4—of which the specialist military equipment part is \$3.586 billion.

Senator CHRIS EVANS—This is from that small purchases account. What page is that on?

Mr Roach—Page 63.

Senator Hill—This is just a start in replenishing our war stocks. The total cost is still being determined. Over the next few years we would hope to be able to bring the war stocks up to contemporary requirements. That sum is unlikely to be able to be funded from within the existing budget, so to make a start on the project this year the amount that is specified—that we have been talking about—will be funded internally. As I understand it, this is separate and distinct from ammunition that is utilised for training purposes and the like.

Senator CHRIS EVANS—You are saying to me that increased munitions war stocks are different from ammunition used for training and ongoing purposes by the forces?

Senator Hill—Yes, as I understand it. It is basically the stock you keep for the emergency you hope you are not going to have. It gets run down over time—the munitions are no longer suitable because they have a fixed life and so forth—and from time to time it needs to be updated. There is an accounting argument as to whether it is capital or not if it is a war stock.

Senator CHRIS EVANS—It is capital until you use it.

Senator Hill—It is not like a consumable that you are using for training. If it is capital, should it require an amendment to the defence capability plan? That is part of the exercise we will go through later this year. Part of that will be how it should be funded.

Senator CHRIS EVANS—It is kept completely separate from your funding for training and ammunition. What is the right term?

Adm. Barrie—Operating expenses.

Senator CHRIS EVANS—Right. So the actual training and ammunition show up as an item, an operating expense. But you use a separate account, as it were, for war ammunition. For instance, the ammunition being used by SAS soldiers in Afghanistan would come under war stocks rather than operating expenses?

Adm. Barrie—Part of that would be allocated from war stocks to use.

Senator Hill—It does not necessarily mean that the munitions will not be used in an exercise, but if they are used in an exercise then they need to be replenished to maintain the war stock, as opposed to ammunition that is simply purchased with the intention of using it in exercises as part of training or whatever.

Senator CHRIS EVANS—I assume that because of the life of some of this stuff you would recycle some of it as training stock and then replenish it. It is not locked away in a cupboard.

Adm. Barrie—Ideally, you transfer some of it into an operating account to use it.

Senator Hill—It got confusing because Defence were actually conducting two different studies. One was on ammunition stocks for day-to-day consumption, and the draft report got some airing with assistance from you, Senator, I think. At the same time they were doing another study on war stocks, and we acknowledge that we already knew the war stocks needed to be updated. The issue on ammunition is one that is still to be determined when the draft becomes a final report.

Senator CHRIS EVANS—With the war stocks, we are not talking about two different types of munitions; we are talking about the way you account for them and the purposes for which they are held. Is that right?

Senator Hill—That is what I understand.

Senator CHRIS EVANS—Essentially it would be the same sort of munitions but accounted for as for other purposes. Where would you find that in the general budget line items?

Mr Roach—The war stock purchase?

Senator Hill—No, just consumables.

Senator CHRIS EVANS—It is both, actually. Where would I find the munitions war stocks as a budget item?

Mr Roach—We are planning to purchase the war stocks out of funds that are presently in the DCP. The DCP dollars are against the specialist military equipment line item in table 3.4. The purchase of explosive ordnance for training is out of the inventory budget, which is not separately shown here.

Senator CHRIS EVANS—What page is table 3.4 on?

Mr Roach—Page 63.

Senator HOGG—While Senator Evans is looking for that, could I ask if part of the problem raised by Senator Hill is the fact that there is no single inventory system whereby a list of the stocks are kept—the war stocks versus those that are used operationally?

Major Gen. Haddad—We have an inventory management system that does identify against which category stock is held, and there is a reserve category and there is an operating stock category. From a stock management point of view, you can identify what you are holding it for. The reserve stocks are earmarked or quarantined so that they are available for the purpose for which they were purchased.

Senator HOGG—All right.

Senator CHRIS EVANS—So effectively this does not go to the issue of the training ammunition argument; this is a separate issue. You say, Senator Hill, that this is a starting point. Is there a particular group of munitions that it was felt were necessary to replenish the stock? Is there a priority purchase?

Senator Hill—In the war stocks? Yes, there was.

Adm. Barrie—I think the munition that comes mostly into focus when we talk about the war stocks is the guided missiles category.

Senator CHRIS EVANS—I suspect they are also highly expensive per item.

Senator Hill—They can have long lead times and therefore decisions need to be made now to ensure the stock is kept up to date.

Senator CHRIS EVANS—So is it fair to say that is where that money is being prioritised: towards those missile stocks?

Adm. Barrie—I imagine that is where the bulk of the expenditure will end up going.

Senator CHRIS EVANS—What sort of life span do those munitions have?

Adm. Barrie—I am not qualified to say, except I do know that the motors that drive the weapons have a different sort of shelf life to the electronics and you have a refurbishment capability for those sorts of weapons.

Senator CHRIS EVANS—It was a layman's question and I wanted a layman's answer. I am just trying to get a sense of it.

Major Gen. Haddad—To give you any sense to the answer, I would have to go away and look at the detail. I could not make any judgments on the life of those munitions.

Senator CHRIS EVANS—Are we talking three months or 10 years?

Major Gen. Haddad—It is in years. If you wish, we could go and look at each category. The guided weapons are a category and the non-guided weapons are a separate category.

Senator CHRIS EVANS—But each is in terms of years rather than months?

Major Gen. Haddad—Yes, certainly—numbers of years.

Senator CHRIS EVANS—Senator Hill, are you prepared to give any indication of your view on the cost of the longer term replenishment of war stocks?

Senator Hill—We prefer not to at the moment but we want to be able to later this year. If it means amending the defence capability plan, that becomes part of public knowledge.

Senator CHRIS EVANS—But it would be a significant expenditure, no doubt.

Senator Hill—Yes. Anything that involves guided munitions is expensive.

Senator CHRIS EVANS—So it is fair to say that this measure does not have any impact on that argument about the training ammunition situation. You said that report has not been finalised.

Senator Hill—I assume it has not been finalised because I have not seen it yet.

Senator CHRIS EVANS—I will pick that up with Army. I was trying to take a budget overview approach here but I realise I am driving you back into various service arms and operational areas. Could someone explain to me where the \$87 million in administrative spending is going to come from and how that has been identified?

Mr Bennett—Is that the \$87 million?

Senator CHRIS EVANS—Yes. It is \$97 million less \$10 million for recruitment and advertising, isn't it?

Mr Bennett—Yes, \$10 million for recruitment and advertising, and a reduction of \$87 million in the administrative expenditure.

Senator CHRIS EVANS—That is easily said, Mr Bennett. How is it achieved?

Senator Hill—It depends.

Mr Bennett—It is difficult. It is the result of increased efficiencies within expenses such as facilities maintenance, publishing, printing, consultants and contractors and other general services.

Senator CHRIS EVANS—How has that been identified? Again, that is pretty easily said. Have targets been set for each of those programs?

Mr Bennett—Yes, targets have been set. That is part of the group allocations that are made within the budgeting process.

Senator CHRIS EVANS—So each of those sections got less than they thought they were going to get, and they were told that that was part of their savings measures—is that how it works?

Mr Bennett—They have been told in the broad. We will be working through the specifics of it in this.

Senator HOGG—How is that going to impact on the first category—I did not get to list many of those that you mentioned then—of facilities maintenance? I would imagine that that is a very important area. If you are going to start pulling money out of them, there will be squeals all around the place.

Mr Bennett—As soon as I announce that we are trimming budgets by that order of magnitude, I hear squeals. I do not think we are confusing the facilities maintenance in the general with facilities maintenance, say, in the enhanced security measures.

Senator HOGG—Could you list those things again? There is facilities maintenance, publishing—

Mr Bennett—Printing, consultants and contractors and other general services.

Senator HOGG—I can understand how you can cut a whack out of consultants and you would not miss them; I have no doubt about that. What do you mean by facilities maintenance? I do not want to see it impacting on the normal, everyday running and life of people in the Defence Force.

Mr Roach—The \$87 million represents about three per cent of what we would call our non-operational suppliers expense budgets, across the organisation. Three per cent is not a large figure except, of course, when you get around to actually finding it. We have excluded, from the base from which that offset has to come, the suppliers expenses that basically directly support capability maintenance, inventory and the like. Across all of those residual categories—and there are a great number, from the pens and pencils to facilities operations—we are going to have to find three per cent in 2002-03.

Senator CHRIS EVANS—But that is three per cent on top of the \$100 million you have to find from the white paper savings, isn't it?

Mr Roach—That is correct.

Senator CHRIS EVANS—How did you deal with that \$100 million? Is that again limited to those budgets?

Mr Bennett—No. There are some specific items, including \$14.2 million for a fringe benefits tax liability reduction, travel savings of \$20 million, commercial fleet reduction of

\$4.3 million and a group budget reduction based on re-baselining on the previous year's performance of \$69 million.

Senator CHRIS EVANS—But they are the same sorts of areas, aren't they?

Mr Bennett—No, I think some of them are very specific items—for example, travel and fringe benefits tax.

Senator CHRIS EVANS—So, in fact, you are looking for \$187 million this year?

Mr Roach—Correct. We are on the hook for \$187 million. If you break it into two parts, we have got to find the three per cent. We think we have done a little bit better against the white paper target, if you like. We have already reprogrammed that money into our current priorities which, of course, are operations.

Senator CHRIS EVANS—Because you have got to deliver \$200 million next year from the white paper savings, is that right?

Mr Roach—That is correct.

Senator CHRIS EVANS—So next year you are looking for around \$280 million?

Mr Roach—No, we will be looking for \$200 million.

Dr Hawke—The \$97 million was a one year only effect.

Senator CHRIS EVANS—I see.

Dr Hawke—It did not affect the base.

Senator CHRIS EVANS—So that is only a one-off for this year?

Mr Bennett—If you refer to table 4.1 on page 95, we have detailed where we expect to achieve the numbers that I just referred to.

Senator CHRIS EVANS—Yes, I was going to take you through a couple of those. What have you budgeted for travel for 2002-03?

Dr Hawke—Sorry, I do not have a travel budget number per se, but we certainly do expect to achieve the \$20 million saving.

Senator CHRIS EVANS—In previous years I have had you at about \$110 million for travel. Does that sound about right?

Mr Roach—I can get the figure fairly quickly. But it is important to understand that, in looking at 2002-03, we do not budget at a portfolio level down to that degree of fineness in the expenses.

Senator CHRIS EVANS—So \$10 million is neither here nor there for you, Mr Roach—is that right?

Mr Roach—No, it is all very important.

Senator CHRIS EVANS—A drop in the ocean!

Mr Roach—But multiplying the categories by 10 does not help to manage it.

Senator CHRIS EVANS—It seemed to me that, on previous years, you were looking to save \$20 million out of \$110 million, which is a pretty big call. Maybe I have got it wrong, but it seemed to be quite a huge saving on travel that you were going to make.

Mr Roach—\$110 million is not a figure I recognise, Senator.

Senator CHRIS EVANS—Just looking back at previous years, when we had a bit more information in the budget papers, it looked to be about \$110 million. If you think that I am way out then please tell me. My point is that it seemed to me that you were being asked to save \$20 million out of a budget of that order. If I am wrong and it is \$1 billion, then I will take your point that it is not much.

Mr Roach—I will give you the figures for 2000-01, which is the completed year before. Total travel—both domestic and overseas—for deployment, operations, and everything else was about \$240 million.

Mr Bennett—I cannot quote on the absolute magnitude, but the savings are achieved through contractually negotiated rebates on travel et cetera. So I am pretty confident that the numbers are correct. It is not just an estimate.

Senator CHRIS EVANS—It will be pretty hard to get a rebate when there is only one airline.

Mr Bennett—It depends when you negotiated the contract.

Senator HOGG—I was curious about that, because I thought that the airline agreement was renegotiated a couple of years ago. Is it renegotiated annually?

Mr Bennett—I would have to check on when the contract was last negotiated.

Senator HOGG—It seems that every year I have turned up at estimates there has been some sort of statement made that they are going to keep saving money in travel. I know you have a good bargaining chip, but I wonder where it will end. In terms of the savings that you have just been outlining to the committee, where can the committee see that these savings have actually been made? Where can we verify that the savings have been made or how will you verify to us that the savings have been made in the future? The annual report is the obvious place, but it might not necessarily have a line item which will say, 'We said we would save this; we have, and this is how we can prove we have made the saving.' How will you satisfy the committee?

Mr Roach—We would look to provide that explanation in the annual report.

Senator HOGG—That is part of the problem. I think it is difficult to get those explanations to stand out in the annual report. You say you will save \$100 million, then you go to the annual report and say, 'We were right. We saved \$100 million.' That is fine, but we have no way of testing that you have done what you set out to do. We cannot look at the figures. We cannot say, 'Yes, that was ticked off there. Yes, there are savings of \$100 million.' Is there some way you can assist us in understanding how the savings will be made?

Mr Roach—We would be looking to satisfy you that we had done what we said we were going to do. If we were not able to do it, we would want to be able to explain why.

Dr Hawke—I would be surprised if Treasury or the department of finance did not seek to reassure themselves that we had done that.

Senator HOGG—I would too.

Dr Hawke—We are happy to take that point and report against that in the annual report.

Senator HOGG—It is so that you have it in a language and a form that is easily and readily understood by us.

Senator CHRIS EVANS—Can someone tell me what rebasing of budget group allocations means?

Dr Hawke—Taking money off them.

Mr Bennett—We looked at the actual achievements in the previous year—

Senator CHRIS EVANS—Dr Hawke, I would prefer it if you explained it to us.

Dr Hawke—That is exactly right. We look at their achievements against budget in the previous year. Where they have not achieved, they need to make a very good case about why they could not live with that budget plus any ons and offs in the following year. I have never been surprised, whenever we ask people in the organisation if they want additional money, that they always seem to have a list of reasons about why they would like that. They are not too good at coming back and saying, 'Here are areas where we would like less money.'

Senator CHRIS EVANS—So, by putting the wood on them, you reckon you have found \$69 million?

Dr Hawke—It is basically the pattern of their spend. That is what they have spent over the period. So what is it about that?

Senator Hill—We do not want to penalise them for being prudent.

Senator CHRIS EVANS—I am trying to understand how it works. Is that an ongoing saving?

Dr Hawke—It can be.

Mr Roach—It would depend on its nature. The difficulty is that in all of this work we are constantly looking to harvest what we can and to redeploy it to the priorities that we have. It is not a simple exercise to look at, for example, employee or suppliers expenses and to see the ons and the offs, because we might well be able to harvest and underspend in suppliers there and give it to another group that has a priority in suppliers expenses. At the end of the year you would see no impact in that particular case, but we would certainly have moved money around.

Dr Hawke—These allocations are worked on by the chief financial officers organisation, in concert with the single services and the groups, and they then come up through the Defence Committee for consideration by CDF and me. At the end of the day, as the officer accountable, I sign off on them.

Senator CHRIS EVANS—All right. Could someone explain to me the \$10 million saving from advertising and recruitment? That is out of a total budget of what, and where is the line item for that?

Mr Roach—There is no line item in the PBS for advertising. We spent \$40 million in 2000-01. DPE have the figures for this year. I think it is around \$35 million.

Senator CHRIS EVANS—For 2000-01 the budget for advertising was \$40 million?

Mr Roach—That was for 2000-01. This year it was \$35 million, and \$10 million was removed from that at additional estimates. We have taken \$10 million from the planned budget for 2002-03, so that is now down to about \$25 million.

Senator CHRIS EVANS—So what you are telling me is that last year's budget was \$40 million, this year's will be effectively \$25 million and next year's will be \$25 million?

Mr Roach—Yes, in round figures.

Senator CHRIS EVANS—Effectively, the \$10 million that was taken out at additional estimates has been repeated for the next financial year?

Mr Roach—Just for the next financial year.

Senator CHRIS EVANS—When you say that is the advertising budget, is that the recruitment and advertising budget or just the advertising budget? I just want a proper definition of what we are talking about here.

Mr Roach—It is the total advertising budget.

Senator CHRIS EVANS—Does that mean that Navy, Army and Air Force have a separate advertising budget in addition to this one, or is this the global?

Rear Adm. Shalders—The \$35 million this year is across the three services. There is not a separate split. Of that \$35 million, \$25 million is for media purchase, \$5.6 million is for the agency retainer and advertising development, \$0.9 million is for research and \$3 million is for branding activities conducted by public affairs and corporate communications.

Senator CHRIS EVANS—That is \$35 million, but I just got told you only had \$25 million.

Rear Adm. Shalders—\$35 million was the budget for this year.

Senator Hill—But we cut it back by \$10 million in the additional estimates process.

Rear Adm. Shalders—We did, and of course the year is not complete yet. But a lot of the commitment that we had made, the media purchase, was unable to be retracted, so the final figure for this year is likely to be around \$35 million.

Senator CHRIS EVANS—As someone who watched the second and third cricket tests with my son, if I saw another Defence Force recruitment ad I was going to scream. I figured you had been buying a bit. I know you obviously targeted the cricket market. It worked: it got me, but I didn't join up.

Senator WEST—They are now doing the rugby league.

Senator CHRIS EVANS—Instinctively, I thought it would be surprising if you had spent less this year, given what I had seen of the media buy. You spent \$25 million on media buy?

Rear Adm. Shalders—That is correct. It was \$25.7 million.

Senator CHRIS EVANS—\$5.6 million is—

Rear Adm. Shalders—Agency retainer and advertising development.

Senator CHRIS EVANS—That is effectively what you pay the agency, is it?

Rear Adm. Shalders—Correct.

Senator CHRIS EVANS—There is \$0.9 for research and \$3 million for branding?

Rear Adm. Shalders—That is Public Affairs and Corporate Communication Division below the line recruiting activities, such as recruiting vans to various shows—that sort of activity.

Senator CHRIS EVANS—So that is not for further media buy for general Defence? It is branding.

Rear Adm. Shalders—No; that is general Defence branding.

Senator CHRIS EVANS—Not a media buy as such?

Rear Adm. Shalders—No.

Senator CHRIS EVANS—So your media buy is still at \$25.7 million. Is the reserve campaign that has just been kicked off a part of that or is that funded separately?

Rear Adm. Shalders—That was part of the \$25.7 million this year.

Senator CHRIS EVANS—So the campaign that has just started on the mass media for the reserve recruitment is part of that global figure?

Rear Adm. Shalders—That is correct.

Senator CHRIS EVANS—How much has been allocated for that?

Rear Adm. Shalders—I do not have that figure with me. I will have to take that on notice.

Senator CHRIS EVANS—I would appreciate that. I presume that won't be much in this year because it has only just been launched, hasn't it?

Rear Adm. Shalders—That is correct. That campaign was launched on 25 May so that will be less than five weeks worth of media placement this year.

Senator CHRIS EVANS—In any event, I can take it that that is part of the \$25.7 million—a subset of that.

Rear Adm. Shalders—That is correct.

Senator CHRIS EVANS—How does it work, then, if the government announces a \$10 million cut in advertising but the money is spent anyway?

Senator Hill—That is a very good question.

Senator CHRIS EVANS—I thought that was why you wanted me to ask it.

Senator Hill—Well, the \$10 million is going to be saved because it has been taken out of the budget, so something has suffered by \$10 million.

Mr Roach—If the money is committed and not saved we will have to find it elsewhere.

Senator CHRIS EVANS—I am sure that is right. I am sure the minister will insist on that, too. But why would you put it in the additional estimates budget statement if it clearly is not going to happen?

Senator Hill—It would not have been put in unless we were assured it could be saved from this year.

Dr Hawke—It is not a very good performance to have signed up for the \$10 million saving and then for the minister to find out that the \$10 million has not been saved in this way. So somebody will be doing some explaining about it.

Senator CHRIS EVANS—Is anyone able to help us today as to how that works?

Dr Hawke—I think we will have to go away and have a look at it.

Rear Adm. Shalders—I could perhaps help, partly. A lot of the media buy is long-term placement. A lot of these funds are committed sometimes in excess of six months ahead, for example for particular sporting events, as you have indicated. In some cases where those long-term commitments are made, it would cost us more to back out of the commitment than it would to proceed. So part of the explanation is in relation to the long-term commitment of funding.

Senator CHRIS EVANS—Do you have a particular media buy strategy, Admiral Shalders? I know from having to pay for political advertising that, one, it is expensive and,

two, buying in things like the cricket obviously comes at a significant premium because of the ratings. So obviously you would have bought, say, the cricket packages as part of a media strategy?

Rear Adm. Shalders—Yes. There is a very definite strategy. It is based upon the target audience that we are hoping to attract. You get more people watching the cricket or the football than you do some lesser sporting events. We therefore target the audiences that form part of our potential recruitment pool. There is a very specific strategy that we use.

Senator CHRIS EVANS—I presume your target audience is young men and women aged between 17 and the late 20s.

Rear Adm. Shalders—Age 17 to 24 is the general target audience, but of course we are attempting to attract people of older age groups than that, too.

Senator CHRIS EVANS—Yes, but not quite as old as me. Your advice from the agency is that those sporting events are your best buy in terms of targeting those audiences—is that right?

Rear Adm. Shalders—We take advice on where the best advertising result is going to come from. That advice is based on significant research that is done by the recruiting organisation. It is a very targeted, very measured campaign that we are conducting.

Senator CHRIS EVANS—Who is the agency at the moment?

Rear Adm. Shalders—There is a variety of agencies. I can give you a list of the different agencies that we use. The agencies of course are contracted through the government media communications committee.

Senator CHRIS EVANS—But you use more than one agency, do you?

Rear Adm. Shalders—There is more than one agency, yes.

Senator CHRIS EVANS—Do you have a master agency that controls the strategy?

Rear Adm. Shalders—Not really, no; it changes. I can give you more detail on that on notice.

Senator CHRIS EVANS—I appreciate that. I am just trying to understand. I know you might spread the work around in some senses, but I thought you would have someone managing your recruitment strategy and your advertising project for that. However, you say you use a variety of agencies.

Rear Adm. Shalders—The agencies change, and they change over time. Again, I can give you further details of the agencies we used over the last five years if that would assist.

Senator CHRIS EVANS—I would appreciate that.

Rear Adm. Shalders—I have just been advised that the overall costs of the Reserve recruiting campaign will be \$2.5 million. That will be spread over the current financial year and the next financial year.

Senator CHRIS EVANS—I can assume the majority will be in the next financial year.

Rear Adm. Shalders—That is correct.

Senator CHRIS EVANS—What was the media buy last year, not for the reserves but the global advertising recruitment budget?

Rear Adm. Shalders—I do not have those figures with me.

Senator CHRIS EVANS—Perhaps you can take that on notice.

Mr Roach—If you are after the 2000-01 figure, that was last financial year, the figure for all advertising was \$44.8 million.

Senator CHRIS EVANS—Do you know what the media buy component was?

Mr Roach—No.

Senator CHRIS EVANS—I thought the budget was \$40 million.

Mr Bennett—We mentioned a figure of \$42 million variously for advertising and market research.

Senator CHRIS EVANS—So the budget for 2000-01 was \$42 million and you spent—

Mr Roach—The achieved expense for 2000-01—the end of year figure, the 30 June figure—was \$44.8 million. It is different from the budget.

Senator CHRIS EVANS—You budgeted for \$42 million but you spent \$44.8 million in 2000-01. Is that right?

Mr Bennett—We will double-check those numbers for you.

Senator CHRIS EVANS—We budgeted \$25 million for 2001-02. What is that total now?

Rear Adm. Shalders—We expect it to be \$35.2 million this financial year.

Senator CHRIS EVANS—And the budget is \$25 million for the whole of the next financial year.

Mr Bennett—Yes.

Senator CHRIS EVANS—Do we have budgets for the out years broken down for the advertising as well?

Mr Roach—No.

Senator CHRIS EVANS—That figure of \$35.2 million represents the total expenditure by Defence, Army, Air Force and Navy. Someone suggested to me at one stage that there might have been some separate campaigns in the past, but this is all handled centrally by Defence now, is it?

Rear Adm. Shalders—That is correct, by the Defence Force Recruiting Organisation.

Senator CHRIS EVANS—So there is no separate force expenditure on those other recruitment initiatives or advertising?

Rear Adm. Shalders—No.

Senator CHRIS EVANS—And how much of the campaign is branding rather than direct recruitment?

Rear Adm. Shalders—It is a difficult question you ask, of course, because even if we are advertising for a particular service it will impact on the overall ADF brand. If it would be helpful, I could split the current media buy into the various forms of advertising, the various media, that we use. Would that assist you at all?

Senator CHRIS EVANS—Yes, it might help to give me an indication.

Rear Adm. Shalders—For example, for television alone in this financial year, up until March this year, out of a total of \$12 million, triservice was \$3.8 million, Army \$3.6 million,

Navy \$2.9 million, Air Force \$1.7 million, and equivalent splits in the various other media outlets.

Senator CHRIS EVANS—Is that driven by recruitment needs or relative sizes or the fight among the chiefs?

Rear Adm. Shalders—It is driven by the recruitment requirements, the targets that are needed. We work carefully, of course, to try to analyse where our shortages are and we target those shortages specifically with advertising—by medium and by service.

Senator CHRIS EVANS—Has there been much change in the approach either in the split or in the direction? It looks as though you have put a large proportion of it into TV. Has that been standard for a few years now?

Rear Adm. Shalders—The proportions are very similar. Has there been a change over the years in the proportions to each service? The answer is no. I can go back to 1999-2000 and the figures I just gave you. In that year, we spent \$21 million on television advertising—\$8.8 triservice, \$8.3 Army, \$2.7 Navy and \$1.6 Air Force.

Senator CHRIS EVANS—Did you actually spend more in 1999-2000?

Rear Adm. Shalders—We did—about \$9 million more, in fact.

Senator CHRIS EVANS—I presume that means your total advertising budget was much larger then?

Rear Adm. Shalders—It was larger by about \$10 million three years ago, yes.

Senator CHRIS EVANS—What was it for the 1999-2000 year?

Rear Adm. Shalders—The total media budget for that year was \$29 million.

Senator CHRIS EVANS—And the total advertising budget?

Rear Adm. Shalders—I am sorry, I do not have that figure for 1999-2000. I will obtain that for you.

Senator CHRIS EVANS—Do you have that figure, Mr Roach?

Mr Roach—Yes, I do. The total advertising expense recorded for 1999-2000 was \$35.7 million.

Senator CHRIS EVANS—So it was actually less in the following year?

Mr Roach—Yes.

Senator CHRIS EVANS—But there was obviously a huge concentration on TV that year.

Rear Adm. Shalders—That year \$21 million out of the total was spent on television.

Senator CHRIS EVANS—Do you have an explanation for that, Admiral Shalders?

Rear Adm. Shalders—I think in 1999-2000 the start of our recruiting difficulties occurred. That year was the start of a dip that we are now emerging from. My guess is that we were starting to experience shortages and therefore we were focusing on recruiting.

Senator CHRIS EVANS—Threw some money at the TV, basically, to try to arrest the problem?

Adm. Barrie—I think it was the operational tempo that really focused the enduring effects of a failure to recruit over many years, and I think that led to a higher priority for trying to solve that problem.

Senator WEST—We had had full recruiting, as I recall, two years earlier. We had actually returned money from the advertising budget to the central kitty in about 1997-98.

Adm. Barrie—But in 1999 we began the operation in East Timor and all those other things, so all of a sudden there were real pressures on providing the people we needed to support the op tempo.

Senator CHRIS EVANS—Your explanation, Admiral Barrie, is that there was a renewed emphasis on the need to bump up the recruiting effort and therefore the advertising budget followed?

Adm. Barrie—Yes. I am not saying that it is all one or the other; I am just saying that a combination of factors put a lot of pressure on our recruiting effort.

Senator WEST—I seem to recall that somebody, in the evidence either here or in the inquiry we did, admitted to taking the eye off the ball.

Adm. Barrie—The consequences of turning off the recruiting tap in any year actually linger on for quite some time. It is much easier to turn off the tap in order to achieve a budgetary outcome, but trying to turn it back on again is a lot harder. One of the problems of consistent downsizing over the last 20-odd years has been exactly that consequence.

Senator CHRIS EVANS—I accept that. I suppose that raises the point, though, that we have gone from a budget of about \$45 million to a proposed budget for next year of \$25 million. We are facing a significant fall in our advertising recruitment budget next year.

Adm. Barrie—That is potentially true, but it is related to the effectiveness of the campaigns, I suspect, as well.

Ms McKenry—Senator, you asked about the emphasis on advertising. What has happened with the \$3 million Admiral Shalders talked about is that this year we have been looking at a pilot move away from expensive advertising to what we call some 'below the line' advertising to target young people. We have produced a range of interactive CD ROMs which are targeted at young people along with videos and a range of other activities—editorials in youth newspapers, and a contract for the production of a schools kit aimed predominantly at secondary aged students that is about what Defence does. It aims to get young people thinking very early on about the role of Defence within our community and a possible career in Defence. So there has been an attempt to look at alternatives in order to be able to cope with a reduced budget.

Senator CHRIS EVANS—There is a broader issue, which Admiral Barrie raised, about effectiveness. I have been responsible for some political advertising that cost a lot but did not win us many votes. What sort of assessment procedures are in place to make sure what you are doing is actually driving recruitment?

Rear Adm. Shalders—We watch that very closely. I am pleased to say that the effectiveness of the current campaign is such that we are getting closer to reaching our targets, which have increased over the years, than we have for probably the last four years. Within Army, for example, we are currently running at 94 per cent target achievement. We have not been that high for a very long time.

Senator CHRIS EVANS—Obviously the question is this: is it the recruitment advertising that is driving that or is it the increased awareness of war? Clearly this is a complex question. I am trying to understand what work you do on that and how you try to analyse what works and what does not work for you. Otherwise, on the face of it one could argue—and I do not

argue this—that if you are going from a budget of \$45 million to \$25 million next year you are going to have trouble with recruitment.

Rear Adm. Shalders—I do not think the relationship is quite that linear. Obviously it is a complex problem, as you said. The advertising has played a part in our improved effectiveness in recruiting; as have some process changes that we have made within the recruiting process—the support we have been able to provide to recruiting and the people we have been able to allocate to the job. There is a host of factors; and, yes, we do try to analyse and understand them.

Senator Hill—Greater emphasis on personnel issues probably played a part and an increasing level of operations almost certainly has played a part.

Senator CHRIS EVANS—What process do you have for analysing that or making judgments about that? Is there an assessment process? Are there surveys? I know you do surveys of recruits and how they were attracted. What work have you done to test the effectiveness of your advertising campaigns and various approaches?

Rear Adm. Shalders—One of the rawest measures but one that does suggest to us that we are doing better is the ratio between inquiries, applications and enlistments. The number of inquiries we get each year is very high, as you would imagine. Turning that into applications and then enlistments is a measure of various parts of the process. As a very rough measure, the ratio between inquiries and applications has improved in the last 12 months from 20 per cent last year to almost 25 per cent this year. That is a raw measure of the effectiveness of part of the whole process and part of the advertising campaign.

Senator PAYNE—Do you do any spot checks for people who do not go step 1, step 2, step 3? For example, I took a tour through the recruiting office in Parramatta, which is in the building where my own office is housed. I was very impressed with the personnel who worked there. They are very engaging and very positive about the approach they take to people who come in off the street and make separate and specific appointments. We talked through the inquiry application recruitment figures, but I was not sure what level of follow-up they did to perhaps identify why people do not take the next step.

Rear Adm. Shalders—Probably not as much as we should, and that is a sheer function of resources. Being able to follow up and do that follow-through is time-consuming, as you would understand. For example, last year we had 116,000 inquiries; if we had tried to follow up every one of those it would have been very resource intensive.

Senator PAYNE—I understand that.

Rear Adm. Shalders—It is something we are conscious of, though, and we are trying to move down that path in the future.

Senator PAYNE—I believe you said to Senator Evans that your ideal age range was 17 to 24, but one of the points that was made to me in the Parramatta office was that there is in fact a broader interest. They had just recruited a woman in her late 40s who had gone in as a driver in the Army. For her it was a very significant career move and they felt it was a useful investment of time and effort from the recruiting process. I wonder if that was an exception or if there are more examples like that.

Rear Adm. Shalders—There are examples at both ends of that scale. For those younger than 17, we need to start perhaps not enlisting but certainly attracting—

Senator PAYNE—We cannot take them out of the schools yet, Admiral!

Rear Adm. Shalders—them at a younger age and then building on that interest as they get to the age for enlistment. For the older age group we have just increased the upper age limit. We are now routinely getting recruits well over the age of 30, for example in the Navy, joining their 17-year-old compatriots.

Senator PAYNE—There is hope for us yet, Admiral, meaning this side of the table. If you could pass on my thanks to the Parramatta recruiting office for their courtesy and hospitality, I would be grateful.

Senator CHRIS EVANS—I do not want to drag us off into the personnel area; I am more interested in the advertising budget issues at the moment. I am conscious that the chair will chastise us about sticking to the right outputs; I am sorry, Admiral Shalders, I had a bit of a break-out. Coming back to the commercial support program and the projects listed in table No. 4.2 on page 96: is there an indication of what savings are expected to be made from these activities?

Mr Roach—If you are asking whether we have an estimate of the savings at the moment, the answer is no. We have been very successful in all our commercial support: the long-term average saving from the initial benchmark is around 30 per cent. We are conscious that as we have moved into more specialised areas for market testing the savings have been a great deal less in some instances than that, but until we get the tenders in and evaluate them we are really not in a position to say.

Senator CHRIS EVANS—But one of the drivers of the commercial support program is the savings to Defence, isn't it?

Mr Roach—That is one of the drivers, yes.

Senator CHRIS EVANS—That is one of the rationales, but for these commercial support initiatives you actually do not have targets or budgeted savings for these measures?

Mr Roach—In terms of our budget, no, not at this stage, not for new initiatives.

Senator CHRIS EVANS—So are there targets that are not reflected in the budget? Internally—I am not necessarily even asking you for them, though I might try that as the next question—have you got a target for the program: for instance, for the health services?

Mr Roach—Not at the portfolio level, unless it was something that was still part of DRP, but we would certainly look to these sorts of activities to contribute to the savings that we are required to make under the white paper. We have got a generic target for savings and efficiencies that we have to make across the portfolio as a whole, but we do not have targets for individual initiatives at least at the portfolio level.

Senator CHRIS EVANS—What about for the DID system? That is due to come in this next financial year too, isn't it?

Mr Roach—It is. There may be an estimate. I would have to check and see.

Senator CHRIS EVANS—Is that in the budget or not?

Mr Roach—I would have to check.

Major Gen. Haddad—With the DIDS project we have got a 30 per cent target, as was identified before. I could not tell you whether that is in the Defence budgetary process or not, but it is the notional target of all our outsourcing activities.

Senator CHRIS EVANS—Notionally the DID system should deliver you a 30 per cent saving?

Major Gen. Haddad—That is the target we are aiming for.

Senator CHRIS EVANS—I think that is handballed back to you, Mr Roach, is it, in the Defence budget or not?

Mr Roach—It is not as simple as identifying a line of numbers.

Senator CHRIS EVANS—Nothing is, and if you say accrual accounting I might well leap over the table at you!

Mr Roach—It has nothing to do with accrual accounting. The single biggest reinvestment that Defence has made since the Defence Reform Program is effectively in putting people back into the combat force of the ADF. The services have their planned strength targets from the white paper. You heard before that the Army's, for example, is 26,000. As a result of this budget, it will now be a little bit higher because of the TAG and the IRR, and our ability to move people in that direction depends, in part, upon our achievement of savings from things like DIDS.

Senator CHRIS EVANS—But you do not have a budget line item?

Mr Roach—Is there a single row of numbers which represents savings from activity X? No, not in the budget as a whole.

Senator CHRIS EVANS—But it would be fair to say that whatever DIDS costs you now—less 30 per cent—is where you hope to get to?

Mr Roach—It is certainly where we hope to get to.

Senator HOGG—Is it 30 per cent in the first instance that you hope to save on the commercial support programs? Are you expecting to save 30 per cent again the second time they are up for tender or is it going to be substantially less? The reason I ask that is that I would expect there are a number of those commercial support programs that arose out of the DRP that you referred to which would be up for renegotiation now. Are you expecting to save 30 per cent on those when they are renegotiated or are you expecting a lesser saving?

Mr Roach—I would not like to speak for the people who are actually managing the areas.

Senator HOGG—I am not trying to pin you down—in the broadest sense?

Mr Roach—In the broadest sense I would make two observations. The first is that, as we have moved the commercial support program into non-traditional areas and areas that are not subject to a great deal of competition, the savings have been less than the 30 per cent. I would also not expect to achieve the sorts of savings that we achieved first time round when we re-compete for major contracts.

Senator HOGG—Could I put this question in the broadest sense—there is no trick in it. Would you expect the second time around that, because there might be a lack of competition or you may well find that it is such a specialised skill, the costs have gone up rather than gone down compared to what you would have achieved if you had retained it in-house. Is there anything to test that?

Mr Roach—I do not know. We would obviously have to see how the experience was. Obviously for those things that do not have a natural market we need to have other sorts of protections and benchmarks.

Senator HOGG—Yes. I will speak in broadest terms. These are the sorts of things. Category X in the Navy used to perform a certain task and a certain duty. It went to commercial support. These people left the Navy and went over to the commercial support

program. Whilst that may well have saved Navy money in the first instance, in the longer term that is not necessarily going to be the case, because you have now got the pool of skilled persons with the commercial support supplier basically dictating the terms to Navy. I do not know if that happens.

Mr Roach—I think we will have to wait and see.

Senator HOGG—Yes, I accept that.

Senator Hill—It depends on the level of competition within the private sector as well for the particular type.

Senator HOGG—Yes. That is the cause for concern, though, Minister. That is why I raise it. I do not want to get down to a specific program here and now. Just in the broadest sense, some of the savings that may well appear to be there on the surface in respect of the commercial support program might not necessarily materialise in the longer term.

Senator CHRIS EVANS—Mr Roach, the additional estimates statement released in February included a \$60 million deferment of capital equipment projects in 2001-02. That was used to fund part of the war on terrorism. What happened to the \$60 million?

Mr Roach—It was rolled over into 2002-03 and forms part of the defence capability plan in 2002-03.

Senator CHRIS EVANS—Where do I find that?

Mr Roach—It is not actually visible in this PBS because it is not a measure for this PBS.

Senator CHRIS EVANS—So when I could not find it I was right: it was not there. It is just absorbed back in.

Mr Roach—It is implicit in our financial statements, but because it is not a measure in this budget it is not shown. It was shown at AEs.

Senator CHRIS EVANS—All right. But wouldn't you have to show the rolling over of the \$60 million?

Mr Roach—I do not have the AEs with me.

Senator Hill—Didn't the additional estimates show it being deferred to the next year?

Senator CHRIS EVANS—Yes. Then I went to look for it here and I just did not see it.

Senator Hill—Because it is deferred for the next year and it is not again deferred in this budget, it means we expect to spend it this year.

Senator CHRIS EVANS—So I should be able to find \$60 million more in total in the capital budget in this year's budget papers than last year's for this coming financial year—is that right?

Senator Hill—If it had been deferred again, then it would have been in addition to the sum that was deferred from this year. In effect, it is absorbed within that, so it is not being double-counted. I am only trying to explain the accounts, as I understand what is being said. It does not appear as a new measure this year because it does not need to, because it appeared in additional estimates as only having been deferred for one year. It is not as if it was lost forever.

Senator CHRIS EVANS—Maybe it is my naivety. I would have thought it would have shown up at least as a net additional \$60 million on your budget for this year because at the time of the last budget you were not going to get it this year.

Mr Roach—I am not as familiar with the accounting for 2001-02 AEs; I wasn't here doing this job at that point. The \$60 million that was taken out of the DCP in 2001-02 as an offset for the new ops is most definitely in our budget for 2002-03.

Senator CHRIS EVANS—Unless it is part of the \$150 million that has been deferred to the following year.

Mr Roach—There is \$4.72 billion in our capital budget for this year. It is all part of that.

Senator CHRIS EVANS—I was just trying to find the \$60 million that was deferred. You are telling me it does not show up in the budget papers but it is there?

Mr Roach—It is part of that capital budget number.

Senator CHRIS EVANS—Can someone tell me which particular project was deferred—what that \$60 million represents?

Mr Roach—As with the \$150 million, a lot of projects have had some adjustment to their planned spend. In terms of the \$150 million, it is not just one project. There are a lot of adjustments.

Senator CHRIS EVANS—So I cannot look to find that \$150 million and say, 'That is the purchase of three tanks that have been delayed by a year'? This is a sort of global net figure from all your capital movements, is it?

Mr Roach—Table 3.4 on page 63 sets out the capital budget and the purchase of specialist military equipment, which is budgeted for a bit under \$3.6 billion. If we had not needed to find the offsets for the new operations, that number would be \$150 million higher.

Senator CHRIS EVANS—Which number is the relevant number—the \$3.586 billion?

Mr Roach—Yes. In practical terms, that \$150 million represents slipping the spend and the schedule for quite a number of projects, unapproved projects, for just a couple of months. One of the projects has a slightly longer slip. It is a whole lot of small adjustments as opposed to—

Senator CHRIS EVANS—One big?

Mr Roach—Yes.

Senator CHRIS EVANS—How does it work? Surely you have contractual arrangements with these people about payment?

Mr Roach—No. The \$150 million is coming out of the unapproved part of our capital budget; that is, things that we planned to start in 2002-03. We have pushed some of that money into 2003-04.

Senator CHRIS EVANS—By 'unapproved' you mean uncommitted, in a sense?

Mr Roach—Yes.

Senator CHRIS EVANS—It is not something that you are liable for in the detail?

Mr Roach—It is coming from projects that have not yet been approved by government. We are not in contract for those projects.

Senator CHRIS EVANS—But they are projects for which contracts will be signed off on in this financial year and, effectively, in signing those off you will let them slip a bit over what you originally planned to do. Is that it?

Mr Roach—There is usually quite a hurdle between government approving the project and when a contract would be signed. It depends upon how the project has been developed and at what point it has been brought forward for government approval. I could not tell you how many of these would be planned to actually have a signed contract in 2002-03. Normally it would take more time than that.

Senator CHRIS EVANS—But you would not be spending the money if you had not signed the contract, surely.

Mr Roach—For money of this magnitude there will clearly be some starts and some real progress, but for a lot of projects in their first year we are actually entering into contracts rather than actually entering production.

Senator CHRIS EVANS—But what you are telling me is that we need not worry about the \$150 million because you are going to buy the same basket of goods with that money but you are going to pay for it later; it is not impacting on particular purchases. I am just trying to understand how that works. You are saying to me that we will actually pay for a range of things later than we would otherwise have paid for them. Is that fair?

Mr Roach—I distinguish between the issue of our ability to make payments when we are required to and the schedule for these projects. We are actually slipping the schedule for a relatively large number—I could find the number for you if you want it—of the unapproved projects. One of the projects we are slipping for a slightly longer period of time, but again it is not more than six months.

Senator CHRIS EVANS—And what project is that?

Senator Hill—We have some tentative internal assessments of individual projects, but at this stage I do not think we would really want to put them on the public record. We believe, consistent with what is being said, because we are at the front end of this long period of procurement, we can achieve this deferment without any significant loss either in timetable or the content of the defence capability plan when looked at over the period of that plan. When government considered a deferment of this sum of money for this year, officers provided to it some initial assessment of exactly how it might relate to specific projects. I do not think we are actually, as yet, bound to any of those assessments and, at this stage, would prefer it to be treated as an internal working document.

Senator CHRIS EVANS—But you are saying that it will impact on the timing of certain projects?

Senator Hill—I do not think it will impact on what the admiral says was the in-service state of the equipment, because we are talking about the front end of often quite long projects. It might surprise you, but some even argue that it might turn out to be a blessing in disguise.

Senator CHRIS EVANS—I thought that is what you were arguing earlier—

Senator Hill—It means that in some instances there is a little more planning up front, and you might suggest in relation to some contracts in the past there should have perhaps been more planning up front.

Senator CHRIS EVANS—Dr Hawke earlier advanced the argument on the \$150 million deferral that it was partly tied up with the review of the capability plan as well. I am not trying to verbal you.

Senator Hill—Later this year, the government having decided to defer that sum of money, the government will have to determine what if any changes will need to be made to the defence capability plan in terms of the timetables.

Senator CHRIS EVANS—You mean what the deferment might mean for the defence capability plan, what impact the deferment has on the defence capability plan or whether a changed defence capability plan might make you want to choose different purchases or purchase priorities?

Senator Hill—We think there will be some finetuning of the plan in terms of capability arising from the matters that come out of our review of the strategic environment. That is why we are doing both projects together later this year. We have started them now, but we will deliver them to government later this year. But that is really a separate issue to what I am talking about. The plan was an attempt to put down a very detailed timetable—numbers attached to individual years—and it was always appreciated that it would necessarily be modified as time goes on, as we get better figures on the cost of particular projects, get a more accurate appreciation of the time lines. That is why it was indicated in the white paper that there would be this annual review of the defence capability plan. What I am saying to you is that the government's view is that we can achieve the deferment of this sum of money this year without having any significant effect upon either the time lines or the capability that is set out. Certainly there will be modifications because of the extent to which the projects were detailed in the plan in the first instance.

Senator CHRIS EVANS—So what we might be looking to get out of the capability plan might have changed? What we were looking to purchase or prioritise might well have changed as a result of the review?

Senator Hill—There may be some changes, but when you look at the size of the procurement program as a whole I am not expecting substantial change, particularly bearing in mind the decisions that the government has already taken and funded arising from the terrorist event of September 11. As we have discussed today, we have already written in the increased counter-terrorism capability, the Incident Response Regiment and the extra guarding of bases. I do not think we have discussed it today, but we have written in enhanced intelligence. The ships in the Gulf have taken up some of the new communications equipment in advance. There have been modifications already because we could not afford to wait. In some ways, the review this year is catching up on the reality, as well as refining the plan for the future.

Senator CHRIS EVANS—Dr Hawke, on page 100 of the portfolio budget statements, it looks as if your balanced scorecard project evaluation is somewhat in doubt. It says, 'Development is subject to resources being available.' What do I take that to mean?

Mr Neumann—The Defence Audit Committee gave a higher priority to the other ones that are listed. We have the resources to do only three a year.

Dr Hawke—It is not the balanced scorecard project; it is the evaluation of it that was not given as high a priority by the audit committee as some of the others.

Senator CHRIS EVANS—Does that mean the balanced scorecard project will go on?

Dr Hawke—Yes.

Senator CHRIS EVANS—Will it be unevaluated?

Dr Hawke—No. It just means that that has a lower priority. We will certainly be evaluating it. We look at this issue each month and we have, over a period of time, finetuned it. There is no doubt that this evaluation will go ahead. The question is whether or not it will go ahead this calendar year. It might be a 2003 evaluation.

Senator CHRIS EVANS—That is because of the limited resources.

Mr Neumann—It is the evaluation resources that are limited, not the scorecard itself.

Senator HOGG—So the scorecard is proceeding?

Dr Hawke—Yes.

Senator HOGG—It was described in the annual report as a tool to start communicating Defence's internal business strategy. How effective has this been?

Dr Hawke—It is getting better. It reveals to us internally how things are going and where remedial action is required. The Defence Committee looks at this on a monthly basis. We are still refining it and probably will be for the next 12 months or so.

Senator HOGG—What are the mechanisms for monitoring the effectiveness of the scorecard?

Dr Hawke—The evaluation will be—

Senator HOGG—Is the evaluation available?

Dr Hawke—It has not been done yet.

Senator HOGG—No, when it is done.

Dr Hawke—Yes, when it is done; they are normally publicly available documents.

Senator HOGG—Is the balanced scorecard a regular item at your senior management meetings?

Dr Hawke—Every month.

Senator HOGG—Does it get shoved to one side from time to time?

Dr Hawke—No, it is on the agenda every month.

Senator HOGG—It is something you have embraced, Dr Hawke; we are interested and wish to be assured that it is up and running and functioning.

Dr Hawke—Yes, it is. We rotate: one month we put more focus on this than the next month, because every second month we normally look at some of the bigger strategic issues as part of the Defence Committee meeting—Air 6000 and those sorts of issues.

Senator HOGG—You have a great enthusiasm for this, which I can understand.

Dr Hawke—But it is an enthusiasm not necessarily for the balanced scorecard; it is an enthusiasm for evaluating what we are doing and how we are going.

Senator HOGG—I accept that. Do most of your colleagues share the same enthusiasm for the balanced scorecard as you have?

Dr Hawke—I think you would have to ask them.

Senator HOGG—What is your view of their enthusiasm?

Dr Hawke—When I was in the Department of Transport and Regional Services we used an evaluation program called ‘Investors in People’. The reason the balanced scorecard is more appropriate for Defence is that at least one of the services and a couple of the groups already had a form of the balanced scorecard for their own measurements. So, rather than bring in something different, it seemed that we should build on the work that had already been done in Defence. That was discussed among the senior leadership and it was agreed that was the route we would pursue.

Senator HOGG—But you have detected no resistance to the spreading of the balanced scorecard within Defence at this stage?

Dr Hawke—No, I do not detect any resistance. I do not think we are there yet. We need to refine some of the measures and we need to make sure that we are focusing on the key issues that will drive behaviour and corrective mechanisms, where they are necessary. These things can tend to develop a life of their own. So how you focus on the key issues that actually make a difference to the way in which you manage is what we are pursuing.

CHAIR—Are you finished, Senator Hogg?

Senator HOGG—Yes.

Dr Hawke—Mr Chairman, we have the further information for Senator Faulkner, if you would like to do that.

CHAIR—Thank you, Dr Hawke. We will get Senator Faulkner back after the break.

Proceedings suspended from 3.33 p.m. to 3.53 p.m.

CHAIR—I understand Dr Hawke has some responses for Senator Faulkner?

Dr Hawke—Yes. We have tabled the correspondence that Senator Faulkner was seeking. There is a small addition to what Mr Roach added earlier, then I will ask Patrick Hannan to speak about the email issue which Senator Faulkner raised.

Mr Roach—First of all, Admiral Shalders has asked me to advise you that the advertising agency used for the recruiting is Young & Rubicam Mattingly. The media placement buyer is Mitchell and Partners. Both contracts have been in place since August 2000 and both are three-year contracts. Secondly, I mentioned earlier that the separation rate was about 12½ per cent; in fact, the latest figures show we are doing substantially better than that—11.6 to 11.7 per cent on a rolling average.

Mr Bennett—A question was asked about the use of the overdraft last year. We went into overdraft on six non-contiguous days at an average amount of \$50 million with an interest rate of about 6.5 per cent per annum, so the cost of that was in the order of \$53,000.

Senator CHRIS EVANS—The other issue raised was the interest payments on investments of that cash—the terms of that investment. I was not sure whether you had taken that on notice or not. Was someone getting that for us?

Mr Bennett—Yes, they were. I would have to get the numbers in front of me to quote them, but it varies from two per cent through to higher rates for different sorts of accounts. I will provide that on notice.

Senator CHRIS EVANS—Could you give us an indicative list maybe? I want to get the range—what you get for six months versus what you get for a couple of days.

Dr Hawke—We will get that for you.

Senator CHRIS EVANS—I will be here for a few days.

Dr Hawke—Mr Hannan will talk on the specific issue relating to emails that Senator Faulkner was inquiring about.

Mr Hannan—The account was disabled on 10 December. I am advised that there was no access to that account between the date of the election and the date it was disabled, on 10 December.

Senator FAULKNER—Thanks for that. Mr Chair, I wanted to follow up on a couple of issues that arise from the letter that Dr Hawke sent to Ms Halton and vice versa. Could you let me know when you deem that to be appropriate? Are you happy if I do that now?

CHAIR—If Dr Hawke is happy to proceed and has the advice, we will do it now.

Senator FAULKNER—Dr Hawke, thanks for providing that correspondence. Why did you, in the first instance, think it was necessary to write to Ms Halton in the terms that you did?

Dr Hawke—Because she had failed to understand the nub of the matter in suggesting that I or anyone else in Defence would go behind the Chief of the Defence Force's back on a matter of his judgment. It is a fundamental misunderstanding of the diarchy and the directive that the minister provided to the CDF and me about our respective roles and responsibilities.

Senator FAULKNER—Do you take the same view in relation to communications you might have with the Secretary of the Department of the Prime Minister and Cabinet, in the broad, or is that a different sort of relationship?

Dr Hawke—Normally, both CDF and I are there at those committee hearings. He is there to advise on ADF matters and matters of operational command in his role as principal military adviser to the government. I am there to do the civilian side and the joint issues that I share with him.

Senator FAULKNER—In Ms Halton's letter to you in response to your letter—the best part of three weeks later, by the look of it—the second paragraph says:

I have reviewed the section to which you refer and the context in which answers were given. As we have discussed and contrary to the suggestion in your letter, the simple point I was attempting to convey to Senator Faulkner was that his assertion was not correct.

Then there is this sentence:

There had not been any communication on this issue with me or, to my knowledge, the Department or the Taskforce.

Could you tell the committee what you believe that relates to?

Dr Hawke—I am unclear as to what is meant by that, and I am unclear about the distinction that Ms Halton is drawing. The reason this came to my attention was an article in the *Canberra Times* by Verona Burgess that drew precisely the implication from Ms Halton's testimony in response to your questioning that goes to the nub of the matter. I am not the only one who has read her testimony in that way.

Senator FAULKNER—I am not being critical of that.

Dr Hawke—I know you are not. I am just saying that I am still not sure that she accepts that her testimony can be interpreted in that way.

Senator FAULKNER—But there is this statement:

There had not been any communication on this issue with me or, to my knowledge, the Department or the Taskforce.

I do not see how such a statement stacks up. I would be interested in Defence's view, given what we know about Ms Edwards's claims about the vigorous inquiries of Defence in the period of 9 to 11 October and the fact that Ms Edwards strongly gave evidence that she brought the chronology to Ms Halton's attention and read out the footnote—not to mention the evidence by Commander Stefan King. I really do not see how such a statement can hold water.

Dr Hawke—I do not understand it either. You would have to ask Ms Halton.

Senator FAULKNER—I do not have her before me, as you would appreciate, Dr Hawke.

Dr Hawke—I agree with you: I do not understand that view. My memory is not perfect in any shape or form, and maybe she did not remember those issues.

Senator FAULKNER—Did you discuss these matters with anyone in the ADF or, more broadly, with any officer of the Commonwealth before you sent this letter to Ms Halton? Did you seek any counsel?

Dr Hawke—Yes, I spoke to the team that CDF and I have set up that is working on this issue.

Senator FAULKNER—Do you mean Admiral Gates's team?

Dr Hawke—Correct. I spoke to that team before I sent the note to Ms Halton.

Senator FAULKNER—I am not being critical, but why did you discuss that with Admiral Gates?

Dr Hawke—I asked them whether it was just me who was seeing it this way, and they were of a similar mind.

Senator FAULKNER—So you were trying to assure yourself that your own interpretation was a valid one?

Dr Hawke—That could be, and was, held by others.

Senator FAULKNER—And that view was reinforced?

Dr Hawke—Yes.

Senator FAULKNER—And it was only Admiral Gates and his team that you discussed it with?

Dr Hawke—There were a couple of people there, including a former public servant who is on that team.

Senator FAULKNER—Ms Halton says a little earlier in the same paragraph in her letter:

As we have discussed and contrary to the suggestion in your letter ...

You mentioned, I think, that you had a brief discussion with Ms Halton in the Great Hall here at Parliament House. Was that the only discussion?

Dr Hawke—No, my recollection is that I actually telephoned her in response to her telephone call later that week to discuss the issue. She then indicated to me that she would be writing back about her version.

Senator FAULKNER—This is after she had received your letter?

Dr Hawke—Yes, it was after that. That is correct.

Senator FAULKNER—Was it only that, Dr Hawke?

Dr Hawke—Sorry?

Senator FAULKNER—Was it only that, in relation to your conversation with Ms Halton?

Dr Hawke—I am not sure I follow you.

Senator FAULKNER—It was not a very pleasant conversation, was it? Was it a bit strained?

Dr Hawke—It was a bit testy, but I guess you would expect that. She and I have different views about this issue. Essentially, we have agreed to disagree.

Senator FAULKNER—As testy as conversations get between—

Dr Hawke—No, it was not heated. It was just that we have different views of the matter.

Senator FAULKNER—Ms Halton said in her evidence on 16 April some things we have already spoken about but she also used these words:

... not only were we not told; it was never alluded to—there was never the slightest suggestion.

Did you also consider that evidence when you determined to write to her?

Dr Hawke—No, I did not. I was essentially picking up on that newspaper clipping and the testimony that she had given in response to your questioning. I would have to go back and get the extract from the *Hansard*; it went over a couple of pages, from my recollection.

Senator FAULKNER—Did you at any stage determine to inform the Secretary of the Department of the Prime Minister and Cabinet that you had undertaken this course of action?

Dr Hawke—I copied my letter to Mr Moore-Wilton, and you can see that on my letter. In my view, it affected an officer of his department at the time, and I thought that in the circumstances he perhaps needed to know about this and that I held this view.

Senator FAULKNER—Have you spoken to him about it at all?

Dr Hawke—I had a half conversation with him—

Senator FAULKNER—A half conversation?

Dr Hawke—About a week or so ago he just noted that I had written to Jane and she had responded, and in his view it was a matter between us. He did not think he had any role to play and I did not think he had any role to play in it either, but my view was he needed to know about it.

Senator FAULKNER—Why did you decide to write today to Senator Cook as the chairman of the select committee?

Dr Hawke—Because I have been away for a week and I thought, in fairness to the select committee, they should know my view about this matter as well, since it goes very much to my view of the matter.

Senator FAULKNER—Does this issue go to a difference between senior officers of respective departments—in this case it is Defence and an officer of the Department of the Prime Minister and Cabinet—or is it a difference between departments?

Dr Hawke—It goes to the nub of the view about the diarchy: what the diarchy actually means and the way it works—which, it seems, some people do not understand.

Senator FAULKNER—What do you mean by ‘some people’? Do you mean Ms Halton does not understand?

Dr Hawke—I do not think she is the only one; I think there are other people around who do not entirely understand.

Senator FAULKNER—Who else does not understand?

Dr Hawke—There are people within our own department who do not always understand the nature of the diarchy and the way it works.

Senator FAULKNER—Does Mr Moore-Wilton understand the nature of the diarchy?

Dr Hawke—I think he has got a very good idea of the way it works.

Senator FAULKNER—You would not describe yourself as a diarchy fan, would you?

Dr Hawke—Yes, absolutely! I wrote a paper in February 2000, I think, on this precise issue to try to explain why the diarchy was important to Defence, how it had evolved and what it was then so that people could understand the evolution of the diarchy and the way in which it works in practice now. I am happy to make that paper available to you.

Senator FAULKNER—Don’t make it available to me—I think I have read it. I think it is Ms Halton you should be sending it to. Did you send Ms Halton a copy?

Dr Hawke—I did not.

Senator FAULKNER—There you are, you see; you should probably have appended it to that letter, Dr Hawke.

Dr Hawke—Perhaps I should have.

Senator FAULKNER—Yes, I think so. I think another letter is in order.

Dr Hawke—I do not think we will be having any further correspondence on this issue.

Senator FAULKNER—I doubt you will be having any further communication at all.

Dr Hawke—Quite the contrary.

Senator FAULKNER—Oh, come on! It is the worst kept secret in Christendom that relations between you as the Secretary to the Department of Defence and Ms Halton—you described them as testy—

Dr Hawke—I think people are reading too much into it. We had a difference of view over this professional matter. We have had the difference and that is it; we will go on.

Senator FAULKNER—You would accept that it is pretty crucial, given the evidence that has been collated and examined by the select committee on this matter.

Dr Hawke—That is why I have written to Senator Cook about the matter.

Senator FAULKNER—It is very crucial, isn’t it, Dr Hawke, to Defence’s reputation?

Dr Hawke—And to mine.

Senator FAULKNER—Yes, and not for one minute do I suggest that you should not be concerned about your personal reputation—we all are. But this goes significantly broader than that, doesn’t it?

Dr Hawke—It is fundamental to understanding the way in which Defence works.

Senator FAULKNER—As far as you are concerned, that is where the matter rests now.

Dr Hawke—Certainly.

Senator FAULKNER—And you have not heard any more about it?

Dr Hawke—No.

Senator FAULKNER—Was it a very long discussion you had in the Great Hall?

Dr Hawke—No. It was very fleeting because it was at the lunch for Prime Minister Koizumi.

Senator FAULKNER—Fleeting and unpleasant.

Dr Hawke—Not Prime Minister Koizumi's lunch, no.

Senator FAULKNER—No, I am not saying the lunch was fleeting. I did not attend but I know many who did and they told me it went for a good hour-and-a-half.

Dr Hawke—No, that is fundamentally not true.

Senator FAULKNER—The lunch.

Dr Hawke—Oh, the lunch—our discussion went for only a few minutes before we were called to table, because the Prime Ministers were arriving. I said to her that—

Senator FAULKNER—People nearby were relieved at that, weren't they?

Dr Hawke—I am sorry?

Senator FAULKNER—People were relieved when you were called to the table.

Dr Hawke—I am not sure about that.

CHAIR—Senator Hogg, do you have a question?

Senator CHRIS EVANS—This is going to be a bit dry by comparison, isn't it?

Senator HOGG—Yes, it is going to be very dry.

Senator WEST—It was a good lunch.

Senator HOGG—I did not know we were discussing the lunch. Taking the finance officers back to page 22 of the PBS, there is an item at the bottom of the page headed 'Location of new immigration detention facility in south-east Queensland'. In the table, under 'Capital' it has 'Not for publication'. I can understand people putting that on their Lotto entries and the like but I do not think 'not for publication' is something that I have ever seen in a PBS before. Can you advise me why it is not for publication and what is not for publication?

Mr Roach—I think so. There may be somebody here who can better answer that, but I will give you the answer as I understand it and I can then confirm it.

Senator HOGG—If we need someone to clarify it for me later on—

Dr Hawke—It goes to not putting in the public arena the commercial information. If we say how much we expect to get for this parcel of land you can bet your life that whoever bids for it is going to bid at or around that figure. So, as I understand it, it is that issue. We are selling this land.

Senator HOGG—So it is not the whole site?

Dr Hawke—We are selling the land, and if we tell them that we expect to get X dollars, that is what the issue is.

Senator CHRIS EVANS—As I understand it, this is not going on public sale. Aren't you making this available to the department of immigration?

Dr Hawke—Only a portion of the land.

Senator CHRIS EVANS—That is right. As I understand the plan, a portion of it is to be sold at private treaty or whatever but the rest of it is a government asset transfer between departments—is that right? Obviously there would be a commercial price for that part of the land as well.

Senator Hill—As I recall, if Immigration go ahead with their proposal part of it will be sold to Immigration and part of it will be sold at large.

Senator CHRIS EVANS—I presume the price it will be sold at to Immigration is not commercially sensitive. I guess it has not been set but I presume there is an established procedure for selling land between departments, is there?

Senator Hill—I don't think it has been set.

Senator HOGG—A voice of wisdom has joined us.

Senator Hill—It is all out of the same pot in the end. Where are we in relation to the sale to Immigration?

Mr Pezzullo—In relation to the site at Meeandah, departments are currently negotiating the final arrangements for a transfer of a portion of the site. The site will be approximately one-third of the current site. Minister Ruddock has announced that it is the preferred site of his portfolio but it has not yet been announced as being a definitive and final site. Minister Ruddock is undertaking a process of community consultation. He is being assisted in that by the Defence department to the extent that we control the facility. We control the base and the personnel et cetera.

Senator HOGG—I understand the sensitivity that it is being sold. Can I ask the department therefore: has the element of the sale that Defence will retain been built into this year's budget?

Mr Pezzullo—Yes. We knew of the government's decision in the general before we put the budget together. We have accounted for the fact that potentially up to a third of the site is not going to be available for disposal by way of either outright sale or sale and lease-back, depending on the outcome of the DIDs process, which you have gone to earlier today. We have allowed for that. It might well be that the government-community consultation process yields up a different result, but Minister Ruddock at this stage has indicated that that is the government's preferred site, subject to those community consultations that he has initiated.

Senator HOGG—Can I use some hypothetical figures so that I can get the process in my own mind. Let us just say the site is worth notionally \$30 million—and I have no idea what it is worth and I am not asking you. Let us assume that it is worth \$30 million. Can one assume that, of that \$30 million, \$10 million would be the figure that would be retained by Defence? Is that how it works? And the other \$20 million would be returned to Finance?

Mr Pezzullo—Without going to the precise, either the percentages or the values—

Senator HOGG—Use my figures.

Mr Pezzullo—It is not so much moneys that are retained by Defence. Within the budget there will need to be a transfer of a payment from DIMIA to Defence. That will show up in

the accounts in the normal manner. Then the rest of the site is available for disposal by way of either outright sale or sale and lease-back.

Senator HOGG—Is the not-for-publication amount designed to be the amount that we will at some stage, later in this financial year once the sale has been effected, see reflected in the additional estimates statement?

Mr Pezzullo—There will be an amount that the Commonwealth receives out of the sale on the open market or through a priority sale, and that will be encapsulated within general government receipts for Defence property sales.

Senator CHRIS EVANS—As I understand it, the two options are these. If DIMIA go ahead with the detention centre then you will sell a third to them and put the rest on the market in whatever arrangement is determined. The other option is that you sell the lot in that manner. Are those the two options?

Mr Pezzullo—As you indicate in your predicate there, if DIMIA on a whole-of-government basis require, let us say hypothetically, up to a third of the site, then that is obviously not available for disposal in a market sense.

Senator CHRIS EVANS—But if they decide not to proceed with that site then Defence would intend to dispose of the rest of the site in any event?

Mr Pezzullo—That is correct.

Senator CHRIS EVANS—So there will no longer be any Defence establishment at that site?

Mr Pezzullo—It is not possible to be definitive about it now because it does depend on the outcome of the DIDS tender process. You would be familiar from previous *Hansards* that there has been some discussion over the last year or so about the nature of the DIDS tendering process. There are mandated facilities and optional facilities throughout the country. It is possible that a DIDS successful contractor may well say, 'We would like to put our footprint there,' in which case they will get into a negotiation with the department or with some other commercial party who might seek to have an interest in that land. It would not directly be a defence department piece of land, but it would be servicing defence department interests.

Senator HOGG—With regard to 'not for publication', I understand Dr Hawke's reasons and the explanation that has been given but, in terms of the overall budget that has been framed for 2002-03, can I assume that there is an amount there that impacts on the overall total? That is what I am wondering.

Mr Pezzullo—Yes, Senator. The budget papers you have do not disclose individual property values, nor do they definitively list the sales that we are targeting because clearly we would not be able to operate in a market. However, we would have built into our preparations for the budget certain assumptions about the kind of receipts that we are expecting, yes.

Senator Hill—But in those calculations we have not discounted, have we, the site for what might be sold to Immigration?

Mr Pezzullo—We have made a contingency for that, Minister.

Senator Hill—However, if you say that if they buy it there would be a book entry, we would still end up, on our budget, getting the whole lot.

Mr Pezzullo—That is right. Defence would receive moneys, of which a portion would come from a general sale and a portion would come from another Commonwealth agency.

The amount that hits the bottom line is obviously the moneys that the Commonwealth has received out of the sale.

Dr Hawke—The total of these sales is at page 60 of the PBS.

Senator HILL—I think that what the committee might want to know is whether the anticipated full value of the site is still within that figure.

Mr Pezzullo—No, it is not, Minister.

Senator Hill—So it has been discounted by the one-third that might be sold to DIMIA, as far as those figures go. It is really looking at the effect on the Commonwealth as a whole.

Mr Pezzullo—That is right.

Senator HOGG—So it could subsequently appear in the additional estimates statement making the sales higher.

Mr Pezzullo—I defer to my CFO colleagues on the classification treatment of it but, on what you are asking me about the impact on the bottom line, the only moneys that we have factored in for any sale relates to what the Commonwealth receives from a disposal by way of either sale or sale/lease-back, not a transfer payment out of another department.

Senator HOGG—Then why would one put that in there as a budget measure?

Mr Roach—I think the answer to that is partly that this is a measure which affects more than one department, so you will actually find it against DIMIA as well. There is a corresponding entry.

Senator HOGG—Elsewhere?

Mr Roach—Yes.

Mr Pezzullo—It requires a book entry between two agencies.

Senator HOGG—All right. Is there a deadline for the sale of that property?

Mr Pezzullo—It is a 2002-03 sale.

Dr Hawke—It is part of that total on page 60.

Senator HOGG—That is the question I had on page 22. The finance people may be able to give me the answer to this question now or later. On page 23 under discretionary grants there is the Defence Family Support Fund program. It is not a huge amount of money, but it has been relatively static for a number of years. Is that because the funds allocated are not fully utilised or is it that the funds have been capped? What explanation can you give?

Rear Adm. Shalders—The funds are fully utilised and have been since the program was introduced in 1989-90.

Senator HOGG—How has the level of funding changed in that time? Has it changed at all or has it been relatively static?

Rear Adm. Shalders—It has been relatively static, certainly in the last three years. I do not have the detail of the years prior to that, but I can ascertain that for you.

Senator HOGG—Has it been relatively static because demand has not been pushing the threshold to get it increased?

Rear Adm. Shalders—Demand always exceeds the available funds and we use a prioritising mechanism to allocate the capped funding.

Senator HOGG—There is a cap. By how much does the demand exceed the allocation, either in money terms or percentage terms?

Rear Adm. Shalders—I do not have that information.

Senator HOGG—Can you take that on notice?

Rear Adm. Shalders—Yes.

Senator HOGG—In taking that on notice will you also supply me with an answer on the movement, relatively speaking, over the last, say, five years? Do not go too much further than that. Can you give me some idea of the number of cases that are addressed each year under that?

Rear Adm. Shalders—Broadly speaking, it is of the order of 50 to 70 applications from each region. Those 50 to 70 are generated from local areas before they come forward seeking funding.

Senator HOGG—I accept that; I just want to get an idea. Without being overly specific I would like some sort of description of the types of issues towards which the grants are made.

Rear Adm. Shalders—Broadly speaking, the grants are made to assist community groups to overcome the impacts of military life, particularly the mobility and separation that comes with military life. The funding is made to community groups, such as playgroups, and groups such as the Defence Special Needs Support Group. There are 50 to 70 allocations each year from each region for a wide variety of purposes.

Senator HOGG—By how much does the demand outstrip the allocation?

Rear Adm. Shalders—I will take that on notice.

Mr Bennett—If I may, I can provide some numbers for you. In 1997-98, \$1.091 million was provided to 261 recipients; in 1998-99, \$1.212 million was provided to 243 recipients; in 1999-2000, \$1.238 million was provided to 298 recipients; in 2000-01, \$0.938 million was provided to 228 recipients; and our estimate for 2001-02 is \$1.35 million to be provided to 179 recipients.

Senator HOGG—If I understand what you are saying, the estimate for 2001-02 exceeds what would have been the allocation in last year's budget. So is there a bit of flexibility to exceed the cap?

Mr Bennett—I would have to check on what flexibility there is.

Rear Adm. Shalders—My current allocation for that program is \$1.25 million, so we will have to live within that cap.

Senator HOGG—You will have to live within your cap?

Mr Bennett—The \$1.35 million is an estimate.

Senator HOGG—I understand that it is an estimate, but it exceeds the cap that exists.

Senator WEST—When were last year's successful projects announced?

Rear Adm. Shalders—In August. Our aim is to get the projects announced and distributed in August each year.

Mr Bennett—In 2001-02 there was an increase of \$100,000 factored in for the commencement of the Defence Family Emergency Fund scheme as was agreed on 6 December 2001. This establishes a fund for Defence families to borrow from and therefore is not an ongoing expenditure.

Senator WEST—That is a new one. That has not been in that program before.

Rear Adm. Shalders—That was a part of the \$100 million we spoke about earlier, which is administered by the Defence People Committee. That was an initiative targeted through that committee at recruiting and retention.

Senator WEST—Is there going to continue to be the \$100,000 borrowing?

Mr Bennett—No, that is not an ongoing expenditure.

Mr Roach—It is seed funding which should replenish itself.

Senator CHRIS EVANS—These are low interest loans?

Mr Bennett—Yes.

Senator WEST—How is it going? How many loans have been let? How many defaults?

Rear Adm. Shalders—I will take that on notice.

Mr Roach—It is a very new program.

Mr Bennett—Some aspects of this question have been answered previously. The \$100,000 is a total fixed amount to be maintained over a four-year period. It is a one-off capital allocation maintained over the four years with loans being drawn from it as required to meet family support issues.

Senator WEST—Who can borrow from it? Who can access the loans? Is it family support organisations or individual ADF members?

Rear Adm. Shalders—Individual ADF members.

Senator WEST—I am interested to know how many are out, what sort of amounts and what the repayment schedule is.

Rear Adm. Shalders—I will provide that information to you for the period since the scheme was introduced. As was indicated, it is a fairly new scheme. The numbers are quite small, but I will give you the details.

Senator WEST—The amount of money is quite small too: it is only \$100,000. You are not going to be making very big loans; you are not going to give one person \$100,000.

Rear Adm. Shalders—I do not have that information with me at the moment. I will provide it for you.

Senator WEST—What sorts of things are they going to be borrowing money for?

Rear Adm. Shalders—It could be used, for example, for unexpected travel that families are required to undertake. It can be used for a variety of purposes. It is administered by the military support officers across the three services. The uses to which the loans can be put are very wide and very varied.

Senator WEST—I am sure my colleagues will be interested to follow up the answer when it arrives, as I will not be here.

Senator CHRIS EVANS—We got into a bit of a discussion about property as a result of the discussion about that particular immigration detention centre site. I presume we should be doing the property questions under corporate services. Is that right?

Dr Hawke—Yes.

Senator CHRIS EVANS—I will come back to that then. I was going to move on to DMO issues—capital projects et cetera.

Mr Bennett—Before you do, I might take the opportunity to provide another answer to you. The interest earnings in 1999 to 2001 were as follows: in 1999-2000 the interest rates were in the range of 4.67 per cent to 6.0 per cent and there were earnings of \$29.5 million; in 2000-01 the interest rate ranges were in the area of 5.9 per cent to 6.49 per cent and the earnings totalled \$28.6 million.

Senator CHRIS EVANS—So \$28.6 million was earned in interest in that year. Have you got the length of those investments?

Mr Bennett—No, I do not have a breakdown of the specific sorts of contracts.

Mr Roach—Can I just clarify one thing before we move off this. I did misspeak earlier on the question of the measures and the specialist military equipment and facilities for TAG and IRR. Looking at the budget measures under the GFS format, which is what I think was being referred to at the time, the specialist military equipment is not in the capital line; it is actually expended. I am quite happy to provide you with a breakdown of those numbers under our own standards.

Senator CHRIS EVANS—In other words, there is a smaller line item of about \$150 million for that, isn't there? Is that what you are referring to?

Mr Roach—No, I think we were referring to the measures on pages 19 and 21.

Senator Hill—We have quite a detailed breakdown of that. I think we said earlier that we could provide it. That way you would get an answer that would clearly set out every aspect of the financial commitment.

Senator CHRIS EVANS—Thank you for that.

ACTING CHAIR (Senator Ferguson)—We will move on now to the capital budget items.

Senator CHRIS EVANS—Can I just start with a general question about the response to the audit report on risk management inside DMO. Could you, in general terms, outline for me what the response has been to that audit report and what measures have been put in place to address the concerns it raised?

Mr Roche—I might seek some assistance on this. Can you just give us a bit of information on the audit report you are referring to?

Senator CHRIS EVANS—The one from December, which talks about concerns about risk management and the major projects inside DMO.

Mr Roche—I will just arm myself with a copy of that report.

Senator Hill—I do not think we have given a formal response to the report as yet—

Mr Roche—No, I do not think so.

Senator CHRIS EVANS—This is the one that rates the likelihood of failure of major capital acquisition projects as very high, so I presume it would have taken some—

Senator Hill—I made some comments and I have spoken to the Auditor-General since then about it as well. Some aspects of the report I think you will find we accept and some parts we think included errors. If it is the one I am thinking of, it was in relation to the Collins class submarines. Is that the report we are talking about?

Mr Roche—The reason for my confusion is that I think this was a preliminary study. I think that the Auditor has in fact deferred the full report. I am not sure that it went beyond the preliminary study. Do you have the reference there, Senator?

Senator CHRIS EVANS—I thought it was December 2001. That was my recollection.

Senator Hill—Why don't we come back to that one after dinner and get the reports out in the meantime?

Senator CHRIS EVANS—I think it goes to some fairly general questions about the management of risk in DMO, so I wanted to start with that approach. As I recall, it was fairly newsworthy at the time.

Senator Hill—It was about systems, wasn't it? If it is the one I am thinking of—and I used the example of the Collins—it said that the Collins illustrated a failure because there was an enormous figure of something like \$2 billion still to be expended. What it did not do was distinguish between what was being expended to achieve an original capability and what was being expended in the future to enhance that capability—new combat systems, new weapons and the like.

Senator CHRIS EVANS—This is the December 2001 Audit Office report *Status reporting of major Defence acquisition projects*.

Mr Roche—I think that is a preliminary report that did not require a full departmental response. I think it foreshadows a more detailed report to be done at a later stage. It made a number of preliminary comments, but I think we would be looking for the full report to respond in detail. Certainly we can talk about mismanagement of projects.

Senator CHRIS EVANS—I was not really interested in the tabling of the formal response. It seemed to me that it was a fairly explosive and critical report, and I was really trying to get your response as to what you have taken from that and what adjustments have been made to the concerns raised. I was not asking you for a copy of the government's formal response.

Mr Roche—I do not think there has been a formal response, because there has not been a full report. I think it was a preliminary report that identified the need to do a full review of the issue at a later stage. The Audit Office does a number of preliminary studies like this. Of their nature, they are preliminary findings and do not require a departmental response.

Senator CHRIS EVANS—Mr Roche, I am happy to concede that you are correct on that. I am more interested in what you have done in response to the Audit Office's criticisms and concerns in a practical sense.

Ms Thorpe—The particular report that you are referring to was actually a summary of previous findings that ANAO had had. They had scheduled an audit for that particular time and, because DMO was going through a number of changes, they accepted that it was going to take us some time to implement the concerns that they had raised and they therefore only did a preliminary study. Their preliminary study simply summarised earlier findings, and they recognised that DMO was in the process of going through quite significant change and

implementing a number of measures that would, within the next 18 months to two years, address those particular issues. Because they had scheduled that audit, they had to table something in parliament, and therefore they tabled a summary of their previous findings and identified in that report a recognition that DMO was currently working on those issues and that they would come back at a later stage and review the work we had done to see how well we had addressed those issues. So we are currently in the middle of a process of change that will address those issues that ANAO recognised were not yet in place for them to assess as to whether or not we had been effective.

Mr Roche—The short answer to your question is that the whole process that we are going through at the moment is actually directed towards addressing many of those issues.

Senator CHRIS EVANS—But it is also true that that whole process provides some additional risks to you too, doesn't it?

Mr Roche—Yes, if you change processes, you do introduce risks that have to be managed.

Senator Hill—But risks are assessed in terms of timetable, capability and cost and are now reported to government on a monthly basis with individual, more specific reports from time to time in the first instance to me, and in some instances right through to the National Security Committee of cabinet. So, in talking about where we are at the moment, we believe we have a much better handle on risks than was the case in the past. That does not solve the problems that we know exist, but hopefully it puts us in a more realistic situation in addressing problems. Mr Roche could speak about this in great detail, but the risks areas in new contracts that are entered into are identified up front and particular mechanisms are put in place in order that those risks can be continually monitored and addressed. If it is the AEW&C contract or the TADRS contract, we know where the greatest risks are. Addressing those challenges right from the start of the contract seems to be doing business differently from what was done in the past.

Senator HOGG—But, Minister, that does not mean shifting the risk away from the Commonwealth and on to the successful or proposed tenderer, does it? I think I have heard this at the hearings of another committee I am a member of. There was an emerging criticism that too much of the risk was being shifted away from Defence and that Defence was not facing up to taking enough of the risk itself.

Senator Hill—I think that, in my short term in the business, Defence has accepted too much of the risk in the past if anything. But it is not so much a question of apportioning responsibility; in the end we the public miss out on cost or capability or timing, or whatever. Therefore, if we know there is a risk area, such as systems integration, it receives the appropriate planning and attention up front—and from then on, continuously—rather than, as we have seen in other instances, getting well down into the contract, seeing a problem and starting to address it.

Mr Roche—Senator, were you referring to the committee into the annual report where that was raised?

Senator HOGG—I just cannot pinpoint where. We are on so many committees in this place you flash in and out.

Senator Hill—Don't blame us for that.

Senator HOGG—I am not blaming you for that, Minister; I am just saying.

Senator CHRIS EVANS—You were more keen on them when you were in opposition.

Senator WEST—Yes, I seem to recall that you had an input—a big input.

Mr Roche—The comment was made at that committee that Defence was attempting to lay the blame entirely on industry for projects that were late. I think that is very intrinsic to that interpretation of what we have been saying. I think we have been prepared to step up those responsibilities. The minister mentioned what has been done with new projects. We have a risk management program now that starts right at the top of Defence, goes right through the entire department and spreads out into individual areas such as DMO. DMO has always had a risk management approach, but now it has been systematised even more in the sense that it is part of an overall departmental risk management program. It goes down to each of the individual areas in DMO, in that we go through a process of identification and treatment of risks that are peculiar to individual projects and for generic risks. The minister mentioned the integration of software where, for example, we tackled that particular risk by increasing very significantly the amount of scrutiny we do on software components in projects. We are also subjecting all of our senior people to training in overall risk management of projects—software projects, software architecture and so on. So there is a very large range and we would be happy to share the details of our risk management program with you. I think the Audit Office report reflected that that was work in progress and that they would come back in 12 months or so.

Senator CHRIS EVANS—No doubt, as I say, there are some risks with the changes that you are driving. One of those is obviously retention of staff. I asked you a question on notice, for which we got answers—and I thank you for that—that indicated that about 100 of the 300 staff had not yet responded to the question about transfer. Can anyone give me an update on that issue of whether or not we have more, and better, information as to that transfer process as part of your reorganisation?

Mr Roche—I think those figures we gave you are quite recent. I do not have any more recent figures. We do acknowledge that having staff move to the new system program offices is a challenge, but I guess the fundamental point from my point of view is that you cannot sensibly expect to support, say, a submarine platform based in Perth which undergoes deeper maintenance in Adelaide with engineers that are in Sydney and Canberra. It makes very sound sense to locate your specialists close to the customer and close to the supplier, and that is what we are doing. I think some of the system program officers are already showing significant benefits from that approach and we have had some very positive reactions from Air Force and from Navy, as well in the project offices that have already been set up. I would be happy to go into that in some more detail, but there is a Senate committee looking into that later this year.

Senator CHRIS EVANS—Yes. Senator Hogg and I have been discussing that. We are interested in how it is working and, as Western Australians, we have often raged against the failure to take that action in the past. It has been put to me that some of those systems programs officers have not had any civilian staff at all transferred with them, that you are having a lot of resistance and that you have lost large numbers of people in that process. Is that right?

Mr Roche—We have not lost any people at all, in the sense that the people that have not transferred with the program officers have been largely redeployed within either Defence or the DMO; so they are certainly not lost to us.

Senator CHRIS EVANS—I mean the program office.

Mr Roche—There are some program offices where it is a challenge to get people to move.

Senator CHRIS EVANS—Which are the particular ones of concern?

Mr Roche—Probably the one that worries me most is naval aviation at Nowra. There are some Army ones that need to move to Melbourne, but I believe that we can deal with those. We have timed the movement of some of those projects to take best advantage of the people that are working in them at the moment. The Navy one worries me most, as I said, because it requires trained aeronautical engineers and we are trying now to recruit additional engineers to cover those shortfalls. We will do work out of Canberra; there are a number of approaches that we are adopting to get the work done. I find it difficult at times to understand what people would find wrong with Nowra. I think that, as far as living conditions go, it has to be pretty attractive.

Senator CHRIS EVANS—Obviously those sorts of things have quite significant implications for the continuity of project management, don't they? I am just trying to understand what pressures that might be putting on DMO.

Mr Roche—Any large-scale reorganisation—bringing together an organisation of 8,000-odd people from three separate organisations—will create stresses and strains, and moving people at the same time. We have a fair bit on our plate, but again none of that can be an excuse for not moving to do this and do it quickly. It is better to move quickly to do it and to set up the organisation in the way that you expect it to go forward rather than to drag it out.

Senator CHRIS EVANS—but I am interested in this risk management question, which is where I started—we seem to have got lost. For instance, you have the patrol boat systems program officer transferring. They are currently in the middle of short-listing the patrol boat replacement, aren't they?

Mr Roche—Yes, they are, and they will not transfer until that is done.

Senator CHRIS EVANS—You are not going to transfer them until after that has been done?

Mr Roche—Let me just check on the exact date. No, that component of the project will not transfer in fact until we get down to a project contract award.

Senator CHRIS EVANS—You will hold on to them until the contract is awarded?

Mr Roche—There will be some movement before that, but I would expect them to be here in Canberra. The point we have made about these moves to the SPOs located with their customers is that major capital acquisition will probably still continue to be done in Canberra. It involves a large amount of interaction with the parent service, with other agencies, with the chief finance officer and so on. Most of that work will continue to be done in Canberra.

Senator CHRIS EVANS—Have you explored the option of staff commuting to relocation sites?

Mr Roche—Some staff in Defence do commute—not too many. I do not know that it is practical for the sites that we are concerned about. Ultimately we have to solve the problem of the Navy aviation. I think that the Army projects in Melbourne will be solved probably more easily. In the meantime, if some of the shortfall can be covered by commuting, we will do it, but it is not my preference.

Senator CHRIS EVANS—Are some of your people commuting now?

Mr Roche—Some commute now, yes.

Senator CHRIS EVANS—How many?

Mr Roche—I cannot give you an exact number.

Senator CHRIS EVANS—Are there 10 or 100?

Mr Roche—I would think we are talking just small numbers.

Senator CHRIS EVANS—Are they long-term arrangements or short-term arrangements?

Mr Roche—They vary. The head of my LAN systems division, for example, spends two days a week in Canberra and three days in Melbourne. That is inevitable at his level, and that will continue for the foreseeable future. Others I would be trying to make as short term as possible.

Senator CHRIS EVANS—Are these arrangements approved by you?

Mr Roche—Yes—either by me or one of my division heads.

Senator CHRIS EVANS—So it would be a senior decision about whether or not such arrangements were replaced?

Mr Roche—I would expect so, yes.

Senator CHRIS EVANS—Are any of these semipermanent arrangements?

Mr Roche—Again, I would have to check.

Senator CHRIS EVANS—If you would not mind—I would be interested to know. So you are effectively paying some staff to fly in and out of new locations on a weekly basis. Is that right?

Mr Roche—I have some, but I cannot give you the exact number. I will have to check on that.

Senator CHRIS EVANS—Perhaps you could take that on notice for me. Can you explain to me the role of the management audit branch within DMO?

Mr Roche—That does not belong to me. It reports to the Inspector-General of Defence.

Senator CHRIS EVANS—Is it still involved with the DMO?

Mr Roche—The management audit branch undertakes internal audits of the branch.

Senator CHRIS EVANS—Could someone outline for me when the new risk management arrangements the minister was referring to started and how they operate in a formal sense?

Mr Roche—I do not know that you could actually describe them as having a particular starting point. Risk management has been a feature of the work done in the old DAO and in Support Command. It has been there for quite some time; it is not a new concept. We have brought it together in more of a whole-of-organisation sense, and that happened last year. It is within the last six months that we have formalised the whole of the DMO risk management plan and actions, but that is not to say there was not risk management in place right across the board beforehand.

Senator CHRIS EVANS—So, when the minister was talking about the monthly reports et cetera to himself, is that new?

Mr Roche—No. That one has been in place now for probably 18 months to the Defence Committee and has probably been going to the minister for some 12 months. That would be my estimate. I could check on those.

Dr Hawke—What is new is the way in which the government looks at these issues in the National Security Committee of cabinet—what is called a two-pass process—and the fact that in the past, until the National Security Committee did this, each year the total defence capability projects used to be part of the budget submission. This did not get much visibility at all among the central agencies, let alone at the National Security Committee. Now each project gets separate consideration, firstly, by the Secretaries Committee on National Security and, then, by the National Security Committee itself. The minister takes a submission forward to the NSC so that they can see what the risks are and what the costs are. Then we report back against changes in cost, capability outcome and schedule delivery. That did not happen until the National Security Committee was set up.

Senator CHRIS EVANS—When was that, Dr Hawke?

Dr Hawke—That would have been before I arrived—probably in 1996. It probably got further development during our preparation of the white paper. We have followed that process since the government delivered the white paper, which I think was on 6 December 2000. That would be my understanding. I will ask Mr Roche to explain to you the two-step process that is involved.

Mr Roche—The whole process has been an evolutionary one. So those reports that we talked about going to the minister and to the executive committee have changed in their coverage over the last 12 months or so to the point where a larger number of projects have been picked up, more information has been provided in relation to each project and so on. They now pick up support issues as well as acquisition issues. As I said, this has been an evolutionary process. Just going back to what the secretary was saying: the reforms to defence acquisition that the government has agreed to include a two-step process. We now come to government at a much earlier stage than we used to, which gives them the opportunity to look at a project very much in its formative stages when it is still at the options stage. It also gives the government the opportunity to raise issues of risk and any strategic issues that arise. Following the first stage approval, it comes back for a second stage when much more work has been done to identify budget risk in detail, acquisition, methodology and so on, at which stage we should have a much better idea of schedule, budget and risk. I think that that is improving the flow of information to government and it is actually making sure that projects get much closer attention in the early stages.

Senator CHRIS EVANS—That seems to be giving government a chance to be more hands-on and more involved in the process. What does that do inside DMO, though, in terms of your risk management strategies, other than having someone keeping a closer eye on your decision-making processes?

Mr Roche—Clearly it forces us to have a much closer look at those projects because we are going to be facing up to more detailed scrutiny not only from government but from other departments at an earlier stage in the project—not that I suspect we need that forcing these days, but it does mean that all of the big issues, and certainly the risk issues, are going to be addressed very early on in a project.

Senator WEST—Can I turn to Bushranger. What is the latest there? What is going on? Are you making any progress?

Mr Roche—Yes, we are making progress. This project, as you know, has been a troubled one. We have now worked through with ADI what our options are and we have some

proposals and options to put to government. I expect government to consider those in the very near future on the way forward with this project.

Senator WEST—I think it was in March that the minister put a time frame on of two months.

Senator Hill—I said that I expected NSC to reconsider the project in June and that, therefore, any negotiation between ADI and the department which might be considered in that NSC deliberation would have to be concluded by the end of May. That process is being concluded and is being fed into the NSC consideration which, hopefully, will be in the next short while.

Senator WEST—Are there going to be any changes to the number of vehicles we are going to order or receive under the project? What was the original number?

Senator Hill—I do not really want to go into that now, because you know that I said on the previous occasion that we believed there was a significant failure on the part of the contractor. There is not much point in going through it all again, but it left us with few options. The Army, nevertheless, still had a desire to have a vehicle with that capability. We obviously still have a preference that it be constructed in Australia, and in Bendigo. We also had a budget that we had to stick within and a few other criteria such as that. As I said, with those benchmarks, the contractor and the department have worked constructively to see if there is a proposition that could be put before government that would give government the option of continuing with the project. That will be considered in a very short time space.

Senator WEST—What was the original number required?

Senator Hill—I think the original number changed a bit, didn't it?

Dr Williams—The original number was indicatively 370, but that was before there had been a thorough analysis. As a result of some of the early work with ADI, the figure was agreed at around 340.

Senator WEST—So we wait for the NSC deliberations this month?

Senator Hill—Yes. What I asked should occur has occurred, and we will be making a decision this month. There is always the possibility that the decision might be that some other—

Senator CHRIS EVANS—Is this the May decision?

Senator Hill—I said that the negotiation had to be completed by the end of May to be presented to government to be decided upon by government in June, and that timetable has been met.

Senator CHRIS EVANS—And that will be a decision made by you, Minister, in the end?

Senator Hill—No, by the government as a whole through the National Security Committee.

Senator CHRIS EVANS—Does that end up having to go to cabinet?

Senator Hill—That is cabinet.

Senator CHRIS EVANS—What could be the earliest production start for the Bushrangers then?

Senator Hill—We could go right through the alternative proposal that is being put to government, but I don't know that that would be helpful a couple of days before consideration

by government. I would prefer government to consider it and make a decision, and then we can have the political debate.

Senator CHRIS EVANS—It was not a politically charged question. I was just trying to get a sense of where we are at with the project. If it were to proceed, when would we be proceeding with it?

Senator Hill—I think full-scale production would proceed in 2004.

Dr Williams—By the end of 2004 for the initial production vehicles.

Senator Hill—The initial production would commence in 2004.

Senator CHRIS EVANS—What would be the delivery date for Defence then?

Dr Williams—If we worked to that time frame, it would be some tens of vehicles per year for a few years thereafter. So, by 2006-07, we would be getting up towards the total.

Senator HOGG—I refer you to page 75 of the PBS. It is a matter of being able to track the projects from one PBS to the additional estimates to the annual report. There seems to be a number of things listed on page 75. Is it possible to give some sort of consistent name to these projects? I seem to find from time to time there might be a subtle change in the name and one has difficulty in following the project through. Is that possible?

Mr Roche—They all have a project number.

Senator HOGG—That is what I know.

Mr Roche—It should be possible to give them a project number.

Senator Hill—Project number is what I try to avoid because then you find the number is divided into subnumbers.

Senator HOGG—That is one of the things I have noticed.

Mr Roach—It is possible for us to track the projects. I guess the qualification I have is that the make-up of projects does actually change over time as we develop them. A nice linear progression from one year to the next is not something that will ever be achieved.

Senator HOGG—I accept that, but it would make tracking some of these projects a little easier if there were something that clearly defined the project.

Mr Roche—We do track them on page 77. It is there in the footnotes to the projects which have been removed from the top 20 table.

Senator HOGG—With respect, I think that is about the first time that has ever appeared. It has probably appeared because of questions I have asked previously. If it has been there a couple of years, it has appeared because of my request to be able to track some of these projects. I have asked this question before, but could you just refresh my memory. If you turn to page 77 you will see that some of these approved project costs are substantially higher—in some instances up to 10 per cent—than they were in a previous PBS. Is that due to currency fluctuations?

Dr Hawke—Which one in particular?

Senator HOGG—I will give you one in particular—the approved project ‘Airborne Early Warning and Control’ expenditure in the 2001-02 PBS was \$3,110 million; now it is \$3,455 million. What has caused the project to blow out that much?

Mr Roche—I will get you the detail on it, but I think you will find it is nearly all currency.

Senator HOGG—There are a number of projects similar to that. I am sure there is a common explanation.

Mr Roche—There are three likely causes of change in the number. The first two are a change in the price and a change in the exchange in the project approval and the third is a change in scope.

Senator HOGG—In that instance there is almost a 10 per cent change.

Mr Roche—There is no change in scope in that project. It would be almost certainly currency or indexation.

Ms Thorpe—There was no change in scope. There was a lot of up and down on that particular project at different times over the years. There seems to have been an error in the \$3,110 million in a previous year's PBS. That seems to be an error; it was not quite as low as that. The National Security Council reduced the cost of the project by \$166 million in April 2001 and, in June 2001, the \$45 million price and \$40 million exchange were approved so that was added on. The figure of \$3,110 million was incorrect; it should have been slightly higher.

Senator Hill—The last advice I had on that project is that it is still within budget and on time. Each of the areas of risk and the technological aspects of that project are extreme. It is meeting the milestones that have been set.

Senator HOGG—All right. I will not take the time of the committee to go through some of the other projects there, but I think if officers of the department check there are a number of fluctuations. Some have gone down slightly, but there are a couple that have gone up—in the order of five per cent. But, as I say, I am not going to pursue those at this time.

Mr Roche—I would expect virtually all of them to move within the year because of currency and other indexation. The ones that change because of scope would be the exceptions.

Senator HOGG—Where they move up, is that additional expenditure brought to account in that budget?

Mr Roche—No. The project expenditure is at project approval and it can cover expenditure over many years. In the case of AEW&C, that project approval covers expenditure over probably the best part of 10 or 12 years.

Senator HOGG—So the approved expenditure could continue to increase but the increased costs might well be a deferred cost later in the project itself?

Ms Thorpe—You need to differentiate between price and exchange increase, which are just nominal, as opposed to real cost increase. Over the life of the project, every year we adjust the project approval in line with the DOFA prices and exchange the department is given, as we discussed earlier. We in turn adjust each of the project approvals. That is why you often see in text '01-02 prices or 00-01 prices'.

Senator HOGG—Are those identified for us?

Ms Thorpe—Yes, for each of the tables each year. I notice that this table does not have that footnote, but usually we say, 'This table in this PBS is in 01-02 prices.' You often see references. For some reason we do not seem to have that footnote in this year, but generally they are in the prices of the year that we have. We do not have the 2002-03 prices yet, so they are still in 2001-02.

Senator Hill—But if there is an extraordinary increase, say an argument of wanting to vary the capability or failure of a major contract or something, then under our arrangements Defence would have to go back and seek a whole-of-government approval to that change. I do not think that is the problem. I think historically the problem has been that, more often than not, in determining the desire to achieve a certain capability the price that has been put alongside it has been grossly underestimated. That has remained a problem pretty much up to now. A lot of thought has been given to how that can be improved in the future. I hear lots of reasons as to why it occurs, but the bottom line is that it does make planning for delivering a range of capabilities according to a schedule almost impossible.

Senator HOGG—Thank you, Minister. Just one final question. It is a fairly specific question. On page 75, in the new capital equipment projects proposed in 2002-03, there is an air warfare destroyer study. Is it normal to include that sort of expenditure under capital equipment projects where there is a study?

Mr Roche—Yes, it is. I think that probably what is unusual is that we are intending to spend more up front on projects these days than we have in the past. But there are a number of expenses connected with the project that are capitalised both during the progress of the project and in the initial stages.

Senator HOGG—In respect of that particular study, I presume it has not been started yet.

Mr Roche—No, it has not.

Senator HOGG—It will be started some time within the next financial year?

Mr Roche—I do not have a time line at this stage.

Senator HOGG—I am not going to hold you to this. Just broadly speaking, though—it is down to be started?

Senator Hill—There is a range of studies such as the platform designs, combat designs—there are about four different ones.

Senator HOGG—All right. So they are down to be started in this forthcoming financial year. That is what I wanted to know.

Senator JACINTA COLLINS—I had requested Mr Mike Scrafton, Head Infrastructure, Defence, but I understand someone else is acting in his position.

Senator Hill—He is on leave. Mr Pezzullo is able to fill in for him.

Senator JACINTA COLLINS—Minister, whilst we wait for Mr Pezzullo, can you explain the nature of Mr Scrafton's leave?

Senator Hill—He is on recreation leave.

Senator JACINTA COLLINS—Is that standard practice for this department—for senior officers to take recreational leave during the main budget round?

Dr Hawke—Not necessarily. But one of the things that I have been doing is to insist that the SES people manage their recreation leave credits down because a lot of them have had a habit of basically not taking their leave. I believe that it is incumbent upon me and them to take their leave for the purpose for which it is made available. It may well have suited Mr Scrafton to do that around this time, because I think we are on the verge of school holidays or the like.

Senator JACINTA COLLINS—Canberra school holidays, is it?

Dr Hawke—Yes.

Senator JACINTA COLLINS—I am not aware of it being school holidays.

Dr Hawke—I think we are within a week or so of school holidays. But it is recreation leave he sought and in my view he was entitled to have it.

Senator JACINTA COLLINS—I thought the school holidays were during the break in late June and July.

Senator WEST—I thought that was when it was.

Senator JACINTA COLLINS—Yes, that is our understanding of ACT school holidays. What period of leave is Mr Scafton on?

Senator Hill—I do not understand what is going on here. The officer that you have requested is on leave. I understand the matters that you wish to raise are historical and therefore did not occur on his watch in any event.

Senator JACINTA COLLINS—No, that is not quite true, Minister.

Senator Hill—You have been seeking to call him for other committees—

Senator JACINTA COLLINS—No, I am not, Minister.

Senator Hill—in an attempt to subvert a decision that the government had made—

Senator JACINTA COLLINS—No, I am not, Minister.

Senator Hill—and now we seem to be playing another game or at least another chapter of the same game.

Senator JACINTA COLLINS—Minister, I am not playing any game at all.

Senator Hill—Then, Mr Chairman, I invite all questions to be asked of me.

Senator JACINTA COLLINS—Chair, would you allow the minister to let me conclude a sentence.

ACTING CHAIR—Order! The minister has invited questions to the person to be asked of him.

Senator Hill—To be asked of me and either I will answer them or I will determine who can answer them.

Senator JACINTA COLLINS—The questions I sought to address to Mr Scafton on relate to his position as Head Infrastructure, Defence. They relate to his dealings with *Cerberus*—and there may be some question about his ability to answer some questions in this area—both during his period on the minister's staff and after his period on the minister's staff.

Senator Hill—What I was going to say is: if you ask me a question that I think should be answered by him and that question relates to his work in the department, when he worked in the department as an official, then it might be that that has to be deferred until another day, but I—

Senator JACINTA COLLINS—So you are suggesting that we might need to call him back?

ACTING CHAIR—Order! Senator Collins, let the minister finish, please.

Senator Hill—But that is why I would like to hear the questions. If you are going to ask questions relating to his duties within the previous minister's office—

Senator JACINTA COLLINS—No.

Senator Hill—Then you might as well not waste your time.

Senator JACINTA COLLINS—I have got no intention of wasting time, Minister. I think that perhaps—

Senator Hill—I must have misunderstood what you just said then.

ACTING CHAIR—Ask your question, Senator Collins.

Senator JACINTA COLLINS—Chair, when I made my request to talk to Mr Scafton, as Head Infrastructure, Defence, I was quite clear as to the purpose for which I sought to speak to him. The minister has already alluded to a suspicion that I might want to cover other areas, which is no more than a suspicion, and the minister should calm down a bit.

ACTING CHAIR—No, I am asking you to ask your questions; I am not asking anybody to calm down. If you have questions to put to the committee, put the questions and we will get the answers if we can.

Senator JACINTA COLLINS—With respect, Chair, the minister made a statement and I am going to seek clarification of one component of it.

ACTING CHAIR—Ask for clarification then. Do not make a statement.

Senator JACINTA COLLINS—The clarification I am seeking from the minister is that in his earlier comments he indicated that, if it were clear that the questions I was asking needed to be addressed by Mr Scafton, we could bring him back. Did I misunderstand his intention there or is that what he is prepared to do?

Senator Hill—What I said is that, if I form the view that the answer is only within the knowledge of Mr Scafton, I will seek to accommodate you after Mr Scafton returns. But until I hear the question I cannot do that. It may well be that Dr Hawke can answer the question.

Senator JACINTA COLLINS—It may be.

Senator Hill—We only go down the line when something is within the knowledge of the individual that is not held by the more senior officer.

Senator JACINTA COLLINS—There are two issues here. One is: since when was it standard conduct for senior SES officers to take leave during the main budget round of estimates? I do not think that Dr Hawke adequately dealt with that issue.

ACTING CHAIR—That is your opinion. He has answered your question, and that is all he has to do.

Senator Hill—I have never really addressed that. I have been in committees where I have sought to examine a witness and I have been told that the witness is on leave and everybody has accepted that that is an understandable thing. If it was Dr Hawke on leave, it might be less understandable, but I am very pleased to say that he will be sitting here for three days to assist the committee in its efforts.

Dr Hawke—I am very delighted to be here.

Senator JACINTA COLLINS—Let me say that it is quite understandable, except when the minister is being paranoid about what a senator's intentions might be.

ACTING CHAIR—That is a comment, Senator Collins. Can we move to questions. You can make your comments in the chamber.

Senator JACINTA COLLINS—I will move to my questions in relation to an SSL Asset Services contract with Ridgewell Pty Ltd. I am not sure who I should be directing these questions to.

Senator Hill—You can direct them to me.

Senator JACINTA COLLINS—Can you explain how Mr Ashman and his company, Ridgewell Pty Ltd, were paid \$174,275 for works on a junior sailors galley at HMAS *Cerberus* when no-one in the Defence Estate Organisation or SSL Asset Services could find the contract for those works?

Senator Hill—No, I cannot, personally. I will seek advice. Can anyone help?

Mr Carmody—The issues of *Cerberus* are the subject of an ANAO investigation, which was commenced at the previous minister's direction. The ANAO investigation is not yet complete. We have a draft report and we have, I think, until the 20th of this month to respond, but ANAO's fieldwork is still ongoing.

Senator JACINTA COLLINS—Is that the report that the minister would have been referring to in a letter to the shadow minister for defence, when he indicates that he has directed the head of Defence Estate to implement specific recommendations relating to compliance with entertainment and hospitality, procurement guidelines, developing a capability to hold contractors accountable for poor performance and improving document handling and file management procedures?

Senator Hill—What was the date of that letter?

Senator JACINTA COLLINS—It was 6 April.

Senator Hill—Last year?

Senator JACINTA COLLINS—Yes.

Senator Hill—Mr Carmody, do you know of that letter?

Mr Carmody—That was in response to the investigation by the inspector-general. The investigation by the inspector-general was then followed up by this ANAO investigation at the minister's request. It essentially seems to be validating the inspector-general's original findings.

Senator JACINTA COLLINS—This letter says that the review is concluded and reported to the secretary and that the review found that about half of the allegations were partly or fully substantiated by the available evidence.

Mr Carmody—That is correct. I believe that, in substance, the review found that there was no criminality but that there are incidents where procedures could be improved. It was directed that we seek to improve those. Even though the investigation is ongoing with ANAO, we are still seeking to do that.

Senator JACINTA COLLINS—I have some concerns about a finding of no criminality on the basis of some of the material I understand that has been lost within the Defence Estate Organisation or SSL Asset Services. The contract, in this instance, that I am referring to was significantly amended without the consent of the subcontractor and a copy of that document was handled by SSL Asset Services and by Defence Estate Organisation and I also understand

from my records forwarded to the legal advisers to Defence when they sought to rectify some of these problems with the novation contract, Clayton Utz—a record of losing documents.

Senator Hill—But, with respect, Mr Chair, we know there has been a problem in this instance; that is why it has been subject to previous and ongoing examination, including the most recent one by the Auditor-General. The fact there have been problems need not be debated. Also with respect, it might be that Senator Collins is unwilling to accept the findings of a previous examination. Perhaps, when she takes into account the Auditor-General's view, she might be more willing to accept it. Until we get that Auditor-General's report, it is difficult to debate it here.

CHAIR—I think we will have questions, Senator Collins. If you want to have a debate, have it somewhere else.

Senator JACINTA COLLINS—I am not debating; I am indicating that a document which was handed to Minister Reith in the presence of Mr Scafton has been failed to be acknowledged in this process and this document raises some serious concerns about criminality. You have indicated to me that the inspector-general found no criminality. One of my first questions on that point would be whether the inspector-general had access to that document and what were the circumstances under which that document was amended.

Senator Hill—Can you identify the document to which you are referring?

Senator JACINTA COLLINS—The document that I am referring to was the original contract, which was forwarded by Defence to Clayton Utz.

Senator Hill—So it is a contract between whom?

Senator JACINTA COLLINS—It is a contract between Ridgewell Pty Ltd and SSL Asset Services.

Senator Hill—And the question is: was the contract examined?

Mr Neumann—I do not know what my staff looked at in terms of specific documents. I will have to take that on notice. I say in our report that one of the allegations was that DEO is very professional in doctoring their paperwork to avoid scrutiny and my auditors found that the allegation was not confirmed and that no evidence was found to support doctoring of paperwork by DEO.

Senator JACINTA COLLINS—Was the question of doctoring of paperwork by SSL Asset Services addressed in your review?

Mr Neumann—I think we would have treated it the same way.

Senator JACINTA COLLINS—You treated them the same way?

Mr Neumann—Treated the same way. There were occasions when documents that we thought should have been available were not available, and that was one of our findings, but in terms of doctoring it I do not think my auditors would have made a distinction between one or the other; so if they thought there was an issue they would have raised it.

Senator JACINTA COLLINS—What of these short-order contracts that are used with contractors within Defence Estate or SSL Asset Services? I do not know if this fits your definition of doctoring but—

Senator Hill—You have raised the question of doctoring. I was going to ask you what you mean by doctoring?

Senator JACINTA COLLINS—I thought I asked if significant changes were made to a document. I might be wrong—I am tired, it has been a long day and maybe I said ‘doctoring’ but I do not recall doing so—so let me go through the circumstances of this document.

Mr Neumann—The informant we had used that terminology.

Senator JACINTA COLLINS—There you go, Minister, it was not mine.

Senator Hill—I still do not understand what it means in terms of a contract. But the point is that it was examined by the inspector-general and his staff and it is now being examined by the Auditor-General, and I cannot immediately think of a more authoritative process to give public confidence to this matter than what has and is occurring.

Senator JACINTA COLLINS—My questions go to the scope of that investigation and whether that investigation was provided material that I am aware was provided to the minister and Mr Scafton in relation to the operations at *Cerberus*.

Senator Hill—I think if you are identifying a particular document, the inspector-general and his staff should be able to check the records—I am not saying they can do it now—and ensure that they had access to that document. If they did not have access they might explain why they did not have access. As I understood it, it is the principal contract that you are talking about between—

Senator JACINTA COLLINS—It is the original contract between Ridgewell Pty Ltd and SSL Asset Services.

Senator Hill—And dated when?

Senator JACINTA COLLINS—There are actually two dates because that pertains to the circumstances of this contract, which is concerning. There is the short order form which was submitted as the tender, which was then accepted as the successful tender. The date of that is signed and witnessed on 19 October 1999 and I think it was filed on 20 October 1999. It was then signed on behalf of SSL Asset Services and amended somewhere before 16 November 1999.

Senator Hill—I think my answer stands that we will get you an early response on whether the inspector-general had access to that document. If he did not have access to it and you have access to it, perhaps you might make it available.

Senator JACINTA COLLINS—Yes, I may. But I would rather understand whether, having been furnished to the minister’s office, it was then passed into that process first.

Senator Hill—I do not know that it was furnished to the minister’s office. Who says that?

Senator JACINTA COLLINS—The member for Holt provided it to Minister Reith and Mr Scafton at a meeting.

Senator Hill—A member of parliament said that?

Senator JACINTA COLLINS—Yes. This issue was being canvassed in the House of Representatives sometime during the course of last year and was probably, in part, the stimulus for this review. What has come to light is that it appears—

Senator Hill—Do you feel that in some way it did not get into the assessment process, so you do not think the Auditor-General has got it either?

Senator JACINTA COLLINS—There are two issues which raise concern in terms of the minister’s response to the material that had been provided to them. One of the issues is related

to delay costs for the contractor. The original contract that I have—that I am advised Mr Byrne was advised that Defence and SSL Asset Services could no longer find—indicated a contractual obligation for delay costs.

Senator Hill—Do you allege that contract was given to the minister?

Senator JACINTA COLLINS—Yes. The minister's response to Mr Byrne indicates that SSL Asset Services delay any contractual obligation to delay costs. Defence, at one stage, had sought to resolve the dispute with a novational contract which failed and the dispute is ongoing. There is an original contract which was provided to the minister, which Defence and SSL Asset Services claim not to be able to find, and I have some concerns about how that original contract has been explained to government and query whether it has been incorporated in this review process. On the face of the document, as I have seen it, what has been done with this document is possibly documentary fraud.

Senator Hill—What I do not understand is: if it was provided to government and government set up an inquiry process then I cannot see any reason why it would not be available to that inquiry process.

Senator JACINTA COLLINS—Let me explain that to you then. The minister's response to Mr Byrne—which I suspect was drafted by Mr Scrafton, but I cannot ask him what documents he relied on when he produced this letter because he was not here—addresses the issue of delay costs. Regarding a claim for delay costs, he indicates in his letter:

SSL Asset Services have advised Infrastructure Division that the claim for delay costs was rejected as there was no contractual or other entitlement for Ridgewell to be paid these costs. Ridgewell was not instructed to suspend works and had access to the site for the entire period of the contract.

If you look at the original contract, which Defence and SSL Asset Services claim to no longer have a copy of, it is clear in it that there was a provision for \$250 per day delay costs and yet that is not reflected in the minister's response to Mr Byrne.

Senator Hill—I cannot ask questions of the honourable senator but I am assuming that, if the honourable senator has a copy of this contract—

Senator JACINTA COLLINS—Yes.

Senator Hill—she has made it available to the Auditor-General.

Senator JACINTA COLLINS—I am questioning whether this review that has already been conducted had access to this document. This document has only recently come to my attention.

Senator Hill—I see; we will get you an answer on that. If the inspector-general did not have it, then I would respectfully suggest you provide it to the Auditor-General, who is still in the process of completing his investigation.

Senator JACINTA COLLINS—Yes. As I said, I can imagine that would not be a problem because it was already provided by Mr Byrne to the minister. But, before I provide another copy, I would like to know what happened to the original.

Senator Hill—This is the start of a three-day process and I am sure that, by the third day, we will have an answer for you on it. That will allow all of tomorrow to be subject to an exploratory effort—a search, in other words.

Senator JACINTA COLLINS—Perhaps when you look at the question of the contract itself you will also address the scopes of work relevant to this contract. The minister has

indicated in his answer back to Mr Byrne claims of continuous alterations to the scope of works:

The scope of work in the contract entered into by Ridgewell matches the Defence work brief for SSL Asset Services in respect of the remedial works of the Junior Sailors Galley. The only items varied during the contract were of a minor nature and would be unlikely to have affected the ability of the contractor to deliver the remainder of the work.

My understanding of the facts in this case is that they are very different from what appears to have been purported to the minister. The contract itself indicates significant changes, and I question on what basis the minister's response was drafted. But without Mr Scrafton here—

Senator Hill—I do not think we will ever get an answer on on what basis the minister's answer was drafted. With respect, I do not think that is really the point. The point is that an authoritative and independent investigatory process has been put in place, firstly, through the inspector-general and, secondly, through the Auditor-General. The latter is still current and what is needed is to ensure that all documentation, including whatever has just come to light, is before the Auditor-General so that everyone can be confident that nothing has been hidden and that best efforts are being made to establish the justice of this matter.

Senator JACINTA COLLINS—In terms of the inspector-general's investigation, I also ask whether it dealt with the various scopes of work that occurred in this matter. I have verbal confirmation from a gentleman previously employed by SSL Asset Services at HMAS *Cerberus*—and this, in part, perhaps provides additional information, or maybe it was addressed and discounted; I do not know at this point—that he sighted at least three different scopes of works, file 1-5 for building 523 for the junior sailors galley contract and that they were forwarded by a document transmittal service to SSL Asset Services in North Melbourne in September 2001, some weeks after the issue was first raised in the *Herald Sun*. It may be that the inspector-general was aware of the loss of these documents and can explain how they went missing but, at this stage, we have no explanation for how those documents went missing.

Senator Hill—I do not know whether documents are missing. Mr Neumann, was the issue of the scope of works looked at as part of the investigation?

Mr Neumann—We looked at the allegations made by a particular informant. We looked at the accommodation roofs of *Cerberus*, which would be the dislodging of roofs; the junior sailors galley cafeteria; and the replacement of floor tiles. We confirmed the allegation that tiles were replaced at departmental expense—

Senator JACINTA COLLINS—I missed what you said there.

Mr Neumann—The allegation that tiles were replaced at departmental expense was confirmed, although the cost of replacement claimed varied slightly from the actual. I think it said in January 2000 that it cost \$160,000. The allegation was that the original floor tiles specified and laid by these consultants and contractors did not meet OH&S standards. The response is:

The consultancy report sighted indicated that the tiles originally specified and laid did meet the relevant standard 3661 at the time they were installed. However, six months wear negated this.

Senator JACINTA COLLINS—Six months wear negated that they met a standard?

Mr Neumann—Yes, the OH&S standards.

Senator JACINTA COLLINS—How would that occur?

Mr Neumann—By the wearing away of the non-slip surface, I presume.

Senator JACINTA COLLINS—The non-slip surface wore away in six months so they needed to be fully replaced, to the cost of Defence.

Mr Neumann—No. It was replaced at Defence expense.

Senator WEST—Do non-slip surfaces usually last only six months?

Mr Neumann—I do not know; I am not an expert in this field.

Senator WEST—Neither am I, but if I bought something for the house I would want it to be going a bit longer than six months.

Senator JACINTA COLLINS—I am curious about what standard is applied if the non-slip surface can disappear in six months.

Senator Hill—Is the point that the allegation is that the Commonwealth paid for work that was unnecessary?

Senator JACINTA COLLINS—The allegation that the inspector-general was referring to was twofold: firstly, that the contractor did not perform to Commonwealth standard—that is, fit the appropriate tiles—

Senator Hill—That is a normal civil dispute. There is nothing extraordinary in that.

Senator JACINTA COLLINS—That is right. Secondly, rather than resolving it as a normal civil dispute, Defence itself simply paid to replace the tiles.

Senator Hill—Rather than pursuing the contractor.

Mr Neumann—That is right.

Senator Hill—Who benefits out of that?

Senator JACINTA COLLINS—The taxpayer does not.

Senator Hill—I suppose the contractor does because he is not forced to remedy his default. But I still think that, if the matter is now the subject of investigation by the Auditor-General, that is the best way to go forward. We will get the inspector-general to get answers to the questions you have asked but, really, his contribution to this process is to some extent historical now; it has been overtaken by the Auditor-General's examination.

Senator JACINTA COLLINS—Yes, if the Auditor-General's examination is picking up this material originally raised by Mr Byrne for the answer I am seeking.

Senator Hill—You should have a talk with the Auditor-General.

Senator JACINTA COLLINS—Yes, we possibly should; but until I ascertain what was already dealt with by the inspector-general it is hard to do that.

Senator Hill—I do not think so at all. You speak to the Auditor-General and check that he has the information that you want him to consider. But we will in the meantime see what information the inspector-general has, because that might be of some historical relevance at least.

Senator JACINTA COLLINS—Did the inspector-general's investigation deal with the role of Defence Estate and SSL Asset Services with respect to *Cerberus*? What was the full scope of that investigation?

Mr Neumann—We got a series of allegations which run to over five pages; we looked at each allegation made.

Senator JACINTA COLLINS—Is there any reason that report cannot be made available to me?

Mr Neumann—It has people's names in it and, at the moment, it has legal-in-confidence on it. Presumably, if we take out the names that might make it available. The informant particularly did not wish to be identified, and the name is in there.

Senator JACINTA COLLINS—Perhaps you could remove any areas where there are confidential concerns and make that report available to me. That might fast track dealing with these issues. I am happy to follow the minister's approach, which is to look at what information you can provide and then deal with what additional questions I might have following from that, because I have broader questions than just this particular contract at *Cerberus*. I also have questions about the comprehensive maintenance contract, both at *Cerberus* and more generally in Victoria. You may have dealt with that as well.

Senator Hill—You had better tell us what your questions are on that. That is historical too; is that a contract that was, rather than something that is, current?

Senator JACINTA COLLINS—No, it is current.

Senator Hill—Ask the question. We have the man here.

Senator JACINTA COLLINS—But I am just saying that, if there is a historical component, I can remove some of my questions so that I can deal with it later, once I have dealt with this component. I am suggesting that it might fast-track it.

Senator Hill—If it is unrelated, we might as well get it out of the way.

Senator JACINTA COLLINS—It goes back to the scope of the inspector-general's review of matters originating in allegations coming from *Cerberus*. This contract is connected to the issues of *Cerberus* as well.

Senator Hill—What else is there?

Senator JACINTA COLLINS—I would say that is mostly it. I would suggest that I would wait until you come back to me about the earlier information in relation to the Ridgewell matter.

Senator Hill—So the question is whether the inspector-general had the contract?

Senator JACINTA COLLINS—It is about the full scope of the inspector-general's investigation. I can now look at the full scope—

Senator Hill—He can tell you that now. Can we get a written response on the full scope of the investigation? That will not be difficult. You want advice on whether the inspector-general had access to the contract or contracts or maybe you want to know what contracts he had access to.

Senator JACINTA COLLINS—Yes.

Senator Hill—Then you can determine whether there is a missing document. That is basically it, isn't it?

Senator JACINTA COLLINS—If I also then look at the terms of reference for the ANAO report, that may diminish the questions I then need to ask direct to Asset Services.

Senator Hill—We will get a copy of the terms of reference for the ANAO report.

Senator JACINTA COLLINS—As you said, you are here for the next two days. I can come back once I have reviewed that and deal with it then.

Senator Hill—Then we will have another go.

Senator JACINTA COLLINS—Yes.

Senator Hill—Okay.

Senator CHRIS EVANS—I thought I would have a chat with Mr Roche about the Super Seasprite. I suppose the starting point might be the minister or Mr Roche. I appreciated your detailed responses to the questions I asked on notice. One of the key answers was to a question regarding the contracts entered into with Kaman for the Super Seasprites. I understood from that answer that the minister directed the department to continue investigating all options in respect of these contracts—that is, the acquisition and the servicing and, basically, looking at what your legal position was and what might be able to be done in terms of those contracts. I would ask as a starting point: what progress has been made in either renegotiating or seeking relief from those contractual obligations?

Senator HILL—Do you want to bring the committee up to date?

Mr Roche—Two streams of action have been afoot. Firstly, we are still seeking some senior legal advice on our options under the contracts. We already have quite a deal of legal advice, but we are seeking a QC's opinion. At the same time we have had a Defence team negotiating a series of proposals to restructure payment schedules and to tie the acquisition and service contracts together. Kaman have already written to the Commonwealth—and they did this some time ago—saying that they were prepared to link the delivery of the service contract to the delivery of the aircraft; in other words, their undertaking was to provide the amount of service that was originally envisaged in the service contract regardless of the actual delivery of the aircraft.

Senator Hill—Within the existing price.

Mr Roche—Yes, within the existing price; that is an important point. The original contract for in-service was for 10 years and I think that included 9¼ years of actual flying of the aircraft. That is what they have undertaken to deliver. The proposed contract changes—which have not been agreed by the Commonwealth yet, because they have to go to the minister, or indeed by the Kaman board—provide for that linkage: the extension of the in-service support contract out to the full period at no increase in cost, compensating for the fact that the aircraft will be delivered late; aligning payments under the acquisition contract to specific milestones; and changing the withholdings under the acquisition contract to ensure that we have sufficient funds withheld to ensure that fully capable aircraft are delivered.

Senator CHRIS EVANS—Could you say that again?

Mr Roche—We intend to withhold sufficient funds under the acquisition contract to ensure that fully capable aircraft are delivered. It is important in that regard to note that the piece of capability that is missing is the software systems, and we have a fairly good idea of the value of the software systems that are missing because of the contractual discussions between Kaman and Computer Sciences Corporation. We believe that we have withheld sufficient funds to ensure that that is delivered or, indeed, that the Commonwealth could, in the worst case, find its own subcontractor to deliver that capability.

Senator CHRIS EVANS—Have you not paid about 85 per cent of the purchase price already?

Mr Roche—Yes, indeed.

Senator CHRIS EVANS—I thought the software systems were the expensive bit.

Mr Roche—The amount of software remaining is of the order of about \$25 million.

Air Vice Marshal Conroy—I think it is about \$28 million.

Senator Hill—The sophistication of the solution remains the challenge. It is the piece of software that pulls the various systems together so it is critically important but, in terms of the total contract price, it is not a large proportion of the contract. That is my advice.

Mr Roche—We estimate that the value of the system to be delivered is approximately \$US28 million. We are currently withholding \$US40 million from the contract and we will reduce that only when key milestones are met. That means that we are still going to be withholding \$US35 million at a time when the critical design review for the system is completed, and that is in March 2003. That date will precede any acceptance on our part of the helicopter even for interim purposes.

Senator CHRIS EVANS—You are talking about \$40 million out of about \$1 billion that we are going to pay out, though, aren't you?

Mr Roche—Yes, but the piece of the system that is missing—

Senator CHRIS EVANS—Just in terms of withholding, it does not sound terribly threatening in the sense of withholding payment. I am just trying to get to grips with the concept.

Senator Hill—But it is much the same value as the piece that is missing.

Senator CHRIS EVANS—Yes, but in terms of bargaining power \$40 million out of a \$1 billion contract does not sound like you have really got them where you want them. They have got your \$960 million and you only owe \$40 million.

Senator Hill—I understand that argument, but I must say that I feared the last time we met that that critical piece of the jigsaw was a much greater part of the total price than it seems to be.

Mr Roche—There is an addition to these amounts. There are financial guarantees associated with this project in addition to this withholding, which brings the amount that we will be withholding at the critical design review to \$US70 million. And we will still have over \$42 million in total between financial guarantees and withheld moneys at the time of the delivery of the fully capable aircraft. I take your point in relation to the total contract cost, but the critical thing is that these amounts more than cover the risk that we believe there is in software delivery.

Senator CHRIS EVANS—The whole foundation of this had been explained on the basis that this system was critical and that this is what had delayed the project. The impression given was always that it was the major component of the whole thing, but now you are telling me that it is relatively small—certainly in cost terms.

Mr Roche—That is the point: it is relatively small in cost terms but it is very big in impact terms. Until it is there, the aircraft is nothing more than a utility aircraft.

Senator CHRIS EVANS—What is it that we are describing? Both Senator Hill and I were discussing it in very non-technical terms. It would be helpful if someone actually described it for the record. I do not think either Senator Hill or I should be the one to do it.

Mr Roche—I would call it the combat system. It probably has a far smarter name than that. I understand that it is the integrated tactical avionics system.

Senator CHRIS EVANS—What is that?

Air Vice Marshal Conroy—It is the software program that ties together the sensors on board the aircraft—the radar, the datalink and the software that is needed to target the missile. It also generates all the displays on board the aircraft. By having this highly integrated, the intention is that you can do with two crew what you would otherwise need an extra crewman to undertake. That subcontract in this billion dollar program with the Litton company was, to the best of our knowledge, a subcontract let by Kaman to Litton for something in the order of \$US60 million to \$US65 million. As you can see, it is somewhere between 10 to 15 per cent of the total value of the project.

Senator CHRIS EVANS—Litton was the company that defaulted?

Air Vice Marshal Conroy—They defaulted.

Senator CHRIS EVANS—So who now has the contract for this piece of work? I know that Kaman is your main contractor, but are they doing it themselves now?

Air Vice Marshal Conroy—They have engaged two new subcontractors to finish the work. The work is half finished and they have engaged CSC Australia and Northrup Grumman Information Technology of the US.

Senator CHRIS EVANS—So an Australian company is now involved, in partnership, in doing this. Is that a joint project or are they involved in separate tasks?

Air Vice Marshal Conroy—They have a separate contract.

Senator Hill—But have they got separate tasks? Are CSC and Northrup Grumman contributing separate parts of the total package?

Air Vice Marshal Conroy—Yes, that is correct. Northrup Grumman Information Technology are doing the part of the software package that integrates the link 11 datalink and the remaining operational functions are the responsibility of CSC Australia.

Senator CHRIS EVANS—They are both subcontracted to Kaman. I want to go back through those measures that you have just outlined to us.

Mr Roche—There are a few other measures involved. I mentioned the withholding of contract funds and the financial guarantees. We are also looking at roughly halving the monthly in-service contract management fee until the support activities ramp up in preparation for Navy flying. If all of these things come to pass, and if the critical design review in March 2003 is acceptable, by the middle of 2003 we could be looking at the Navy taking on this aircraft for training. At that point, they would have access to 10 aircraft, which would be a significantly greater number than originally envisaged.

Senator CHRIS EVANS—Why is it a greater number?

Mr Roche—Originally, the aircraft were to come on stream more slowly and ramp up to the full number of aircraft. In this case, because we have deferred delivery, the aircraft are basically sitting there ready to be used when we agree that the—

Senator CHRIS EVANS—If you get one ready, you will get them all ready.

Mr Roche—That is right.

Senator CHRIS EVANS—What is the status of this agreement? You say you have not finalised renegotiation of these contracts.

Mr Roche—We have an undertaking from Kaman in writing that they will link the in-service contract to the acquisition contract, but the negotiating team has only just returned from the United States—they were there over the last two weeks of May—and I am waiting for a formal report from that team. I know that the minister is awaiting a formal report from them before we agree to it on our side. It is required to go to Kaman's executive board for their agreement.

Senator CHRIS EVANS—So, during May, you sent a negotiating team to the United States to renegotiate these agreements?

Mr Roche—Yes, we did.

Senator CHRIS EVANS—Who led that?

Mr Roche—Andrew Wood, the branch head.

Senator CHRIS EVANS—Do you see the major challenge as the linking of the two contracts so that the service contract bears some relationship to the delivery date of the helicopters?

Mr Roche—Assuming that Kaman stand by their written undertaking and these contract changes go through, the service contract will provide exactly what it was intended to provide in the first place and at the same price.

Senator CHRIS EVANS—You just said they are halving their in-service fee until things ramp up, so you are still paying the service fee.

Mr Roche—We are slowing down the rate of payment so that it will ramp up further. But the total paid under the service contract will be the total originally intended to be paid for the 10 years of support for flying aircraft.

Senator CHRIS EVANS—But that would be a payment over 12 years or whatever rather than over 10 years.

Mr Roche—The payment is obviously going to extend longer than the original 10 years.

Senator CHRIS EVANS—That tries to link the service contract in and keeps you at the same level of in-service support. You said there were some changes relating to linking acquisition to milestone payments. I thought you told me that was the case last time, and the schedule you gave me included various milestone payments already. I am not quite clear what you are trying to tell me.

Air Vice Marshal Conroy—You might recall that last time I explained that our contract was roughly a fifty-fifty mix between earned value payments and milestones. Whilst earned value is an effective mechanism for when you are producing something tangible, we have come to the view that earned value is not the best way to manage a largely software based contract. The point is that you could do 90 per cent of the work and therefore get paid 90 per cent of the value, but you would leave all the tough nuts to last and maybe have something that does not work. What we have been negotiating with Kaman is to get earned value out of this contract at this stage. So the software is going to be paid for as it progressively develops against a number of milestones.

Senator CHRIS EVANS—Again, we are talking about a small fraction of what is left. We have paid 85 per cent already, haven't we?

Air Vice Marshal Conroy—Yes, but that is not untypical.

Senator CHRIS EVANS—I am just trying to put it in perspective. We are arguing about the last bit, are we?

Air Vice Marshal Conroy—Yes, but in the structure that we have negotiated with Kaman the milestones are heavily back-loaded, so that there is a substantial incentive to complete for the money that is still outstanding. For instance, if you look at the portfolio budget statements, on page 77, you will see a table of major capital equipment projects. In the budget estimate for 2002-03 we had anticipated, under the existing contract, to be paying out \$72 million next financial year. Under this revised contractual change that number will reduce to about \$40 million, and it will probably be about half of that in the following year. So what we are doing is moving the money that we would otherwise have paid earlier, under the earned value regime, towards the milestones at the rear of the program, as an incentive to complete.

Senator CHRIS EVANS—So this is the argument that you are, effectively, withholding till they are fully operational. Is that it?

Air Vice Marshal Conroy—Yes, plus the financial guarantees.

Senator CHRIS EVANS—Where are the helicopters now?

Air Vice Marshal Conroy—There are eight helicopters at Nowra, there are two on the production line and there is a prototype doing developmental work in the US.

Senator CHRIS EVANS—When will those other two be delivered to Nowra?

Air Vice Marshal Conroy—One aircraft will be delivered in the next couple of months. After that, we will leave two aircraft in the US doing prototyping and developing work until that is finished.

Senator CONROY—So you have just got them in storage at Nowra, basically?

Air Vice Marshal Conroy—They are in build-up. A lot of the installation of systems et cetera is being done in the hangars at Nowra, by Safe Air, a subcontractor.

Senator CHRIS EVANS—So there is ongoing work on them now?

Air Vice Marshal Conroy—Yes.

Senator CHRIS EVANS—But that cannot be finalised till the crucial bit of software is—

Air Vice Marshal Conroy—It will be finalised in time for the decision we take to start flying for flying training and ships qualification trials in the utility role, with the existing software. You might recall that the existing software does allow the aircraft to be flown. We have chosen not to embark upon flying activities until we have some confidence that the new software subcontractors are actually going to produce to the latest notified schedule.

Senator CHRIS EVANS—So where are we in relation to confidence about that? Confidence is a hard thing to measure, but where are we at with that process and assessing whether or not that is on track now? I presume that is separate from the negotiations. Kaman's was about trying to sort out the contracts—

Air Vice Marshal Conroy—Indeed.

Senator CHRIS EVANS—and the payments, but your critical issue remains whether they have got the ability to solve your software problem, doesn't it?

Mr Roche—It is not so much a software problem as a task, Senator. There are a number of critical points in this process. One of the reasons why this took some time to untangle was that when Litton and Kaman parted their ways, until Kaman were able to produce a new subcontractor that had credibility in our eyes we had no real confidence that the project could be delivered. They are now in contract with CSC, but that took probably the best part of last year to happen.

Senator CHRIS EVANS—This is only a recent development, that CSC—

Mr Roche—They have been working with CSC. CSC were actually connected with the project; they were going to be responsible for support from the Australian end, so they were not newcomers to it. But in terms of actually getting a contract with them, Kaman had to get a contract with CSC, and CSC were not about to commit to something unless they were convinced that they could deliver it at the price. So there was a pretty hard negotiation between CSC and Kaman. That contract is now in place. We have had separate discussions with CSC and we have undertaken software reviews of CSC's capability. We have made a number of suggestions to them about things they need to do and we have got undertakings from them. So our confidence is improving all the time in relation to that.

Senator CHRIS EVANS—Do I take it that CSC are doing the hard bit—to use a non-technical term?

Mr Roche—CSC are critical to this. They have to succeed.

Senator Hill—I think the question was: is the risk in the CSC part or in the Northrup Grumman part or both?

Mr Roche—I would think it was CSC. My support team agrees. The tricky bit is in the CSC side.

Senator CHRIS EVANS—I think they said both, actually.

Mr Roche—Yes. You need both. The question is which one is the harder one.

Senator Hill—But I think what Senator Evans is asking, and it is certainly a question that I have been asking, is: in both of those critical contracts, when are the key assessments intended that will give government greater confidence that the capability will be delivered?

Mr Roche—The critical date is the critical design review and that is March 2003. Until that critical design review, we will not be absolutely confident that it is going to come together.

Senator Hill—Does that cover both the Northrup Grumman part and the CSC part?

Mr Roche—Yes, it does.

Senator CHRIS EVANS—Basically, they both have to have solved their side of the problem by March 2003.

Mr Roche—They have got to have a very detailed way forward, a very precise design that shows us that they know exactly what the problem is and how they are going to solve it—the whole shooting match.

Senator CHRIS EVANS—What happens if at March 2003 they come up short? What do we do then?

Mr Roche—We clearly have a problem if they do not make that critical design review, but we are putting an extraordinary amount of effort into ensuring that they do. That is why we have spent the time assessing CSC's ability to do this. I think Northrup Grumman have done more of this work than CSC so I think we have some confidence about that. It is being managed and monitored very closely. We are doing everything that we humanly can at this stage.

Senator CHRIS EVANS—I do not have any doubt that you are taking a bit of interest in the success of the project but I guess I am asking you what is plan B? If they cannot do it, are these helicopters useless?

Mr Roche—It is hypothetical.

Senator Hill—I really do think that cannot be answered at this time. These critical design reviews seem to be part and parcel of all these complex programs of system integration. You can ask the same question with each of the contracts. If we take the AWACS one, which is the biggest and most complex of all, it seems to me that every couple of months there is another critical design review. The answer basically is: if it fails you go back and find another way of doing it. The problem with this contract is that that which we are still awaiting to be done should have been done a long time ago and did not get done because of the failure of the principal subcontractor and of all the complexities that flowed therefrom. The advice that I have is that it is back on the road. The department has confidence in the new subcontractors. It has carried out every test it can to give itself confidence that they can deliver the outcome that they are seeking. There are now a new set of critical dates and they are working to those dates. At the same time we are seeking to reschedule the payments to be able to better reflect the reality of the new time lines.

Mr Roche—And we will be withholding more than the value of that software by a fair margin.

Senator CHRIS EVANS—I accept that. But certainly my exposure to this issue has been that this is the critical component to bringing the systems together. It still seems to me it is relevant to ask: if these people cannot solve the problem at March 2003 what then are your alternatives?

Senator HOGG—Following on from that, can I ask is there someone else who can resolve the problem? Do we know that there is a fall-back position to another contractor with the skills to deliver what this contractor might not be able to?

Mr Roche—There are a number of companies in Australia that have the type of competence that we want. Not all of them are familiar with this system, but CSC has an advantage in the sense that it has been associated with this project already so it has a running head start. But I have to emphasise that we have put a considerable amount of work into assuring ourselves that CSC understands this problem and has the capability to do it. So you are talking about a situation that I find pretty hard to conceive happening at this stage.

Senator CHRIS EVANS—You say you have now sought senior legal advice. I presume you have had legal advice from a firm previously. Who has been providing that advice on those contracts?

Mr Roche—Blake Dawson Waldron have been providing advice to date.

Senator CHRIS EVANS—You have now sought advice from a QC. Whose advice have you sought?

Mr Roche—Bathurst QC.

Senator CHRIS EVANS—And that goes to which issues?

Mr Roche—I mean we are getting into some fairly difficult commercial areas here. I do not know that I would want to tip our hand about the precise nature of that advice that we are seeking.

Senator Hill—Obviously it is sensible to know all of your options, but the option that we are seeking to pursue at the moment is principally to get the equipment delivered with the capability that we contracted for within price and as quickly as possible, recognising that there is nothing that we can do that will not result in being now some years late. The best advice I have got is that we can still get the aircraft with what we contracted for within price. That is the emphasis of the direction that we are taking at the moment.

Senator CHRIS EVANS—All right. I assume that this legal advice does not relate to the question about renegotiation of the contract and the linking of the two?

Mr Roche—No.

Senator CHRIS EVANS—So that should be able to proceed—

Mr Roche—We have taken separate advice, obviously, on the renegotiation. And indeed I think the team was accompanied by one of our legal advisers.

Senator CHRIS EVANS—So you sent a legal adviser to the contract negotiations in America as well, did you?

Mr Roche—Yes, we did.

Senator CHRIS EVANS—How many people did you send over?

Mr Roche—Four.

Senator CHRIS EVANS—What is the time line? If that contract renegotiation is successful to both parties, when will that be finalised?

Mr Roche—I would expect to see that result within the next couple of weeks.

Senator CHRIS EVANS—Who has to tick off from the Australian government side? Is it just the minister or is that for—

Mr Roche—We have to satisfy ourselves within the DMO. I have not had the opportunity to review the changes at this stage. When I am satisfied I will put it to the minister.

Senator CHRIS EVANS—But that is not a cabinet decision; that is a ministerial decision?

Senator Hill—I will decide what level of comfort I need. It is only \$800 million, isn't it! I might look for a little support in whatever judgment I might make.

Senator CHRIS EVANS—I suspect you will not get the level of comfort you desire, whatever you do. So we are not sure at what level that decision will be made. Have you got an ongoing representative in the US on the Seasprite project? I see some of these credit card bills have been coming through.

Mr Roche—Yes, we have got a resident project team over there.

Senator CHRIS EVANS—A resident project team—how many people are there?

Mr Roche—Ten.

Senator CHRIS EVANS—And they are Defence employees?

Mr Roche—Yes, I think they are mostly uniformed personnel—a mix of civilian and military.

Senator CHRIS EVANS—How long have they been there?

Mr Roche—The team has been there for the duration of the project.

Senator CHRIS EVANS—Back to 1997?

Mr Roche—December 1998.

Senator CHRIS EVANS—And have we had about 10 there the whole period?

Air Vice Marshal Conroy—It has been pretty constant.

Senator CHRIS EVANS—So there are 10 personnel, a mixture of civilian and military, based at the contractors. Are they at Kaman?

Air Vice Marshal Conroy—Yes.

Senator CHRIS EVANS—Where are they located?

Air Vice Marshal Conroy—At Bloomfield, Connecticut.

Mr Roche—We have had some at San Diego. Two of the 10 are at San Diego.

Senator CHRIS EVANS—It would be warmer, anyway. So two of the 10 are at San Diego and the other eight are at Bloomfield, Connecticut. What do they do?

Air Vice Marshal Conroy—They perform Department of State functions. In particular, the team at Bloomfield monitor very closely the refurbishment activity that is occurring on the airframes. They actively participate in how much of the structure is being replaced.

Senator CHRIS EVANS—On the refurbishment of the airframes? Why would they bring expertise for that? I do not doubt the expertise of your personnel, but I do not understand that.

Air Vice Marshal Conroy—The company might make a decision about whether a certain structure needed to be replaced and whether there was corrosion there or not, but we want to participate in that process.

Senator CHRIS EVANS—So your people are checking whether the airframes are corroded or whether they are competent to be maintained?

Air Vice Marshal Conroy—A substantial proportion of the aircraft are replaced, more in fact than Kaman originally intended. About the only piece of the aircraft that are the original structure are the tail boom and a small amount of the floor area. All the rest is replaced—or, as I think I am being advised, something like 70 per cent.

Senator Hill—I am sorry, it is not a chat shop here. You are answering questions specifically and they are being recorded by *Hansard* so I am not sure how much conversation is being recorded and how much is not. What percentage of the airframe is being replaced?

Air Vice Marshal Conroy—It varies from aircraft to aircraft. But it is of the order, I am told, of 70 per cent of the structure.

Senator CHRIS EVANS—To a layman it suggests the question: why did you not start from scratch?

Senator Hill—That is the question. Why would you not start from scratch?

Air Vice Marshal Conroy—I can answer that question. Kaman, in their tender which was submitted back in March 1996, offered two options: one was a complete, new-build aircraft,

and one was the use of refurbished aircraft. The delta cost for the rebuild in the tender was of the order of \$32 million. The tender evaluation, which involved the naval technical airworthiness authorities of the day and DSTO, examined the refurbishment option and concluded that the original build standard and the fatigue testing done by the US Navy were such that they could recommend accepting the refurbishment option in the tender.

Senator CHRIS EVANS—As I understand it—I think you told me last time—the alternative tenderer went for a new airframe, didn't they?

Air Vice Marshal Conroy—Yes, they did.

CHAIR—I have had some indication as to how far we might be able to go this evening. It looks as if we will be going no further than output 1, Defence operations, which may take us up to 11 o'clock..

Proceedings suspended from 6.31 p.m. to 7.33 p.m.

Senator CHRIS EVANS—When did Litton actually default on their subcontract?

Air Vice Marshal Conroy—At the end of the year 2000.

Senator CHRIS EVANS—It has been 18 months since they defaulted.

Mr Roche—I think I mentioned earlier, Senator, that it took the best part of 12 months for them to reach a new agreement with CSC.

Senator CHRIS EVANS—Effectively, this is Kaman's responsibility, isn't it?

Mr Roche—Indeed, it is.

Senator CHRIS EVANS—I am not saying it is not your problem as well, but the buck stops with them in the sense that they have got a contract to deliver the whole package.

Mr Roche—Indeed. And they had to get an agreement with CSC but, given the difficulties they had had with their previous contractor, we saw little point in forcing them at speed into a contract that they might wish to regret later. This was an important contract and it was important that they get it 100 per cent right. We would have liked it to have happened a bit faster, but both Kaman and CSC were cautious about that contract—and I guess, in view of their experience to date, reasonably so from their point of view. It means that CSC has got a very good understanding, in our view, of the contract and what they are entering into and, hopefully, the deal that has been done between the two of them is one that both sides can live with.

Senator CHRIS EVANS—Air Vice Marshal Conroy, these 10 people we have in the United States are monitoring the development of the helicopters. Are we paying for them or is the contract paying for them?

Air Vice Marshal Conroy—No, they are part of my project office budget resource, if you like. It is not paid for by the contract. They are there to examine, scrutinise and accept the contract deliverable requirements as they fall due. They are monitoring the test flying activity that is occurring. They conduct a quality assurance task and, in the case of the two people in San Diego, they are monitoring the activities at Northrup Grumman.

Senator CHRIS EVANS—Will those 10 stay there for the duration of the contract?

Air Vice Marshal Conroy—Some have been replaced by posting action.

Senator CHRIS EVANS—Effectively you have 10 positions there for the life of the contract?

Air Vice Marshal Conroy—We will gradually start winding them down near the end of the contract. We will probably leave a couple of key individuals there longer than others as we finish up.

Senator CHRIS EVANS—You were telling me before about their monitoring of the worthiness of the airframes et cetera, and you indicated that a large percentage of them had been replaced. I saw the *Sunday Age* article on the weekend. What do you know about the history of each of those airframes? Do you have a complete history of those airframes?

Air Vice Marshal Conroy—Under the contract Kaman entered into they were willing to write in a contractual condition that these aircraft were to have a fatigue service life of 10,000 hours against a specified usage spectrum and to be supportable for a period of 25 years. The airframes themselves were stored at a US storage facility and the Commonwealth sent a team of engineering experts to pick those airframes that were in the best condition.

Senator CHRIS EVANS—Is it one of these desert things that they have?

Air Vice Marshal Conroy—Yes.

Senator CHRIS EVANS—Which one were they at?

Air Vice Marshal Conroy—They were near Davis-Monthan Air Force Base. I think they call it AMARC—Aircraft Maintenance and Recovery Centre.

Senator CHRIS EVANS—That means they are stored out in the desert, does it?

Air Vice Marshal Conroy—Yes.

Mr Roche—They were wrapped in polythene for storage purposes.

Air Vice Marshal Conroy—I believe so. They also had the opportunity to inspect refurbished airframes on the production line that were being built for the Egyptian navy. They were able to verify that those airframes were in extraordinarily good condition.

Senator CHRIS EVANS—I presume that the ones for the Egyptian navy were not the same product that we are buying when remodelled? I know the Sea Sprite comes in a range of variations. What they are buying is not what we are buying, I gather.

Air Vice Marshal Conroy—Yes, it is different, but the rework of the fuselages is very similar, I understand. Our people selected those airframes; they had the pick of them and they chose the best. That was not necessarily the latest built aircraft, as it turned out.

Senator CHRIS EVANS—From the information you have given me, a number of them have been remodelled already.

Air Vice Marshal Conroy—Yes.

Senator CHRIS EVANS—In fact, one has been remodelled a couple of times, I gather.

Air Vice Marshal Conroy—Yes. But you have to realise that helicopters are a little different from fixed-wing aircraft when it comes to refurbishment. One would be much more circumspect about trying to relife or refurbish a fixed-wing aircraft because fixed-wing aircraft bear most of their loads through their primary structure. In the case of helicopters, it is a truism to state that the majority of loads are borne through the rotors and the gearbox rotating components. So it is quite a feasible proposition to relife a helicopter fuselage, particularly one of that vintage.

Senator CHRIS EVANS—I tried to convince some of them—they asked me about it the other day—that there is still some life in things that were 40 years old, but I found I was not making a very convincing case.

Air Vice Marshal Conroy—We can call a technical expert to explain to you why this is a reasonable and rational prospect, if you wish.

Senator CHRIS EVANS—I was referring to myself, Air Vice Marshal, not the helicopter.

Senator HOGG—That is why I thought life began at 40.

Mr Roche—We do have available Air Commodore Schmidt, who is the head of the technical directorate in the Air Force, and he is familiar with this helicopter proposal.

Senator CHRIS EVANS—I am happy for you to get whomever you think is appropriate. I wanted to come to this: you have a life history of each of these airframes. Is that right? Air Commodore Schmidt, I found on the web a history of the New Zealand Seasprites. Someone had a complete history of the airframes. Do you have that information available for each of the ones we are using as the basis for our purchases?

Air Cdre Schmidt—No. I will explain where I come from. I am the technical airworthiness authority. I respond to project requirements. If it is a specific project issue, I leave it with the project authority. In fact, I think they have done some surveys and comparisons with other operators. Once an aircraft is presented or acquired I ultimately have to make sure that it is safe and airworthy on introduction to service. Therefore, I am certainly responsible for applying rigorous and appropriate technical standards and going through a certification process. That is what I am looking at with respect to the documentation for these aircraft which are being offered at the moment. I have not done any broader surveys as to other aircraft—in this case, the New Zealand aircraft.

Air Vice Marshal Conroy—We do have a complete history of these aircraft, which we will be presenting for certification at the appropriate time.

Senator CHRIS EVANS—That history takes you through their original form, their reconditioning or whatever the appropriate term is at various stages, where they have been stored and all those sorts of things?

Air Vice Marshal Conroy—Yes.

Senator CHRIS EVANS—Despite that, you are saying that large parts of them have been cut out because of issues of rust or concern about the airframe durability?

Mr Roche—It is important to note that Air Vice Marshal Conroy did not actually say that. He made no comment about rust or anything like that.

Senator CHRIS EVANS—I think you will find that the *Hansard* will prove you wrong there, Mr Roche, but we will leave that to check the *Hansard*. This is not a trick question. As I understood it, the comment made was that up to 70 per cent of the airframes have been replaced because, I presume, one thought a new section would be better than what was there.

Mr Roche—I just wanted to make this point: you said that 70 per cent of the aircraft had been replaced. There has been no comment about the reason for that replacement.

Air Vice Marshal Conroy—It was a judgment made by the prime contractor in order to satisfy the contractual condition to have a 10,000-hour service life. The contractor makes his own judgment on what structure needs to be replaced and each individual airframe will differ

in terms of its condition. I did not use the word rust, but there may be places where there is some minor corrosion and replacement will occur when they discover that, as well.

Senator CHRIS EVANS—Sorry, I am not trying to put words in your mouth. The basic principle is that the contractor, in order to meet your specifications, has decided that some of these frames—up to 70 per cent—have to be replaced. Is that fair?

Air Vice Marshal Conroy—That is correct, yes.

Senator CHRIS EVANS—I am having difficulty coming to terms with why one would want 30 per cent of an airframe to start a new multimillion dollar project.

Air Vice Marshal Conroy—What has been replaced in this aircraft has been the cockpit section almost in its entirety, the upper ceilings—the roofs that carry the engines themselves: complete new engine mounting structures—newer technology engines have been installed, composite rotor blades have been used, completely different nose housing for the various radars and forward-looking infra-red systems that are on board the aircraft. So it is a substantial rework of the existing frames. The reason existing frames were used is that the company tendered an additional price of \$32 million to build new aircraft from scratch.

Senator CHRIS EVANS—Are you saying to me that you think the contractor thought they would get away with more of the old frames than they have?

Air Vice Marshal Conroy—Yes, they did.

Senator CHRIS EVANS—And so you think they have had to rebuild more of it than they had envisaged when they first tendered?

Air Vice Marshal Conroy—I have been told so, yes.

Senator CHRIS EVANS—What sorts of hours would these airframes already have flown? I know you said you can provide me with a service history. Did any of them fly in the Vietnam War?

Air Vice Marshal Conroy—From their build dates, it would appear so. Of the airframes that we selected, the airframe hours vary from about 3,000 through to some 11,000, but it has to be remembered that the airframes have been effectively relined in the construction process.

Senator CHRIS EVANS—Those actual airframes have done 3,000 to 11,000 hours of flying time already?

Air Vice Marshal Conroy—Yes.

Mr Roche—It also needs to be considered against the background that the US Navy has fatigue-tested those airframes to 40,000 hours and that our requirement is for 10,000 hours. The US Navy, I understand, is working on a two-to-one factor.

Air Cdre Schmidt—To clarify that, the fatigue testing was to 20,000 hours—that is, there was a test factor of two. There was a factor of four placed on design but a test factor of two, which means it has been fatigue-tested to 20,000 hours. Might I just clarify that when you talk about airframes there is a lot of new structure; therefore it is not quite correct to say that these airframes—that is, the total structure which has been delivered to us—have seen all of those previous service hours.

Senator CHRIS EVANS—I think that is taken as read, Air Commodore, that only the old bits have seen that much service.

Mr Roche—I think that we are talking about the same thing. My 40,000 hours had to be divided by two.

Air Cdre Schmidt—The service life was 10,000 hours and that needed to be demonstrated either by analysis with a factor of four or by test with a factor of two.

Senator CHRIS EVANS—Are you aware whether any of these helicopters served in Vietnam? Is that part of their history—where they served?

Air Vice Marshal Conroy—Yes, some did.

Senator CHRIS EVANS—Are you able to provide us with that sort of history of them today, Air Vice Marshal?

Air Vice Marshal Conroy—Not today, but we could.

Senator CHRIS EVANS—I thought you had the document in front of you, that was all.

Air Vice Marshal Conroy—No.

Senator CHRIS EVANS—If you could take that on notice, I would appreciate that. Apart from the remodelling for the Egyptian navy—and I think New Zealand bought four—are there any others of that vintage being remodelled?

Air Vice Marshal Conroy—I understand that a foreign military sales contract has been let for some aircraft for Poland and there could be a prospect of a follow-on Egyptian buy as well.

Senator CHRIS EVANS—While these are based on the same frames, what they are purchasing is not necessarily the same. The command system argument is not one that is live for New Zealand, Egypt or Poland. They are buying a different command system package.

Air Vice Marshal Conroy—Yes, they are different avionics.

Senator CHRIS EVANS—Would we argue that ours are superior technology to what they are selling to Egypt, Poland and New Zealand?

Air Vice Marshal Conroy—Indeed, I would argue that. When we get through the current difficulties it will be a very capable helicopter.

Senator CHRIS EVANS—In layman's terms, what is the substantive difference between what New Zealand bought—and I think they have had theirs delivered—and what we bought?

Air Vice Marshal Conroy—Basically, instead of a glass cockpit, the New Zealanders have traditional round dial cockpits. Their systems are not as integrated in their software. Instead of being able to fire the Penguin missile, the New Zealanders opted for a missile called the Maverick, which is a shorter range infra-red missile.

Senator CHRIS EVANS—As I understand it, we did not actually buy these originally for the Anzac, did we?

Air Vice Marshal Conroy—Yes, indeed, we did. The existing Seahawk helicopter would have fitted on the Anzac. At the time there was a joint project with Malaysia for a joint patrol vessel. We were planning it at that stage as the replacement for the Fremantle patrol boats and that was a much smaller vessel. It would not take Seahawks, so the decision making of the time was that an intermediate size helicopter—something smaller than a Seahawk but not a light helicopter—would be purchased for both this patrol vessel and the Anzac frigates. That is how it came about.

Senator CHRIS EVANS—When was the patrol vessel project abandoned?

Air Vice Marshal Conroy—That was effectively abandoned in February 1998 when Malaysia selected a German tender over the one submitted by the Australian company.

Senator CHRIS EVANS—So the rationale for going for the Seasprite over the Seahawk disappeared, did it?

Air Vice Marshal Conroy—It did, except that we had signed the contract for the Seasprite on 26 June 1997.

Senator CHRIS EVANS—Why was that?

Air Vice Marshal Conroy—That was driven by the requirement to get a helicopter for the Anzacs as soon as possible.

Senator CHRIS EVANS—But it seemed to me there was obviously a link into this other patrol boat project which then did not go ahead. Isn't it the case that you could have settled for the Seahawk?

Air Vice Marshal Conroy—It would have meant breaking the contract with Kaman.

Senator CHRIS EVANS—If a contract had not been signed then, wouldn't we have just got more Seahawks?

Air Vice Marshal Conroy—That was certainly an option we could have pursued. It is a hypothetical situation. I do not know what our decision would have been.

Senator CHRIS EVANS—Forgive me, I am not after a highly technical explanation, but what is the difference in the capability between the Super Seasprite and the Seahawk in general terms?

Air Vice Marshal Conroy—Our Seahawk variant is more optimised towards an antisubmarine capability. The Super Seasprite was optimised towards an antisurface ship capability.

Senator CHRIS EVANS—Was that specifically because we needed that antisurface capability on the Anzacs?

Air Vice Marshal Conroy—That was the operational requirement of the day, as I understand it. But there is a variant of the Seahawk that can undertake antisurface ship capability, so we could have acquired a Seahawk to do that.

Senator CHRIS EVANS—I know that is a hypothetical question now. Did we purchase the Seasprites because they had a superior antisurface capability or was it more to do with the size?

Air Vice Marshal Conroy—It was entirely due to the size. There is a variant of the Seahawk that carries the Penguin missile.

Senator CHRIS EVANS—So effectively we could have got the same capability out of the Seahawk if it was not for the size question. Is that fair?

Air Vice Marshal Conroy—Yes.

Mr Roche—The size was driven by the requirement for the JPV.

Senator CHRIS EVANS—Yes, but that is no longer—

Mr Roche—And the size then drove the RFT and the RFT produced only two bids, the Super Seasprite being the successful one.

Senator CHRIS EVANS—But in a perfect world, if you had not had that contract, you could have then looked again at the question of Seahawks doing the same job?

Air Vice Marshal Conroy—Yes.

Senator CHRIS EVANS—How many Seahawks do we have currently?

Air Vice Marshal Conroy—Sixteen, Senator.

Senator CHRIS EVANS—I gather the Super Seasprites will have Penguin missiles. I think you just confirmed that for me.

Air Vice Marshal Conroy—Yes, they will.

Senator CHRIS EVANS—Have they begun to be delivered?

Air Vice Marshal Conroy—Yes, they have. That contract is running without any significant schedule problems.

Senator CHRIS EVANS—I should allow you five or 10 minutes to expand on that, just to even it up.

Air Vice Marshal Conroy—Oftentimes one is confronted with underperforming contractors. We have, with the prime contractor for this particular system, a pretty good performing operation.

Senator CHRIS EVANS—So I gather that Kaman do not do the Penguin as well?

Air Vice Marshal Conroy—No, we contracted quite separately with a Norwegian company for that missile.

Senator CHRIS EVANS—What is the name of the company?

Mr Roche—Kongsberg.

Air Vice Marshal Conroy—Kongsberg.

Senator CHRIS EVANS—What is their contract for? How many Penguin—

Air Vice Marshal Conroy—The number is classified, Senator.

Senator CHRIS EVANS—Is it for, say, a 10-year contract for regular supply or is it a one-off, all get delivered on day one—

Air Vice Marshal Conroy—We are buying the number of Penguins out of the production lot because there is a production line running at the moment. We cannot run the risk of ordering a couple every year. The costs are not quantifiable in advance. It is a standard problem with munitions. You cannot be assured that production lines are going to be open when you need them.

Senator CHRIS EVANS—How many have you taken delivery of so far?

Air Vice Marshal Conroy—Approximately 10 per cent of the stock.

Senator CHRIS EVANS—When will the remainder be delivered?

Air Vice Marshal Conroy—We have entered into an arrangement with Kongsberg to slow down those deliveries. They have other customers and it suits them to do that. As to the exact details, I will just have to consult for a minute. We have managed to defer the delivery of the remainder until about September 2003.

Senator CHRIS EVANS—So the rest of them will now be delivered in September 2003?

Mr Roche—No, by September 2003. We are making some progression there.

Senator CHRIS EVANS—They will be progressively delivered up until then?

Air Vice Marshal Conroy—Yes.

Senator CHRIS EVANS—We have 10 per cent already. Have we paid for them already?

Air Vice Marshal Conroy—We have paid in the order of 75 to 80 per cent of the contract value.

Senator CHRIS EVANS—So we have paid the vast majority of the contract value on these. When were they originally supposed to be delivered?

Air Vice Marshal Conroy—I have a recollection that they were probably going to come during this calendar year—July 2002.

Senator CHRIS EVANS—So they were due to be delivered by July this year; you put that back by a year and a bit—

Air Vice Marshal Conroy—Yes.

Senator CHRIS EVANS—to September 2003, but you have 10 per cent already and the rest are coming. We paid according to the original schedule, I gather, and you have paid the majority of the contract. Are you able to tell me?

Air Vice Marshal Conroy—No, we would have reprofiled our payments.

Senator CHRIS EVANS—I think you just told me you had already paid 75 to 80 per cent of it.

Air Vice Marshal Conroy—We paid a total of about 85 per cent. We have paid \$170 million out of a \$200 million contract.

Senator CHRIS EVANS—So you paid \$170 million out of \$200 million but the rest will be rescheduled over the period up to September, I presume.

Air Vice Marshal Conroy—Yes.

Senator CHRIS EVANS—I gather from an earlier discussion on munitions that these things have a shelf life. What is their shelf life?

Air Vice Marshal Conroy—The shelf life of munitions is normally the point at which the solid propellant of the motors, in most cases, needs replacing or, if you like, becomes unsafe. The actual shelf life is something we define over the time that we have the missile. It comes with an initial warranted number out of a manufacturer and then, through a surveillance program and testing and looking at proof-tests in other countries and whatever, we make with our own explosives experts our own judgments. It is typical that the shelf life of any missile with a solid propellant rocket motor is about 15 to 20 years, and we would expect that for these missiles. However, in the particular case of the Penguin, certain battery components become obsolete at about the 10-year point and we have programmed in a technology injection at that point. If you like, it is that technology injection point at the moment that could perhaps define the shelf life of the non-explosive or non-rocket motor component, but in reality we would expect to get something out near the 20-year mark.

Senator CHRIS EVANS—And this contract for the undisclosed number of Penguin missiles is expected to last you a while?

Air Vice Marshal Conroy—It is an operational stock, yes.

Senator CHRIS EVANS—There are not the same sorts of issues with shelf life as there would be for things that have a much shorter shelf life; you think 15 years or so is a reasonable expectation?

Air Vice Marshal Conroy—I would expect somewhere between 15 and 20 years.

Senator CHRIS EVANS—How long have these Penguin missiles been around?

Air Vice Marshal Conroy—They were first designed back in the 1970s I expect. They were initially employed as a shore-to-sea type missile for unique Norwegian defence requirements, with fjords et cetera—firing from shore batteries. But they developed an aeronautical version for their F16. That occurred in the 1970s, so the first aeronautical application occurred in the 1970s.

Senator CHRIS EVANS—I presume these are the latest model.

Air Vice Marshal Conroy—Yes, they have been subject to product improvements during their life.

Senator CHRIS EVANS—Can I ask you about the installation of harpoon missiles on the Anzac frigates—

Senator Hill—Do you mean Seasprites?

Senator CHRIS EVANS—No, it is a related issue in terms of the capability of the Anzacs and the role of the Seasprites. If I have got the wrong people here, then I will ask it later.

Senator Hill—I thought we might finish with all the airworthiness stuff. I am not quite sure if we have given the experts the opportunity to explain airworthiness.

Senator CHRIS EVANS—If I have stopped anyone from saying something they wanted to, I am happy to—

Senator Hill—I thought it was left in a slightly unsettled position.

Senator CHRIS EVANS—I am happy, if the officer wants to put something on the record or say something, to give him the opportunity. I am sure the chair will cooperate.

Air Cdre Schmidt—There has been a lot of discussion about ageing aircraft and old aircraft, and I really wanted to stress the point about what causes aircraft to age. There are two elements. One is fatigue—and people have talked about fatigue—and we talked just before about the factor of two and four and the amount of testing that has been conducted. Also, the fact is that the basic airframe itself has certainly been proven through a long service life, to date, not to have any fatigue problems. There are some new rotating components, and they are still going through a test and substantiation process. I still do not have all that data, but this is just routine. It is routine for any civil acquisition that fatigue substantiation sometimes takes a little time to move on. So that is the fatigue side.

I think you have certainly explored the matter of corrosion, but the point that I would like to stress is that there was a lot of emphasis put on the assembly techniques with respect to wet assembly and also corrosion protective compounds—CPCs. All of that is really wrapped up in the word ‘marinisation’, to the point where my specialists—what I call ‘airworthiness compliance finding staff’—have now gone through a lot of that documentation and feel somewhat confident that we have probably got one of the best marinised airframes of the aircraft in the fleet to date. In fact, the comment has been made, ‘Wouldn’t it have been nice to have had this on a couple of other fleets in the past?’ I think that really addresses the two elements—fatigue and the corrosion—with respect to ageing aircraft.

Senator CHRIS EVANS—Did you and Mr Roche resolve in the end whether you had a 20-year or a 40-year test on this?

Mr Roche—I think we might have to go back to airworthiness, Senator.

Senator CHRIS EVANS—Does that mean that you are deferring to the air commodore?

Mr Roche—I always defer to him on airworthiness issues.

Senator CHRIS EVANS—So you say that they have been tested to 20 years?

Air Cdre Schmidt—Not 20 years—20,000 hours.

Senator CHRIS EVANS—Sorry, 20,000 hours.

Air Cdre Schmidt—That is the life of the airframe itself, which needed to be demonstrated by test where components were in fact certified on the basis of tests. There were some other areas where fatigue life substantiation was provided by analysis. That is where a factor of four was applied. That is why there is sometimes a bit of confusion.

Senator CHRIS EVANS—I do not mean to make it our chief debating point, but it seems to me that—

Senator Hill—There are 40,000 hours—is that what you are saying?

Air Cdre Schmidt—Yes. By simple analysis, one needs to conclude that you can get 40,000 hours; however, we apply a factor of four on any analysis against a service life requirement. That is pretty standard within the broader civil plus military airworthiness environment.

Senator Hill—So, if you can test it, you test to 20,000 hours and these airframes will be tested to 20,000 hours?

Air Cdre Schmidt—And overlaid on that is the requirement to test some structure. In a civil environment, some people step back from the need to mandate tests of all structure and allow fatigue design and analysis of some structure, but in a military environment—and certainly in the case of civil authorities for heavy lift aircraft—there is a mandated requirement to test. That is where we come in and apply the factor of two and hence mandate a requirement of 20,000 test hours to certify 10,000 service hours.

Senator Hill—Yes, but I think what some people in the committee might have trouble understanding is that you are testing to give you confidence that you can use the aircraft for 10,000 hours, but it has been suggested that some of these airframes have already been used for up to 10,000 hours. Could you explain—

Senator CHRIS EVANS—I do not really want to open this up, but I think Senator Hill wants it clarified for the record, and that is fine. It has been suggested that some of them have already done 11,000 hours and we want them for 10,000, so it seems to me that puts you over the 20,000—

Senator Hill—So why shouldn't that be a problem?

Air Cdre Schmidt—I am sorry if I have caused a little confusion here, but I think the confusion potentially exists as we look at the total airframe, which consists of both new structure and original structure. With respect to the original structure, I would describe it primarily as a statically loaded airframe. In the fatigue design, it is designed to have an infinite life. So there are really three elements: one is an infinite life of statically loaded

structure under steady state 1 G-loads; we then have a dynamically component structure, which is rigorously tested to 20,000 hours; and there is another element—

Senator Hill—That is different parts of the structure?

Air Cdre Schmidt—Yes. It gets back to critical areas of structure. It is all tiered.

Senator Hill—I am sorry, but I think it is quite important that people understand this. It is not straightforward.

Senator SCHACHT—You can help us out, can you?

Senator Hill—I am trying to help you out. I am trying to help myself out too. When you have a structure that is comprising the old and the new, you have got to test each part according to the function that it performs, do you?

Air Cdre Schmidt—Yes. As I tried to pick up a couple of minutes ago, there is potential confusion here between general structure, which should have an infinite life, versus dynamically component structure, particularly of a composite main rotor blade, the main transmission, the nose transmission and the combining transmission. All of those items are treated differently. Likewise, the tail rotor is treated differently. That is why we come back to the basic structure, which was original, retained structure. Most of that should have an infinite life. A lot of that has already been proven as a result of past experience. No fatigue problems have been identified in most—I cannot say all—of the retained structure.

Mr Roche—And the replaced structure is effectively zero-lived.

Air Cdre Schmidt—Correct. Senator, I hope that has clarified the issue.

Senator CHRIS EVANS—Have you got any further questions, Minister?

Senator Hill—I reckon that is about as clear as we are going to get it.

Admiral Barrie—The next thing is a six-week course.

Senator CHRIS EVANS—I do not mean to be rude; we are just struggling with the technical stuff.

Senator Hill—You have got to understand that we are mere politicians.

Air Cdre Schmidt—I am sorry—

Senator CHRIS EVANS—I am sure your explanation makes perfect sense. It is your audience that is your problem.

Air Cdre Schmidt—I stand before you as an aeronautical engineer. I try to explain things as much as I can.

Senator SCHACHT—The other question, Minister, is: would you fly in one of these frames when it is ready? That is the real test.

Senator Hill—Absolutely. If the RAAF certifies it as safe for 10,000 hours, it will be safe for more than 10,000 hours. Of that I am confident.

Senator CHRIS EVANS—I think we were going to talk about harpoons. I did not mean to get us off the track, but I understood they are installing harpoon missiles on the Anzac frigates, and I just wanted to understand the capability between that and the Super Seasprite and how that goes into a total package, if you like.

Rear Adm. Scarce—The harpoon system is in essence a ship-to-air capability. We are installing them on all of the Anzac frigates—eight harpoon launchers. What else would you like to know?

Senator CHRIS EVANS—So the harpoon is very much an air capability; it is not an antiship capability?

Rear Adm. Scarce—No, it is an antiship capability. Did I say air?

Senator CHRIS EVANS—Yes.

Rear Adm. Scarce—My apologies.

Senator CHRIS EVANS—You had just made it what I thought was clear as to why it was there, and now you have undone that good work. I guess the question is: why do we need the harpoon and the Penguin on the Seasprite?

Rear Adm. Scarce—I will defer to my capability colleagues to explain the reasons for that. My job is to buy it.

Air Vice Marshall Conroy—I think I can explain the difference. The harpoon missile is an open ocean weapon. It is radar guided, inasmuch as it has got an active radar in the nose. It does not distinguish particularly when it gets into the littoral environment. So you can have the missile seduced by land returns, for instance. The Penguin, on the other hand, is quite capable in the littoral environment because it is an infra-red homing weapon; it is not a radar weapon. It will home in on the heat signature of a ship target. I think that explains the difference. They are complementary weapons and they give the ability to operate both in open ocean scenarios and closer in to shore.

Senator CHRIS EVANS—And the judgment is that we need both on the Anzacs, is it?

Air Vice Marshal Conroy—It gives the Anzacs a very good capability under all or most operational scenarios.

Senator CHRIS EVANS—What antisubmarine capability do the Anzacs have?

Air Vice Marshal Conroy—I will defer to Admiral Scarce here.

Adm. Scarce—It has lightweight torpedoes, which are being purchased.

Senator CHRIS EVANS—They are not currently fitted?

Adm. Scarce—We have torpedoes fitted, but we are upgrading those with a lightweight torpedo—a better quality.

Senator SCHACHT—Are these different torpedoes to the ones we have in submarines?

Adm. Scarce—They are.

Senator SCHACHT—Are these aimed at knocking off a submarine?

Adm. Scarce—These are aimed at knocking off a submarine.

Senator SCHACHT—Where did we purchase them from?

Adm. Scarce—The lightweight ones are purchased from France.

Senator SCHACHT—How much was that bill?

Adm. Scarce—I think, from memory, around \$260 million. But that is a project for aircraft as well as the FFG and the Anzacs.

Senator SCHACHT—Can you tell us how many lightweight torpedoes you get for \$260 million—apart from not enough?

Adm. Scarce—That project is doing its cost profile at the moment. We will not know that probably for about another six months.

Senator SCHACHT—How can you say it is \$260 million when you do not know how many you are going to buy or do you say, ‘We have got \$260 million; let’s see how much that buys’? Is that how you do it?

Adm. Scarce—Correct.

Senator SCHACHT—Nothing much changes in Defence.

Senator CHRIS EVANS—Are they to replace the current torpedoes or to augment the current torpedoes on the Anzacs.

Adm. Scarce—They are to replace the current torpedoes on the FFGs, upgrade the ones that are currently on Anzacs and give a new capability to the aircraft as well.

Senator CHRIS EVANS—What is the difference between replacing the ones on the FFGs and upgrading the ones on the Anzacs? You chose your words carefully. I just want to understand the difference.

Adm. Scarce—The current torpedoes on the FFGs are old and need to be replaced with a better capability weapon.

Senator CHRIS EVANS—But are you not replacing the ones on the Anzacs as well?

Adm. Scarce—Yes.

Senator CHRIS EVANS—You used a different terminology. I am just trying to understand what the difference is.

Adm. Scarce—They are fitted to both ships at the moment and we are seeking to upgrade both vessels with this new capability.

Senator CHRIS EVANS—When will that occur?

Adm. Scarce—For the FFGs, they will be replaced during the upgrade program, and for the lightweight torpedo on the Anzacs I have an in-service date of 2005-06.

Senator SCHACHT—When the new ones turn up, what do you do with the old ones? Do you decommission them or have a shot at an old target?

Adm. Scarce—We will still have some in stock which we will destroy.

Senator SCHACHT—Are the new ones going to be a million dollars a pop, a couple of hundred or is it going to be \$50,000 or \$500,000?

Adm. Scarce—I do not have unit prices yet.

Senator SCHACHT—Why did you set the figure at \$260 million to buy new lightweight torpedoes when you do not know the exact number?

Adm. Scarce—We would have had an original estimate of the cost of the unit.

Senator SCHACHT—What was the original estimate?

Adm. Scarce—I do not have that figure. I will see what the documents provide and send it down the line.

Senator SCHACHT—The only other question I have is: are we buying these off the shelf from the French?

Adm. Scarce—We are buying them from a European design. We will build parts of it in Australia. That is what the alliance is working out at the moment.

Senator SCHACHT—How much of it will Australian industry get, as a percentage—10 per cent, 50 per cent—or is it just a straight cop that we buy from the French?

Adm. Scarce—No, it is not a straight cop. We have Thales Underwater Systems here in Australia who are in an alliance contract with EuroTorp to deliver those weapons. So there will be an element of Australian capability in that, but I do not have the precise figure.

Senator SCHACHT—In the industry development section of Defence, do they set a target for these sorts of things? Do you aim for 30 per cent or 60 per cent?

Rear Adm. Scarce—It depends on the project, but we will set an Australian industry participation level. In Anzacs it is around 70 per cent.

Senator SCHACHT—There are \$260 million worth of torpedoes. Are we going to have \$50 million spent in Australia?

Rear Adm. Scarce—We are working with the alliance to determine what is economical to build here, because there is no point in doing it if the numbers are not satisfactory.

Senator SCHACHT—If you look at it the other way, there is no guarantee we will get any percentage, is there? You have decided to spend \$260 million or thereabouts on a number—and we do not know the exact number. You have decided to buy. Do the Europeans, or the French, know that we are going to buy them anyway, which puts them in the stronger negotiating position to keep the lowest level of industry participation in Australia so that they do more of it in Europe, to their advantage?

Rear Adm. Scarce—We are already spending money in Australia because TUS is part of the alliance. At the moment we are working with the alliance to determine the best split.

Senator SCHACHT—Pardon my ignorance, but what is the alliance?

Rear Adm. Scarce—The alliance comprises Defence, Thales Underwater System—which is a French firm with an Australian branch in Sydney—and EuroTorp, which is a European conglomerate. That alliance is now working through delivering the lightweight torpedo to the various platforms that I have identified. It is working to see what are the most economical means of delivering the project to Australia. Part of that will be a requirement to have some Australian participation, but we have not determined the final outcome of that.

Senator SCHACHT—Mr Roche, as the head of materiel purchases—

CHAIR—Senator Evans has some questions to wrap this up, and then we will come to you and you can do your business.

Senator SCHACHT—I am just interested in industry participation—jobs for Australians.

Senator CHRIS EVANS—I am very pleased to hear it. I want to finish up on the Seasprite. I understand Senator Schacht has a couple of questions. What was the answer to the question about what antisubmarine capability the Anzacs have? Is that currently just from the torpedo? And is that considered sufficient?

Rear Adm. Scarce—It is not considered sufficient; that is why we are upgrading it with the new lightweight torpedo. We are also looking, as a separate phase, to try to improve the

sonar performance, the submarine countermeasures and mine and obstacle avoidance sonar. We are trying to look at the whole suite of sensors on the Anzac, to improve them against submarine and mine threats.

Senator CHRIS EVANS—Do the Super Seasprite helicopters have any role in that antisubmarine function?

Air Vice Marshal Conroy—The Seasprite does not carry sonar buoys, unlike the Seahawk, but it can carry the current Mk 46 lightweight torpedo.

Senator CHRIS EVANS—It can. Is it envisaged that it will carry them?

Rear Adm. Scarce—Yes.

Air Vice Marshal Conroy—Yes, it is.

Senator CHRIS EVANS—When the Seasprites are stationed on the Anzacs, will they carry those lightweight torpedoes as part of their normal armament?

Air Vice Marshal Conroy—I understand that is the intention, yes.

Senator Hill—Is that right?

Rear Adm. Scarce—Yes.

Senator WEST—You enjoy estimates, Minister, don't you? You learn lots of things.

Senator Hill—That is not what I had read.

Senator CHRIS EVANS—It was not what I had read either, so I was a bit taken aback by it.

Senator Hill—You learn something every day.

Senator SCHACHT—You have good prebriefings for estimates, I understand, Minister?

Senator Hill—Just occasionally I am right.

Senator CHRIS EVANS—Are there any further advances on the answer to that question or are we all happy?

Senator Hill—There is an obvious question that follows, but I do not think I will ask it. You are paid to ask that.

Senator WEST—You will ask it later, if we do not.

Rear Adm. Scarce—To clarify, the weapons will be carried on the Anzac, the FFG, the P-3C Orions, the Seahawk and the Seasprite.

Senator CHRIS EVANS—As standard issue?

Rear Adm. Scarce—As standard issue.

Senator CHRIS EVANS—Are you happy, Air Vice Marshal, that the Seasprite as commissioned will contain an antisubmarine capacity by virtue of its ability to deliver those lightweight torpedos?

Air Vice Marshal Conroy—The Super Seasprite will be delivered with the capacity to carry the lightweight torpedo, but it does not detect the submarine target itself. It has to rely on some other means of the submarine being detected and passing the information to it across the link 11 datalink.

Senator SCHACHT—Flares, smoke signals, semaphore flags or how?

Adm. Barrie—P-3Cs, long range maritime control system.

Senator SCHACHT—So they find it?

Adm. Barrie—If they find it and they have exhausted their torpedo stocks, then you would whistle up a Seasprite to go and drop torpedos on the targets.

Senator SCHACHT—And hope that the Seasprites are within reasonable range?

Adm. Barrie—That is where the P-3Cs would be operating, in supporting our surface ships wherever they are operating.

Senator CHRIS EVANS—How would the Seasprite be brought into the target, Admiral?

Adm. Barrie—On the datalink. This is the whole point about joint operations. The ships do not go out there by themselves. They go out and we support them. We would detect submarines using either ship sensors, submarine sensors, Seahawks or P-3Cs. The issue about delivering torpedoes is that airborne platforms quickly run out of them, so if you can operate your Seasprites to deliver the torpedoes on top of the contact until it is destroyed then you have got a greater capability.

Senator CHRIS EVANS—Thanks for that. I will leave it at that for the moment.

Senator SCHACHT—Before I get onto the main question I was going to ask, I just want to ask Mr Roche: going back to the lightweight torpedoes, have you, as head of materiel, had any discussion about the capacity of Australian industry to participate in the program of manufacturing them as much as possible in Australia?

Mr Roche—I have certainly had some high-level discussions with them because this is one of our first alliance contracts, and it is a contract form that we are developing, so we are taking a fairly close interest in it. I have not seen a lot of opportunity in the manufacture side; I am seeing much more of the opportunity in terms of integration and any customising that occurs. But, as Rear Admiral Scarce said, we are still in the investigative stages and at this stage it is not clear just how much will come to Australia. Bear in mind that Thomson Underwater Systems is planning to do work in Sydney on this and has pretty much a worldwide reputation for the quality of their work.

Senator SCHACHT—Are you talking about Thomson CSF?

Mr Roche—They are now Thales Underwater Systems.

Senator SCHACHT—But are they a subsidiary of Thomson CSF?

Mr Roche—No. Thomson has become Thales.

Senator SCHACHT—Sorry, I am not up to date on the change. Often, on these sorts of projects, there is some participation during the delivery and assembly stage, and then when the contract finishes there is not much left and there is no ongoing expertise left at any level. Is that going to be the same with this project? Is it unavoidable that we do not end up with much expertise at any level left over afterwards?

Mr Roche—As I said earlier, I think there is considerable native expertise in Sydney in underwater systems, so much so that Australian companies are selling into the international market with sonar systems, towed arrays and all that sort of thing. So I think it unlikely that we will lose the expertise that is injected into this project. Just exactly what form it will take and how much work could be done in Australia, we do not know yet. But the whole thrust of our new approach to defence industry policy is to look for sustainable work. It is not about just doing this one project because we can.

Senator SCHACHT—I certainly hope that is the case.

Senator Hill—You were not here earlier in the day, but Mr Roche and others were making the point that if, out of this consortium, Thales Underwater Systems in Australia can get a contract to provide a part of the torpedo projects on a global basis or the next generation of those torpedoes there may be a much better long-term benefit for Australian industry. The old way of simply paying for the nose cap, or whatever, is not necessarily the best way. Furthermore, more often than not, when we are buying a platform we are now buying its whole-of-life service capability, and there is a lot more work for Australia coming out of that when it is properly negotiated, à la the Eurocopter Tiger contract and the capabilities that are being constructed in Brisbane for the whole-of-life service of those particular aircraft. As I understand it, we do not have a manufacturer of torpedoes in Australia, but we do have companies in Australia that can provide particular aspects of the torpedo business. Part of the purpose of this consortium, this alliance, is not only to get the best capability for us but also to try and find ways in which we can lever the best opportunity for Australian industry.

Senator SCHACHT—The lightweight torpedo has been fully tested in Europe beyond the prototype stage and is now fully commissioned inside European navies.

Rear Adm. Scarce—Yes, it is. It is a known and working torpedo.

Senator SCHACHT—It works.

Rear Adm. Scarce—It does.

Senator SCHACHT—I turn to another matter which I think is part Air Force part Mr Roche. I appreciate the fact that I had a conversation with Mr Roche early last week about this matter and also with the minister's office. It concerns a contract and dispute between Australian Flight Test Services Pty Ltd, a South Australian company, and Defence. As I understand it, Minister, the chief executive of the firm—a constituent of both of us—has been very vigorous in lobbying and speaking not only to your office but also to Senator Chapman and Mr Pyne on his concerns about the state of the contract between his company and Defence. He was informed over the weekend, or it might have been today—I was informed last Friday—that there is to be some sort of independent review of the contract. Can you give any further details than what you kindly expressed to me on Friday to confirm that there is going to be a review.

Senator Hill—We cannot really say any more tonight because we are consulting a possible reviewer. I have not met them personally, but I have read all the papers and it is a very—

Senator SCHACHT—So you have not met—

Senator Hill—I have not met the individual myself.

Senator SCHACHT—The reviewer or the person complaining?

Senator Hill—The person complaining. But I have read all the papers and it is a very complex issue. It is not just a question of interpretation of a contract. It was an unusual step for us to bring in the outside reviewer, for obvious reasons, but we decided in the circumstances that we should do so—and nothing should be inferred from that. We believe it is the best way to make progress in this particular matter, so that is what we are going to do.

Senator SCHACHT—Will there be an opportunity for the chief executive of the company to discuss with you or your officers the nature of the review and the terms of reference before it is announced? Not that you automatically have to agree to his view, but you could meet him out of courtesy.

Senator Hill—It would be a sensible thing to do, because if he is unhappy with the review process I bet he will be unhappy with the outcome. He might be unhappy with the outcome anyway, but it would not be a bad step to at least see if we can take into account his views in the review process.

Senator SCHACHT—Without in any way prejudicing the fact that there will almost certainly be a review, is the dispute with Australian Flight Test Services about one contract in particular or a series of contracts?

Senator Hill—Now that we have decided to go down this path, it would be better to enable the new process to be progressed with as little constraint as possible in terms of what is said in public debate in the meantime.

Senator SCHACHT—I appreciate that, Minister. I understand that on the contractual side there are two issues.

Senator Hill—In many ways it is more of a relationship than a contract as such. There were contracts or a contract.

Senator SCHACHT—That is what I want to get to. I want to separate the two from the relationship thing—and if you do not want to answer for those reasons then you or your officers should say so. What is the approximate value of the contracts between this company and Defence that may be argued over? Are we talking about \$10 million, \$100 million, \$5 million? Can you give us some idea of the size of them?

Senator Hill—From memory—it must be a month ago that I read it—he said that it would be beyond \$10 million or around that figure. He would say that he was induced or encouraged to spend money on very expensive equipment that might not have been strictly part of the written contract—thus you start going down this very complex road. That is why we decided it was better in the end to have it reviewed so that all the circumstances and all the facts could be fairly and objectively looked at.

Senator SCHACHT—As you know, he has spoken to those of us on both sides of politics in South Australia. He indicated that as a result of the dispute—or the contract or the relationship—his company may be in some financial difficulty and that if this review takes a long time, and even if he got a satisfactory outcome, it may be too late for him, particularly for his own company. Will you give a guideline to the reviewer to complete this review as speedily as possible so that we are not saying, ‘Bad luck, you are dead in the grave but we will give you a nice bunch of flowers’?

Senator Hill—We would seek to do it as quickly as possible but it also has to be done thoroughly otherwise we will have another problem on our hands.

Senator SCHACHT—Concerning the dispute with—and I will call it a dispute for the sake of the discussion—Australian Flight Test Services, are there any other similar disputes on a relationship basis with other companies? Is this an unusual case or from time to time are there companies which claim to have signed up for something that never quite turns out the way they expect and the relationship is affected et cetera? Is this an unusual complaint from his perspective?

Senator Hill—It is almost part and parcel of the defence industry, from the biggest players to the smallest players. The expectations are continually changing and there are suggestions for ‘enhancements’ that raise a number of questions: is that or is it not a contractual term and has it been offered or has it been asked for? Whether you are contracting with the world’s

major defence industry suppliers or a small Adelaide business, you tend to have these problems.

Senator SCHACHT—So he is not Robinson Crusoe in this area, irrespective of the merits of his argument?

Senator Hill—No, but he is unique in the sense that every case is different. What we are really seeking to determine is where the merit lies.

Senator SCHACHT—The chief executive of this company has been concerned that he has not been able to get satisfaction because the relationship between him and other senior personnel in the defence department has got to the stage where it is, to say the least, very cool. I do not know how you weigh those things up. Quite clearly, that is a subjective judgment. One has to be very careful about it. Are you aware that that is one of his complaints, Minister?

Senator Hill—I can recall something along those lines in the papers, but I also know that it is not uncommon in disputes of this kind for the complainant to say that he is not getting a fair go because he has fallen out with somebody who is the procuring authority or whatever. That is therefore another benefit in bringing in an outsider to look at all the circumstances. I would be surprised if there is any merit in this because those who are contracting with him also have responsibilities to protect the public purse and to get the best outcome in regard to capability for public money, and there will be differences of view. Obviously there are differences of view here, or else we would not have a dispute.

Senator SCHACHT—When I spoke to him—when your office told me that there was going to be a review—like everybody he may have been a bit impatient, but I thought, on whatever side of politics, a minister is not going to send him a cheque on the basis that he is complaining. There has to be a transparent independent process. Any minister worth their salt is going to make sure, before they hand a cheque over—if that is the way it turns out after an independent review—that they are able to defend it. Someone might say, ‘Save the money on the review and just give me the cheque,’ but that is not the way it works, for quite obvious reasons, even if a review takes some time and it might be costly. I will leave that there.

Senator Evans may have asked some questions on this already, but I wanted to ask a couple of quick questions about the replacement project for the upgrading of the Caribou. Have we got the right people at the table for that?

Senator Hill—Yes.

Senator SCHACHT—Mr Roche, as I understand it, there is a program to replace the Caribou towards the end of this decade. Is that correct?

Mr Roche—Yes, that is in the white paper. Actually, I think it talks about replacing the Caribou capability. It should not be read as an aircraft-for-an-aircraft replacement.

Senator SCHACHT—What is the size of that, as stated in the white paper, just for the record? Are we talking about \$500 million or \$800 million? It is nothing less than \$500 million these days!

Mr Roche—It is actually beyond the white paper period.

Senator SCHACHT—Have we got an estimate of what we are looking at?

Mr Roche—The previous light tactical aircraft project, which was cancelled two years ago, cost \$800 million, I think, at that time.

Senator SCHACHT—Was that for a replacement capability or a replacement aircraft?

Mr Roche—That in fact extended the Caribou capability.

Senator SCHACHT—So that \$800 million was to be spent to extend the Caribous' life?

Mr Roche—No. It was for a greater capability than the Caribou had; it was for a new aircraft.

Senator SCHACHT—It could do more than the Caribou?

Mr Roche—Yes.

Senator SCHACHT—And that was cancelled two years ago?

Mr Roche—Yes.

Senator SCHACHT—Are we now looking at a replacement for Caribou capability? Is that correct?

Mr Roche—That is right, yes.

Senator SCHACHT—How much is that supposed to be worth—do we have a figure?

Mr Roche—It is \$750 million to \$1 billion.

Senator SCHACHT—Towards the end of this decade?

Mr Roche—The year of decision is 2004-05 and in-service delivery is in 2010.

Senator SCHACHT—So the decision could be made right at the end of this term of government, when that term expires in November 2004? So around the budget in 2004, a decision could be made?

Mr Roche—It could be.

Senator SCHACHT—Is there any capability known that can replace the Caribou? Rather than an enhanced Caribou—a plane doing more than the Caribou does—is there a plane on the market, available from all those who want to sell us planes, that would fill the Caribou capability with an increased capacity—stronger engines, higher and faster flying et cetera?

Mr Roche—I think that the light tactical aircraft proposal, which was for a greater capability than the Caribou, as I have said, had got to the stage where there were two tenderers. So, yes, on the face of it there were a couple of aircraft that would meet that bill.

Senator SCHACHT—There are a couple of aircraft capable of meeting that bill?

Mr Roche—They are more than capable—they are obviously larger than the Caribou and they have greater capacity than the Caribou.

Senator SCHACHT—Do they have the same short landing and take-off capabilities as the Caribou—able to land in mud, take off from sand, fly through jungles and so on?

Mr Roche—They both had reasonably short landing capabilities but not as short as the Caribou, from memory.

Senator SCHACHT—Isn't that the problem: the Caribou is a unique plane and its capability of taking off and landing with a reasonable load is hard to replace?

Mr Roche—It is a difficult question because the Caribou will not take current Army vehicles. It is limited to carrying personnel and palletised cargo. The replacement aircraft that was being proposed under LTAC in fact took the standard Army Perentie—that was one of the requirements. That pushed it up a notch. I think that, by the time we get to carefully evaluating the capability requirements, we will need to look very hard at exactly what it is we

are trying to replace. Is it the short-field capability or is it the capability to move a vehicle? This might have to be looked at, too, in the context of other projects which are under way—in particular, Air 9000, for example, with rationalisation of the helicopter fleet. The range of Caribou functions could in fact be undertaken by helicopters.

Senator SCHACHT—Because bigger helicopters are faster and more powerful, with a longer range?

Mr Roche—Indeed.

Senator SCHACHT—So the problem is that you might get a higher capacity plane in terms of carrying equipment but it might not be able to take off from the short airfields and paddocks, which the Caribou apparently does pretty well, I understand?

Mr Roche—It does.

Senator SCHACHT—It is weighing up one against the other.

Mr Roche—And indeed looking at those fields that we do want it to take off from. In some respects, you need to consider whether the investment in a separate aircraft type is warranted when you look at the types of fields you want to get into and whether it might not be worth putting some money into improving some of those fields.

Senator SCHACHT—You cannot anticipate improving every airfield in the South Pacific, or our own area of Australia or our area of interest.

Mr Roche—No, indeed.

Senator SCHACHT—I would like to see you up in the Goroka highlands or somewhere improving an airfield, Mr Roche, but that is another question. I think the Caribou is manufactured in Canada. Is it still being manufactured?

Mr Roche—Not to my knowledge.

Senator SCHACHT—How many other air forces in the world still have Caribou? Do the Canadians still keep it, or are we the only ones who have kept it going?

Mr Roche—I am sure there are a few around, but I do not think there are terribly many.

Air Vice Marshal Conroy—From my recollection there are none operating in Canada.

Senator SCHACHT—There are no Caribou in the Canadian air force?

Air Vice Marshal Conroy—That is my understanding. There were some in the Royal Malaysian Air Force but they have been taken out of service. I cannot think of who the other customers are. There are commercial operators that fly them.

Senator SCHACHT—Apart from the age, what is the biggest problem with them? Is it with the airframes now getting old, or the engines?

Senator Hill—It is the cost of maintenance, isn't it?

Mr Roche—Yes, it is cost of maintenance. I sense that this is not unconnected with your earlier question, Senator, and engines are an issue. They are our last remaining rotary engines.

Senator SCHACHT—Rotary engines?

Mr Roche—Yes, piston engines. No, radial, I should have said. That is dating me a bit!

Senator SCHACHT—They have been around for a while. They were in good service in the Second World War.

Mr Roche—No, World War I, actually.

Senator SCHACHT—That is probably why they work so well on the Caribou, getting in and out. They are unsophisticated but they work. On one of the other areas of definition: in Europe and North America there are designs looking at planes that have a wing where the engine tilts. It has got a rotor like a short take-off aircraft, almost like a helicopter, then the wing swings round and you can go along in horizontal flight like a normal aircraft. Is that one of the areas that you are looking at as a replacement?

Senator Hill—I certainly hope not.

Senator SCHACHT—I certainly hope not, because that is too expensive.

Senator Hill—I could talk to the Americans.

Senator SCHACHT—The Americans would love to flog you one, I presume.

Senator Hill—I do not know that they would. It is proving a very difficult technology.

Senator SCHACHT—I know it is a difficult technology. That is why I am interested whether—

Senator Hill—It is very expensive, and has great uncertainty.

Senator SCHACHT—Obviously, Minister, they will have to have a good case to get it past you, and make sure the technology works.

Mr Roche—Air Marshal Houston might like to put something on the record after you have set the—

Senator Hill—This is an interesting exchange but I am not quite sure where it is leading us. Is it just a chat?

Senator SCHACHT—I am completing it now. I am just interested that a number of these projects were put out and then cancelled and then we might have something a bit later on.

Senator Hill—It was cancelled, as I understand it, as part of the in-depth review of the whole capability, the order of priority and what we can afford. It simply did not match up on the priority requirements as compared with some other capabilities. So it remains in the white paper but it is further down the list. It gives us more time to think about other options. As has been said, options are being considered other than a replacement aircraft in terms of a replacement capability. We have now got the time to do that. I think the committee would be pleased to hear that as a result we are less likely to enter contracts that we will live to regret.

Senator SCHACHT—Air Marshal Houston, you look anxious to say something.

Air Marshal Houston—We are currently working at enhancing the capability of the Caribou. We have put much more resources into it to improve maintenance, and as a consequence of that we have had about a 50 per cent improvement on on-line availability. So right now it is going quite well and, as you rightly said, it has an ability to operate into very short strips, with very soft surfaces, which some other aircraft cannot do.

All the airfields in Australia have been surveyed in a number of studies over a number of years. A number of strips around the region have also been surveyed to see what sort of mix might be best for our transport fleet in the future. As Mr Roche said, there are a number of complex considerations in terms of how many fixed-wing aircraft, how many helicopters, how many big fixed-wing aircraft such as C130s—can we get away with just C130s and the helicopters and so on. We will continue to study those things. It is probably timely to do another study right now.

In relation to the Osprey technology that you mentioned, I do not think that is suitably developed at the moment. It is incredibly expensive and I would not see it as being suitable for us right now. But at the end of the day, when you look at a helicopter versus something like a Caribou, a Caribou is probably a little cheaper to operate than a helicopter. A helicopter gives you much more flexibility and probably better capability. These are the sorts of things we have to weigh up and they are the sorts of things that our development people will have a look at in some studies in the near future. So it is probably premature to decide whether we are going to go this way or we are going to go that way. We need to do a further analysis.

Senator SCHACHT—After about the end of this decade, will the Caribou, despite enhancing and good maintenance, have come to the end of their life?

Air Marshal Houston—Their planned withdrawal date at the moment is 2010. But we are confident we can keep them going. It is true that they are another ageing aircraft and, as with all ageing aircraft, you have to put more resources into them to keep them going. But they are going quite well at the moment with the injection of resource we put in shortly after I became Chief of Air Force.

Senator SCHACHT—Thank you.

Senator HOGG—I want to turn to the Kalkara project, which I have asked a few questions about over a number of years now. Has the project been completed?

Air Vice Marshal Conroy—Yes.

Senator HOGG—How many Kalkara have been delivered?

Air Vice Marshal Conroy—We have received 21.

Senator HOGG—The original contract was for 20; is that correct?

Air Vice Marshal Conroy—That is correct.

Senator HOGG—How come 21 were delivered?

Air Vice Marshal Conroy—An extra aircraft was negotiated by us to close out some disputes—not disputes, but continuing dialogue—with the company about whether or not the conditions of the contract had been met in detail. We accepted the offer of an extra aircraft.

Senator HOGG—Turning to the ANAO report from this year titled *Test and evaluation of major Defence equipment acquisitions*, it is reported in there:

The flight trials revealed that Kalkara suffered numerous:

- uncommanded tow separations;
- uncommanded pod separations;
- uncommanded and unexpected manoeuvres; and
- premature loss of command causing ocean impact large distances from the recovery point.

The last of those points we dealt with at length not at the last estimates but, I think, at the estimates before that. Were those defects identified in the ANAO report corrected prior to the resolution of the difficulties you have outlined by taking on one extra Kalkara?

Air Vice Marshal Conroy—Initial flights did suffer the problems that you mentioned but they were part of the normal learning curve of introducing a new system, in many respects. Each of those problems has been rectified or is in the process of being rectified and, indeed, we hope soon to start trials on that location device that we spoke of in some detail.

Senator HOGG—You finally purchased it.

Air Vice Marshal Conroy—Yes, we finally got an offer that we could afford.

Senator HOGG—So you are saying that the problems that were identified have now been addressed but, as I understand your answer, not fully rectified. Is that a reasonable assessment of your answer? And if they have not been fully rectified, what are the outstanding problems?

Air Vice Marshal Conroy—There is still an unexplained problem we had on launch of one of the aircraft that we have not really got to the bottom of, but you have to appreciate that this is an unmanned aircraft and it is not designed with the same levels of systems redundancy as a manned aircraft. You can either spend money on changing the design or you can look at it from a total airworthiness perspective—not only technical, but operational—and you can design your operating procedures to a large extent to compensate for any concerns you might have about certain design shortcomings of the aircraft.

Senator HOGG—I understand that but, given the range of problems that were discovered when you first took the Kalkara into service and were trialing it—it may have been before formal acceptance—who met the cost of rectifying the problems that have been corrected so far? Was that done as part of the tender or was that done by way of acceptance of the additional Kalkara?

Air Vice Marshal Conroy—The short answer to that is: the contractor.

Senator HOGG—All right. With respect to the extra Kalkara that was accepted, was it accepted with some of the problems that the previous Kalkara had or have you accepted that only on the basis that it is free from the faults that the others had? As I understand it, this was an off-the-shelf purchase, in effect.

Air Vice Marshal Conroy—It was a standard Kalkara. It is the same as the other 20.

Senator HOGG—Were there modifications done to it?

Air Vice Marshal Conroy—The only modifications done to it were the Australian unique changes to the American version. I would say that we accepted this extra Kalkara as compensation for delays in the project by the contractor and not because of any fault rectification.

Senator HOGG—Do the Kalkaras that have been accepted and have been modified meet the contract specifications that were initially put out by Defence?

Air Vice Marshal Conroy—They meet them in all areas except one criterion; that was the speed that the aircraft could attain with its tows deployed—it streams behind an infra-red target so you do not blow it out of the sky every time you shoot at it. My information is that the actual performance was very close to the specification and in the end we did not pursue that difference.

Senator HOGG—So that did not become a reason to reject the acceptance of the aircraft?

Air Vice Marshal Conroy—No.

Senator HOGG—Are there any implications for Defence in taking an off-the-shelf product such as this, having a range of specifications, finding that those specifications are not met and then proceeding through to the acceptance of the product?

Air Vice Marshal Conroy—All aerodynamic designs are a compromise. There will always be some form of ideal performance that you would wish to have out of a machine that cannot be met. It happens with the more sophisticated machines as well.

Senator HOGG—Does the shortcoming that you have outlined in any way limit the training that you can do with the Kalkara?

Air Vice Marshal Conroy—I do not believe so. The operation profiles or training profiles can be adjusted.

Senator HOGG—What number are you at currently with the Kalkara?

Air Vice Marshal Conroy—Fourteen.

Senator HOGG—From memory, the annual report said that there was an expected attrition rate of two per year—so that is still occurring. I think you had 16 in last year's annual report.

Air Vice Marshal Conroy—Yes, it is occurring. I had best explain that we bought these 20—now 21—aircraft as an approximately nine-year stock, expecting to lose the lot of them over that period of nine years or so. That equates to approximately two per year. We have had them for three to 3½ years; we have lost seven. So, against the time base, the attrition rate is—

Senator SCHACHT—In terms of the record, that means that you deliberately shot them down. When you lose them—

Senator HOGG—No, they lost one.

Senator SCHACHT—You said that you lost two a year. These are not the ones where you use them as drones for target practice or something like that, is it?

Air Vice Marshal Conroy—Yes.

Senator SCHACHT—When you say that you lose two—I want to get it clear in my mind and in the transcript—does 'two' mean that you deliberately aim to lose two by using them successfully for target practice or does it mean that you lost them because the truck they were on disappeared or something and they just got lost in stores?

Air Vice Marshal Conroy—Lost for all reasons. There was one aircraft that was hit during a missile shoot.

Senator SCHACHT—That was a successful loss.

Air Vice Marshal Conroy—The specification for this type of target was that we expected it would float for about 30 minutes, and we had 30 minutes to get—

Senator SCHACHT—You hit it, but you expect to get it out of the water and to redo it.

Air Vice Marshal Conroy—Oftentimes, yes. That is what we are trying to do.

Senator HOGG—That is why they are now going to fit a tracking device to it, Senator Schacht, so that when it falls in the water they can find it.

Air Vice Marshal Conroy—This machine that was supposed to float for 30 minutes actually ended up floating for six months and popped up—

Senator SCHACHT—And some tuna fisherman in my state got it caught in his net, I suppose.

Air Vice Marshal Conroy—No. Two of them have been washed up on beaches.

ACTING CHAIR (Senator Ferguson)—Senator Schacht, having scored a hit, I think it is an appropriate time to break for a coffee. We are halfway through. We will have a break for 10 minutes and start again at 9.20 p.m.

Senator Hill—We are not getting far if we plan to do the operations tonight as well. There has been a bit of new blood introduced during the hearing.

Senator SCHACHT—The new blood is leaving soon, I can assure you.

Senator Hill—I was hoping the new blood was tiring.

Senator CHRIS EVANS—Mr Acting Chairman, can I say to the minister that I think it highly unlikely that we will get past capital projects tonight. If there are staff waiting for operations, you could safely let them go. I think capital projects will take us to 11 p.m., especially if Senator Schacht is staying.

Proceedings suspended from 9.09 p.m. to 9.21 p.m.

Senator HOGG—I would like to finish off on this Kalkara project. I was having a discussion with Air Vice Marshal Conroy before and he was going to clarify some of the answers in respect of Kalkara.

Air Vice Marshal Conroy—When I said that the project is finished I meant that we have taken delivery of all of the aircraft. We have not actually signed off on final acceptance yet. Before we can finalise the acquisition contract we have still got some test work to go on the issue of flight below 50 feet and also that issue that I mentioned before: speed with tows trailed; those are two outstanding issues. So we have not actually signed off on the acquisition contract.

Senator HOGG—What about the tracking device?

Air Vice Marshal Conroy—The tracking device should begin tests next month.

Senator HOGG—So that will be fitted to the remaining 14 or 13, whatever are left?

Air Vice Marshal Conroy—The remaining 14; yes, that would be our intention. We have a price of approximately \$US150,000. I would need to clarify that.

Senator HOGG—It is in that order?

Air Vice Marshal Conroy—Yes, it is in that order.

Senator SCHACHT—Is that \$150,000 per unit?

Air Vice Marshal Conroy—No, that is for the total.

Senator HOGG—And that would enable the recovery of a single Kalkara which is valued at what cost?

Air Vice Marshal Conroy—That is \$US700,000. It is a good investment because what we are finding is that some of our missile shots knock a wing or wingtip off, it goes out of control, deploys its parachute and lands in the sea some distance away. If we can find that aircraft, we can refit a new wing section and regenerate the aircraft.

Senator HOGG—Right. Are you able to cannibalise those that have fallen out of use?

Air Vice Marshal Conroy—We have been able to cannibalise some aircraft that have been damaged in operations but, to this point, seven are not repairable.

Senator HOGG—Right.

Dr Hawke—Before we go on, with your indulgence, could I ask Air Vice Marshal Conroy to explain this issue involving the 10,000 hours, the 11,000 hours and the zero basing, because I do not think we got the message across correctly to the senators.

Senator CHRIS EVANS—Do you mean in relation to Seasprites?

Dr Hawke—Yes.

Air Vice Marshal Conroy—You might recall I read out some of the flying hours that these particular airframes had done in US Navy service. Some of these were up near the 10,000-hour mark. I mentioned also that Kaman has a contractual obligation to deliver us aircraft that will have a 10,000-hour in-service fatigue life against a certain spectrum. The previous flying done under the auspices of the US Navy is not relevant against that latter 10,000-hours contractual requirement. The aircraft have been effectively relifed through the constructionary refurbishment process that has gone on in this project.

CHAIR—Do you think the airframe is lighter than it was or do you think it is heavier?

Air Vice Marshal Conroy—It is slightly heavier.

CHAIR—But not so heavy as to affect its operational capacity?

Air Vice Marshal Conroy—We believe it is not so heavy as to materially affect that issue.

Senator CHRIS EVANS—So the rest of it is new now, is it? It is not out of cannibalised bits? When you said 70 per cent had been replaced, it has not been replaced by other bits from other airframes and cannibalised?

Air Vice Marshal Conroy—No, it is new structure that has been put in place. There is re-used structure from the original aircraft and then there is some built from new structure.

Senator SCHACHT—Where is that built from new structure coming from? Is that being made in Australia or is it from the United States or England or wherever?

Air Vice Marshal Conroy—It is made in the United States.

Senator SCHACHT—Why can't it be made in Australia? It does not seem to be a particularly complex technology to make a piece of airframe. We have capacity in industry for aluminium extrusion and goodness know what else. Why can't we make the new missing parts in Australia?

Air Vice Marshal Conroy—It is quite possible, but Kaman is a very small company. They really do not have the overheads to establish a second production line somewhere else in the world. They are not a large operation at all.

Senator SCHACHT—I may be missing something here. I am pleased that you will hit me over the head if I am. How much of the frame is to be made of new parts to get a complete frame for one helicopter? Are we averaging 30 per cent of new parts?

Air Vice Marshal Conroy—The figure I believe is correct is something in the order of 70 per cent of the total aircraft being new.

Senator SCHACHT—With 70 per cent, why couldn't we ask for an Australian industry participation program? We do it with other projects.

Senator Hill—I do not think you were here earlier when it was said to us that they believed that Kaman thought it could do it for much less.

Senator SCHACHT—So they can make the new components—

Senator Hill—As the project has developed, they have found that they have had to introduce more and more in terms of new components. So it has not been up to the logical production line process.

Senator SCHACHT—But, as a result, they have had the advantage of making most of the new parts without having to meet any Australian industry participation goals?

Dr Hawke—They have lost money on the deal because they have had to build that 70 per cent when they were not expecting to within the same cost.

Senator CHRIS EVANS—You would be stretching my patience to argue they have lost money on this deal. They have got \$900 million of our money and they have had it for a long time now.

Dr Hawke—They did not get supplementation for doing this. That is not what they intended in the original contract.

Senator SCHACHT—Did they lose money on the \$900 million?

Senator CHRIS EVANS—They have had the interest on it for years.

Senator Hill—All the industry magazines say that it has not been a moneymaker in itself. What they are hoping, interestingly, is that the product is going to be so good it is going to be taken up by others. That is where they intend to get their money.

Senator SCHACHT—I have heard that stuff before in Defence estimates when both sides have been in government, Minister.

Air Vice Marshal Conroy—The AII obligation that the contractor undertook as part of this tender amounts to about 29 per cent of the total contract cost. So 29 per cent of that contract cost is being spent on local materials.

Senator SCHACHT—Which is about \$200 million.

Air Vice Marshal Conroy—It is a bit more than that.

Senator SCHACHT—I come from a small state. A \$200 million contract in South Australia is a pretty significant boost to the local economy. It might not count for much in Canberra or Sydney or Melbourne. I can tell you that it counts big in Adelaide. We allowed them to grow it and said for a start we are going to do 10 per cent but now we are going to do more of it. Now it is up to over a \$200 million part of the contract.

Mr Roche—Senator, \$230 million is being done or has been done in Australia.

Senator SCHACHT—Sorry, I misunderstood the figure. Do we have any idea how much, in their \$900 million contract, the new parts of the airframe that they are now making are worth?

Senator Hill—It was not supposed to be worth too much. What has happened is that they have now found they have had to introduce more and more in terms of new components. But they have not got more money for that. It is not as if the price has increased.

Mr Roche—I think the difficulty here is that Kaman, as the manufacturer, are uniquely qualified to rebuild these aircraft. Leaving aside some of the technology issues, the roof, for example, has been replaced in titanium, not in aluminium. The idea that they would actually set up a second set of expertise to individually assess each one of these aircraft and to build what is necessary in Australia would, in my view, have just added significant costs to the whole project.

Senator SCHACHT—If there is going to be inefficiency in programs, I would rather the inefficient money be spent in Australia than somewhere else in the world, quite frankly. We are spending \$900 million on Seasprites. How many are there?

Senator Hill—Eleven.

Senator SCHACHT—What is that, \$80 million a pop? I hope the titanium on the top of them is bloody good. And you are saying that we have no capacity in Australia to do titanium tops?

Mr Roche—I am not aware of the capacity that we have to do that, but in any event to do it for 11 aircraft is highly likely that—

Senator SCHACHT—But they are doing it for 11 aircraft, and they are making their value added cop out of it. This is what is annoying.

Senator Hill—No, they are investing the capital in the hope that they will get ongoing contracts.

Senator SCHACHT—I reckon that they are doing it because they have taken \$900 million off us as a basis on which to go and build a contract and sell elsewhere in the world. They have amortised their contract for the rest of the world out of us. Goodness me, it is not the first time this has happened.

Air Vice Marshal Conroy—You could have then given the contract to the guy who came second, and paid \$200 million more.

Senator CHRIS EVANS—You might have a helicopter, though.

Senator Hill—You might not. Who is to know?

Senator CHRIS EVANS—I did not put it any higher than ‘might’. We have got an Australian company fixing up the combat system now, so there is local content.

Senator Hill—The Brits ran second.

Senator SCHACHT—The Brits ran second to the Americans. Is that right?

Senator Hill—Yes.

Senator SCHACHT—So the republicans beat the monarchists. Okay.

Senator CHRIS EVANS—I would like to point out that Dr Hawke opened up this conversation for the second time, so I take no responsibility, Minister, if you are not enjoying this.

Dr Hawke—I did.

Senator SCHACHT—We are glad you did, Dr Hawke.

Senator Hill—Next time I will be back on time!

Senator CHRIS EVANS—You could plead jet lag, Dr Hawke.

Senator CALVERT—Could we get off this subject and get onto something more positive? I have got a very quick question to ask, if I could, along the same lines. While we are talking about these sorts of things: how is the program going for replacing the wings on the F111s? I understand you had a good arrangement with the Americans on that.

Senator Hill—The F111 team will come to the table.

Senator SCHACHT—Before that is answered, could I just go back for one question about the Kalkara?

CHAIR—You may just have one question, Senator Schacht, and then we will go to Senator Calvert's question.

Senator SCHACHT—Air Vice Marshal Conroy, did the company which I mentioned earlier on another matter, Australian Flight Test Services, ever provide a consultancy or were they ever employed to do a consultancy on the Kalkara?

Air Vice Marshal Conroy—Yes, they did.

Senator SCHACHT—What was the nature of that contract?

Senator Hill—I thought you wanted one question.

Senator SCHACHT—Now that he has told me yes, I need to follow through. If he had said no, I would have had to stop.

Senator Hill—Why didn't someone say no!

Air Vice Marshal Conroy—The consultancy was to examine one of the phenomena that were causing us problems early on in the project.

Senator SCHACHT—Was that to roll over, or something?

Air Vice Marshal Conroy—There were some uncommanded turns in the launch phase.

Senator SCHACHT—Was that contract satisfactorily completed to the satisfaction of the Air Force?

Air Vice Marshal Conroy—Yes.

Senator SCHACHT—Did it make critical comments about the Kalkara program?

Air Vice Marshal Conroy—It made what I thought were neutral and reasoned analyses of a phenomenon that was causing us difficulty.

Senator SCHACHT—Was it a big contract—a million dollars, \$500,000, \$10 million?

Air Vice Marshal Conroy—In my understanding it was a small contract, smaller than that.

Senator SCHACHT—You were satisfied with the work that they did?

Air Vice Marshal Conroy—Yes, I was.

Senator CALVERT—There has been a problem with wing cracking in some of the F111s or one of the F111s and they are changing the wings on them by using replacement wings

from the United States, from some of their mothballed F111s. Is that program working successfully? How many F111s do we have that are airworthy at the moment? Has it affected the capacity of our F111s in their role? When do you believe that that program will be completed? Has it been an expensive program?

Air Marshal Houston—If I could just indulge you for a little while, I will give you a summary on all those things. Perhaps I will start with the fact that we manage the fleet in a particular way. You would know that back in 1973 we bought 24 F111Cs and then in 1993 we got some F111Gs. The F111Gs were bought by the previous government. The only funding that was provided was \$A79 million. There was no funding for flying those additional aircraft or indeed maintaining those additional aircraft. In fact, because the G models were coming up for retirement from the US Air Force they were all due for servicing. We took on board those aircraft so that we could extend the life of the F111.

We had a project a few years ago to upgrade all the F111s to the same standard. That was Air 5404. But that fell by the wayside because, obviously, it was expensive. The way we are operating the F111 now is we have 28 aircraft that we use for flying activities. There is a total of 35. We rotate 17 F111Cs, four RF111Cs and seven G models through the flying pool. There are two aircraft that are just hulks, really, and we have taken all the spare parts for them. You could call the other aircraft ‘attrition spares’. I stress the reason we do this is we got no additional funding when we got the F111Gs to either maintain them or operate them. Because they are completely different configurations from the C model and they do not have a precision strike capability, we use them primarily for training. So those seven G models we use for training.

When we did the fatigue testing it was not an F111 that we were testing; it was just a wing. The wing failed during routine testing that we have been doing for a number of years. It was unexpected. As a consequence of that our technical airworthiness people had a look at it and determined that the safe flying limit for the long wings that we were operating meant that 15 aircraft would have to have new wings to operate again. Those 15 aircraft are eight RC models and seven RG models. In other words, all the G models were affected by this.

The fix for the problem was to have a look at what was available in the United States at Davis-Monthan at AMARC. We were able to find some really good wings in the United States. We already had four sets of wings in the store, and we have since received another seven sets. We expect to get a delivery of every other set, one every fortnight, until we get 26 wing sets. Those wing sets have cost us next to nothing. In fact, most of the cost involved with getting them is to do with transportation and putting the wings through wing bay servicing at Boeing Australia at Amberley.

The prognosis is that we will be able to remediate the wing problem very easily and relatively cheaply. While we are doing this, we are continuing to maintain a very good level of operational capability. Indeed, we will fly almost the same rate of effort this year as we flew last year, with the remaining aircraft that still have life in the wings. We recently participated in the exercise up in Malaysia—the air defence exercise run by the headquarters integrated area defence system as part of the Five Power Defence Arrangements. The three aircraft that went there flew 110 hours over two weeks and maintained outstanding serviceability. We are also running a conversion course. I am very content with where we sit right now with the F111.

There seems to be a notion around that the way we operate the F111 means that we have to have every aircraft fully serviceable. We have 28 aircraft. If we had absolutely no problems at

the moment, we would have the seven G models doing training; they would not all be serviceable all the time, but we would have enough to meet the training effort. Of the remaining 20, four would be in deeper level maintenance and another four would be in the upgrade program for the new modifications that we are putting into the aircraft. The only aircraft we need to have serviceable are those required to meet our preparedness and training requirements. If we had everything going according to Hoyle, we would fly about 3,600 hours a year. Last year, we flew 2,757 hours; this year, we will fly almost the same: about 2,700 hours. The outlook for next year is about 3,200 hours at this stage, which is getting back towards the 3,600 hours that we would want to fly for the foreseeable future.

Senator CALVERT—Out of your 28 aircraft, you have eight C models that would have the highest capabilities for high performance F111s; the others are training, are they not? You said that you had eight C models that are up to scratch at the moment. They would have the full avionics and would have been upgraded. So they would be providing the A1 capabilities that you require, given that the G models are used for training and the other four that you have are being serviced.

Air Marshal Houston—At the moment, we have 21 C models.

Senator CALVERT—Out of the 28, you have eight that are absolutely 100 per cent at the moment—the C models, right?

Air Marshal Houston—We have eight that are available for flying now.

Senator CALVERT—And that is sufficient, in your opinion?

Air Marshal Houston—We are maintaining our capability with the aircraft. Bear in mind that we are not standing still. We have all those new wings coming in; they are being fitted to the aircraft to replace the wings that are obviously not good enough.

Senator CALVERT—The new wings are shorter, are they not, and decrease the range somewhat?

Air Marshal Houston—I will explain that too. Eventually we will go to the short wing, but at the moment there are airworthiness considerations with underwing stores and other factors that need to be considered—for example, the wings have to be rewired, and so on. We will re-equip these aircraft with new long wings. It is very easy to extend these wings so that they are long wings. We will use those initially and, once we have the airworthiness and certification issues resolved—and that obviously requires some testing, for example, of underwing tanks or underwing weapons on a shorter wing—we will go across to the short wings. The short wings have a much longer life than the long wings and they will take us through to whatever withdrawal date the government requires.

Senator CALVERT—I am sure my colleague Cameron Thompson in the other place will be very pleased to hear all that.

CHAIR—What model, if any, is used for reconnaissance now?

Air Marshal Houston—The C model. We have four of the F111Cs.

CHAIR—Was it always the case that G models were never used for reconnaissance?

Air Marshal Houston—No, the G model has always remained in the same configuration as it was when we bought it. It does not have a precision strike capability nor a reconnaissance capability.

Senator CHRIS EVANS—I want to ask a couple of questions about torpedoes for the Collins submarine. I understand the original tender was abandoned and the government made an announcement about a strategic partnership with the US on submarines. I want to be clear what happened after that with the torpedo decision. I understand the tender process for the original replacement torpedo was abandoned. Could you take me through what the selection process then was? As part of that decision, did the government automatically adopt US torpedo Mk 48 Mod 6?

Rear Adm. Scarce—That is correct, Senator.

Senator CHRIS EVANS—That was a government decision made at the time of the abandonment of the tender. Is that right?

Rear Adm. Scarce—That is correct.

Senator CHRIS EVANS—What due process, testing and suitability arrangements had been made prior to that decision?

Rear Adm. Scarce—As we approached the decision, the government moved to take a more strategic relationship with the US. We had three contenders. We assessed the suitability of those three contenders and when the government decided to take a strategic relationship with the US, we set aside the tendering process. We then looked at the suitability of the Mod 6 and the follow-on torpedo—which we will work on with the US over coming years—to make sure it met our requirements. It did meet our requirements and subsequently we undertook discussions with the USN about the most economical way of acquiring the weapon.

Senator CHRIS EVANS—Mod 6 was one of the tenderers?

Rear Adm. Scarce—The USN ADCAP system, which is the Mod 6, was part of the solution of upgrading our Mod 4 weapon, an analog weapon, to a digital weapon. We will move from Mod 5 to Mod 6 and eventually to a long-term development program which will upgrade the Mod 6 to what the USN call a CBASS torpedo, the next level generation of torpedo.

Senator CHRIS EVANS—I am a little uncomfortable with the terminology. We moved through Mod 4s to Mod 7s, but what is the generic way of describing what we have bought?

Rear Adm. Scarce—It is an ADCAP Mk 46 torpedo with various modifications. They change a range of—

Senator CHRIS EVANS—Mk 46?

Adm. Barrie—Mk 48.

Rear Adm. Scarce—Mk 48, sorry.

Senator CHRIS EVANS—And they were one of the tenderers in the original tender round?

Rear Adm. Scarce—That is correct.

Senator CHRIS EVANS—That is the United States Navy tender, in effect, is it?

Rear Adm. Scarce—That is correct.

Senator CHRIS EVANS—So they are a navy product?

Rear Adm. Scarce—They are a product built for the USN.

Senator CHRIS EVANS—So when they tender for outside work, it is not a private company, it is the US Navy, is it?

Rear Adm. Scarce—In this particular instance, because we wanted a development program, we negotiated with the USN for the delivery of a weapon and the ongoing support throughout the life of the submarine.

Senator CHRIS EVANS—There is not an intermediate company; it is the US Navy you have contracted.

Rear Adm. Scarce—That is correct.

Senator CHRIS EVANS—Had the Mk 48 been assessed, at the time of the abandonment of the tender, as being appropriate for the Collins?

Rear Adm. Scarce—No, it had not.

Senator CHRIS EVANS—It hadn't?

Rear Adm. Scarce—No, not at that stage. That was the next stage of the acquisition process: to look at the three tendered torpedoes.

Senator CHRIS EVANS—So how did we make the decision to buy it when we were not sure it was suitable?

Rear Adm. Scarce—The decision by government was made on the basis of an ongoing relationship with the USN.

Senator CHRIS EVANS—I do not think even a government most keen or friendly with the US would want to buy something that did not actually work—I am not saying it doesn't, but I mean—

Senator Hill—That would be true.

Senator CHRIS EVANS—Even the minister's enthusiasm for the American relationship does not extend to—

Senator Hill—If we believed it was not going to work, it would not have been purchased.

Senator CHRIS EVANS—I am interested in what evidence we had that it was a suitable product to buy at the time we purchased it.

Rear Adm. Scarce—The fact that it was operating in all the USN submarines would have been a satisfactory indication.

Senator CHRIS EVANS—As I understand it, they have very different submarines to us.

Rear Adm. Scarce—They have different submarines to us, but the weapon which is for their use would be similar for our use.

Adm. Barrie—Perhaps I can help here. The RAN has operated the Mk 48 submarine torpedo for several years. The torpedoes that Admiral Scarce is talking about are upgrades and enhanced capability to the Mk 48 torpedo.

Senator CHRIS EVANS—As I understand it, they are also quite a deal heavier. Is that right?

Rear Adm. Scarce—They are heavier.

Senator CHRIS EVANS—At the time of purchase had we done an analysis of whether or not the Collins could accommodate this heavier torpedo?

Rear Adm. Scarce—We had not done a detailed analysis, but we had looked at the overall weight implications. We obviously felt they were manageable. We are now in the process of doing a very detailed analysis of the physical integration of the weapon end of the submarine.

Senator CHRIS EVANS—So that has not occurred as yet?

Rear Adm. Scarce—It is under way.

Senator CHRIS EVANS—When did that start?

Rear Adm. Scarce—In May this year, Senator.

Senator CHRIS EVANS—This announcement about adopting these torpedoes was made last July, if I recall.

Rear Adm. Scarce—That is correct. We have been negotiating with the USN on the method of procurement, and we are now undertaking the detailed physical integration into the submarine.

Senator CHRIS EVANS—We are negotiating on a method of procurement?

Rear Adm. Scarce—Yes: how we will acquire the torpedo from the USN and how we will participate in the ongoing development of the later generations of the weapon.

Senator CHRIS EVANS—Is that now agreed and finalised?

Rear Adm. Scarce—It is broadly agreed; we are looking at the last drafts of the MOU between ourselves and the USN on that particular matter.

Senator CHRIS EVANS—It is not signed off?

Rear Adm. Scarce—No.

Senator CHRIS EVANS—What is the timetable for this integration study?

Rear Adm. Scarce—We expect the integration study to take about six months. It involves the designer, Kockums, and also includes the ASC and us.

Senator CHRIS EVANS—What are the main challenges in that integration study?

Rear Adm. Scarce—The main challenges are integrating the heavier weapon into the physical handling characteristics and the implications that will have on the submarine itself in terms of trim et cetera.

Senator CHRIS EVANS—So weight is the major issue confronting you?

Rear Adm. Scarce—For the physical integration of the weapons system. Obviously it also needs to be integrated into the combat system.

Senator CHRIS EVANS—I am not asking you to foretell the findings of the integration study, but does having a heavier torpedo mean that you will have to build bigger systems inside the Collins to handle it?

Rear Adm. Scarce—Not bigger systems. The torpedo itself is the same size; it is just heavier. We will be looking at where it is stowed and the strength of the stowage areas and, because of the fine balance in the submarine, we will be looking to see what impact that will have on the trim of the submarine system itself.

Senator CHRIS EVANS—I presume you would want to carry the same number of the newer torpedoes. Is that fair?

Rear Adm. Scarce—I will leave it to my tactical colleagues to answer that, but that will be one of the issues that we will be looking at.

Senator Hill—You might not just be carrying torpedoes, though.

Senator CHRIS EVANS—I do not understand the import of the comment.

Senator Hill—The system is designed to fire more than one type of weapon.

Senator CHRIS EVANS—Are you telling me that you would have a trade-off between torpedo capacity and other capacities?

Senator Hill—Yes.

Rear Adm. Scarce—As part of this study, our operations people will be determining the right mix of various weapons in the submarine system.

Senator CHRIS EVANS—Haven't you done that already?

Rear Adm. Scarce—We have, but we will now need to look at the weight differentials and make sure that is still applicable. That is part of this process.

Senator CHRIS EVANS—So the process is driven for you by the weight issue?

Rear Adm. Scarce—Yes, predominantly.

Senator Hill—I asked the same sorts of questions as those that are being asked tonight. Part of the answer is that, every time you seek to upgrade capability—and we are talking about a far superior torpedo than the existing torpedo—a range of integration issues will need to be addressed. In this instance, we are dealing with some extra weight and there are other issues as well. But the best advice I got is that nothing is obviously expected to be insurmountable, or else we would not be going down this path with the US Navy. It is just a matter of working through what needs to be done, which will take place during this six-month study and ultimately, in conjunction with the new combat system, making the alterations.

Senator CHRIS EVANS—I think that would generally be true, but the interesting aspect of this is that the tender process was abandoned and a particular torpedo system chosen outside that tender context. It is interesting to see whether that choice was made on a rational basis or whether we have ended up with a torpedo that is too heavy.

Senator Hill—You might say this is part of the risk of the strategic alliance that we are seeking to establish with the US Navy. We actually see it as part of the benefit, because we have the world's most capable submarine manufacturer and operator assisting us in the continual upgrade in capability of our equipment.

Senator CHRIS EVANS—That is what I am trying to test: whether it is an advantage or a disadvantage, or where the balance lies. That is why I am interested in the issues this decision throws up.

Senator Hill—That is right. Certain European manufacturers say it is a mistake. The view of the Australian government is that it is the right step to take.

Senator CHRIS EVANS—It is the role of the Senate committee to test that.

Senator Hill—Absolutely. Everything so far in terms of the relationship with the US Navy in relation to Collins has been very positive. The recent visit by Electric Boat to ASC, the study that they made and their attitude has been very positive. General Dynamics has been positive and the US Navy has been positive. I have no doubt at all that it is going to be a very

useful relationship to Australia in terms of best ensuring that we are going to have a boat that meets the capability requirements that we need for the whole of its life.

Senator CHRIS EVANS—We will see. Is there a budget for this project?

Rear Adm. Scarce—Yes, there is. It is \$200 million to \$260 million.

Senator CHRIS EVANS—The figure of \$260 million seems to be the magic figure with your projects.

Rear Adm. Scarce—I started with \$200 million.

Senator CHRIS EVANS—Everything you do is worth \$260 million.

Rear Adm. Scarce—I wish that were the case.

Senator HOGG—Where does that magical figure of \$260 million fit in the table on page 77 of the PBS? You see there that the new submarine project is listed as \$5,112 million and the Collins class submarine augmentation is listed as \$228 million. Before you answer that, I will just take you to the ANAO report entitled *Test and evaluation of major defence equipment acquisitions*, which was prepared this year. In that report reference was made to modifying HMAS *Dechaineux* and HMAS *Sheean*. It says:

These redesigns, modifications, upgrades, rectifications and sustainability enhancements amount to almost \$2 billion, and represent an increase of 39 per cent on the approved submarine project cost of \$5.09 billion (December 2000 prices).

You have just mentioned \$260 million. If I look at the ANAO report—and I know you do not have a copy of that before you—it mentions two figures: \$860 million and \$840 million. I am just trying to reconcile it with the figures that are in the PBS. Where does that \$260 million fit in? If you want to get back to me tomorrow morning with an answer, I am quite happy to take it then. It seems as though people are doing a bit of searching for the answer.

Senator Hill—It is obvious that only part of the Collins—

Senator HOGG—Minister, I am quite prepared to accept an answer in the morning on this particular matter. Admiral Scarce has just mentioned an amount of \$260 million—

Rear Adm. Scarce—It is \$200 million to \$260 million and it is an approved project so you will not see those numbers—

Senator HOGG—It is not an approved project, so it is not in the budget.

Rear Adm. Scarce—Yes, it is in the budget.

Senator HOGG—Right.

Rear Adm. Scarce—As the minister has already mentioned, in terms of this report on test and evaluation this is a mix of approved and unapproved projects and I am sure that tomorrow morning I will be able to give you a breakdown of where those numbers come from.

Senator HOGG—Can you give me a breakdown of that tomorrow morning?

Rear Adm. Scarce—Yes, a breakdown of this test and evaluation report.

Senator Hill—We can get you a breakdown of the \$228 million and from that you can work out the figures.

Senator CHRIS EVANS—The \$228 million will not include this because it is not approved expenditure.

Rear Adm. Scarce—The \$228 million in essence passes the improvements for fast track on HMAS *Sheean* and HMAS *Dechaineux* through the remainder of the fleet. I will give you more detail but in essence that is what it is.

Senator HOGG—If you could give me more detail tomorrow morning, because I was getting lost when you were talking about \$200 million to \$260 million and I was looking at those figures and that audit report.

Senator Hill—I think the answer is that although the new torpedo is in the Defence Capability Plan—so it has got through the first door—it is yet to be approved as a contract. Similarly, with the new combat system we are at a stage where we are now addressing the new combat system but the price for that is not on that list either.

Senator HOGG—Can you give an indication, obviously not precisely, of when you expect those to be approved?

Senator Hill—I am expecting the new torpedo project to be approved in conjunction with the new combat system. I really see them as hand in glove.

Senator HOGG—Roughly, will it be six months, 12 months? What sort of time are we looking at in broad terms?

Senator Hill—I am expecting it within the next six months.

Senator HOGG—The reason I raise that is because when we come to additional estimates there is a prospect that we should see those appear in the additional estimates as an approved project.

Senator Hill—No, we may not be spending the money this year. You will see them in the updated Defence Capability Plan but as an approved project.

Senator HOGG—That does not necessarily mean that the money is being spent this year.

Senator Hill—Yes.

Senator HOGG—Okay. Next year there may well be a budget allocation for them?

Senator Hill—That would be my expectation.

Senator HOGG—Thank you.

Senator CHRIS EVANS—Rear Admiral, can I take you back to the \$200 million to \$260 million: is that for development or purchase of the torpedo or both?

Rear Adm. Scarce—That is for the physical integration of the weapon into the submarine and the purchase of training and war stocks. The remainder of the war stocks will be purchased in a latter stage of the project, which is yet to be approved.

Senator CHRIS EVANS—I see. This gets you the development, the integration and some trial—

Rear Adm. Scarce—Some training and some war stock.

Senator CHRIS EVANS—I presume the major war stock is another item.

Senator Hill—The other war stocks have not yet got in the first door because it is further down the track.

Senator CHRIS EVANS—That \$200 million to \$260 million should buy some torpedos but not what we would be looking to purchase if the whole thing went through?

Senator Hill—Not as a full war stock.

Senator CHRIS EVANS—Okay.

Senator Hill—Could we make one clarification on F111s.

Air Marshal Houston—I want to clarify the figures concerning the F111s when the senator said that there are eight aircraft that can fly. Yes, we do have about eight aircraft that can fly out of a pool of 13 F111Cs that have no difficulty with their wings. I wanted to clarify that.

Senator CHRIS EVANS—Who was that in response to?

Senator HOGG—It was Senator Calvert.

Senator CHRIS EVANS—You were looking at me and I thought that I had not raised it with you specifically.

Air Marshal Houston—If we can put that on the record, I would appreciate it. I think a clarification was required. Thank you.

Senator WEST—I want to ask about Defence Headquarters Australian Theatre and the state of play there. What is going on? It is on page 76 of the PBS.

Senator Hill—The development of the project continues. Basically, it is still in its design stages in terms of what will be its capabilities and how it might operate and so forth. Further down the track will be the design of the buildings within which those systems will operate. We are looking to appoint a party to conduct the environmental impact statement under the environment protection and biodiversity conservation legislation. I think we are still within the original timetable. It is still a few years down the track. The goal is to get it through the Public Works Committee by the end of next year and to have it built by 2006.

Senator WEST—Where do I find the funding for work that is currently being undertaken?

Senator Hill—I do not think we have yet approved any specific funding for that work. Is that right?

Senator WEST—If you are doing design work the funds have to be coming from somewhere.

Senator Hill—We have approved the study money for this year.

Senator WEST—How much is that?

Mr Bennett—I do not have the number to hand but it is in the order of tens of thousands of dollars—not any significant amount of money.

Senator WEST—Please take that on notice.

Mr Bennett—Yes.

Senator WEST—The project has not yet been formally approved?

Senator Hill—That is correct.

Senator WEST—This was announced on 3 October last year; is that a normal way to go about things?

Senator Hill—Yes. We announced the intention to establish this facility and we are starting to work on the design of it. When we have enough detail to give us confidence in the figures and so forth, which is perhaps a little different from the way things were once done—

Senator WEST—A little different?

Senator Hill—We want to go to government with a realistic price. When we get to that stage then we will go through the formal approval process.

Senator WEST—I see.

Senator Hill—One of the issues we are considering, and have done considerable work on already, is the method of funding the facility—whether it might be privately funded, for example.

Senator WEST—The possibility of it being privately funded is one of the options you are canvassing?

Senator Hill—That is correct.

Senator WEST—Can you give me the other options?

Senator Hill—The government could buy it.

Senator WEST—You are not fixed on any ideas at this particular stage?

Senator Hill—No.

Senator WEST—So it is still set for completion in 2006-07. Where is it going to be located? Is that absolutely, definitely 1,000 per cent cast in stone, concrete, iron, gold or whatever?

Senator Hill—Yes, in terms of the area. I do not think we can give you a GPS reference.

Senator WEST—From reading some local newspapers I thought that you could have given us a GPS reference. It is on the Hyles' property called Woodlands which is next door to the ACT Nudist Club.

Senator Hill—The admiral says that is correct.

Senator WEST—I did not know the admiral was a ventriloquist. I did not see the admiral's lips move, Minister.

Adm. Barrie—That is the minister's interpretation. Yes, you can have a GPS position. It is out of Bungendore, off the Kings Highway.

Senator WEST—On the property named Woodlands?

Adm. Barrie—I do not know.

Dr Hawke—I think it is on the Hyles' property.

Senator WEST—Is it true that Defence only talked to the Hyles family two days before the announcement was made?

Dr Hawke—I do not know. We do not have any of the infrastructure people here, but we could answer that tomorrow.

Senator WEST—Because I am interested to know how the locations of the sites got to be short-listed and why this one was selected, if anyone can answer that tonight, or do I need to ask that in the morning?

Dr Hawke—My recollection is that it was considered by cabinet, but I am not absolutely sure of that. Again, we will answer that when the infrastructure people are here tomorrow.

Senator WEST—All right. There is also, within five kilometres or so of the Woodlands property—

Senator Hill—The question was answered on notice. It was question No. 15.

Senator WEST—What does it say, to refresh my memory, Minister?

Senator Hill—It will not give you all of the information you would like, but it says that the government considered a submission from Defence on the siting of the co-located headquarters of Australian Theatre and decided it was to be located in or adjacent to the Australian Capital Territory. That is the answer I approved. The admiral says that it is much more specific than that. So we can both be right, provided that it is still in or adjacent to the Australian Capital Territory.

Adm. Barrie—It is that.

Dr Hawke—Landowners were briefed on the implications of the siting decision on Friday, 5 October.

Senator WEST—And the announcement was made on 3 October?

Dr Hawke—It does not say that here, but I will take your word for it.

Senator WEST—I have here former Minister Reith's press release which is dated 3 October.

Dr Hawke—Yes. I am just saying that that answer to the question on notice makes the point about landowners being briefed on 5 October.

Senator WEST—What about the issue of the radio telescope that is within five kilometres of the site?

Dr Hawke—We will have to answer that tomorrow. I am aware of that.

Senator Hill—The answer is that Defence still believes that it is manageable in terms of the telescope's operation. Some at the University of New South Wales who operate it still question that and I have asked for a more authoritative assurance from Defence.

Senator WEST—So you are going to use Defence as the source for the authoritative—

Senator Hill—I have asked them to get it. They can get it from DSTO or wherever. But this issue of dispute between the scientists needs to be resolved. The advice I am getting from Defence is that they are confident that both facilities can be co-located without loss of capability to either.

Senator WEST—So the \$25 million grant that they got from the industry department will not be wasted?

Senator Hill—That is correct.

Senator WEST—You said there was going to be an EIS done. Will that be done under New South Wales EIS legislation or Commonwealth?

Senator Hill—Commonwealth.

Senator WEST—Why is that when it is within the state of New South Wales?

Senator Hill—Because it is our facility. The New South Wales government may become involved in the process, I am not sure. But certainly it is going to have to satisfy the Commonwealth legislation.

Senator WEST—Is the New South Wales legislation weaker or harder than the Commonwealth's.

Senator Hill—The Commonwealth is the strongest in the world!

Senator WEST—Says the former minister for the environment—what else would I expect you to say!

Senator HOGG—Minister for tree-hugging!

Senator WEST—Some people did not think he hugged enough trees! The issue of the water table out there has been raised with me. I do not know the truth of the matter, but the story circulating in the local area was that a lot of this construction was going to be underground. They raised concerns that the water table is quite high and that also some of that area is actually the water source for Bungendore. Has that been raised with Defence?

Senator HILL—I have not heard that, but that is the sort of issue that would be addressed in an environmental impact study.

Senator WEST—Defence is quite happy with the consultation process that has taken place for the people of Bungendore?

Senator Hill—I have not heard anything to the contrary. The answer that we gave is that consultations are continuing.

Senator WEST—In what form? How are they continuing?

Senator Hill—I do not know the detail.

Senator WEST—Will I be able to get the details for that tomorrow?

Senator Hill—I do not know. We think we can find somebody.

Senator WEST—I will wait until tomorrow for the next episode.

Senator CHRIS EVANS—I want to ask a couple of questions about the patrol boat replacement. Is the short list for that project still to be announced in the next month?

Senator Hill—It is still to be announced—hopefully in the next month.

Senator CHRIS EVANS—The timetable was next month?

Senator Hill—Yes, that is our goal.

Senator CHRIS EVANS—Is it still on track or has there been a delay?

Senator Hill—It is pretty much on track. The process for selection of the short list is definitely on track. There have been some other aspects that have caused us a short delay—basically financing issues, which are quite complex—but, in terms of our goal as to when we want to be in contract which was by the end of this year, we are hoping to achieve that. Provided we can make our announcement and that we can settle issues of finance within the next month, I cannot see why we cannot achieve that target.

Senator CHRIS EVANS—By issues of finance, you mean issues of how you are going to finance the project?

Senator Hill—As you might recall, the first bids were on the basis of both private financing and a government purchase option. We have to make a decision as to whether we ask the short-listed tenderers to provide their second bid on the same basis or whether we want to be more explicit.

Senator CHRIS EVANS—That decision has not been made yet?

Senator Hill—No, but hopefully it will be made within the next month. That is our goal.

Senator CHRIS EVANS—Does that have to be made before the short list is announced?

Senator Hill—It does not have to, but I think it would be desirable to announce both at the same time. I think it would make it easier for those that are on the short list.

Senator CHRIS EVANS—Has there been any consideration of adding two or three larger patrol boats to the tender?

Senator Hill—Not adding additional patrol boats or substituting some. I do not think there has been any discussion of adding additional boats.

Senator CHRIS EVANS—Substituting, then.

Senator Hill—I think one or more bidders might have raised the issue of providing an enhanced capability in some of the boats.

Senator CHRIS EVANS—That has not been raised by Defence, though? You would be aware, Minister, that there were prebudget stories in a number of media outlets to the effect that the budget was going to include an announcement about an extra two or three larger patrol boats—to the point where I have actually had difficulty convincing some people that it was not included in the budget. There was a great spin put on it.

Senator Hill—I know.

Senator CHRIS EVANS—Most people will not believe you that it was not a key plank in the budget, so whoever spun that story deserves some recognition—

Senator WEST—Ten out of 10.

Senator CHRIS EVANS—for a very successful ploy. As I understand it, and correct me if I am wrong, there was no provision either in the Defence budget or in the Fisheries budget for—

Senator Hill—It has been a great mystery to all ministers.

Senator CHRIS EVANS—So Defence has not been canvassing the issue with bidders or potential builders.

Senator Hill—There was no discussion in the lead-up to the budget of any new project for larger offshore patrol boats.

Senator CHRIS EVANS—Either for Defence or for Fisheries management et cetera?

Senator Hill—Correct. There is debate. My only hesitancy is that there is continual debate about every option for everything, and there is continual debate around the edges on the issue of a dedicated capability for Southern Ocean patrols which would be a larger, differently designed vessel. Whether that was what in some way got confused with this, I do not know. New Zealand is looking to purchase two offshore patrol boats which would be larger. Whether that was part of the confusion, I do not know.

Senator CHRIS EVANS—No, but of Defence's purchasing of patrol boats it is still intending to proceed on the original understanding about one size of patrol boat.

Senator Hill—That is correct.

Senator CHRIS EVANS—And it is looking at 12, is it?

Senator Hill—We are looking at a capacity of so many days of availability. The tenderers were not limited to the number of boats they could provide to meet that requirement.

Therefore it includes the service capability. The consortiums were to take into account how many boats they wished to provide to achieve that number of days.

Senator CHRIS EVANS—But we are talking in the order of 12, are we? Is that ballpark?

Senator Hill—Most people in the industry seem to be talking about 12 or 13—round about that.

Senator CHRIS EVANS—Therefore, Defence has not been consulting with industry about building some larger patrol boat for Defence.

Senator Hill—No, except I think that again, if you read the industry reports, you will see that one or more tenderers was floating the idea of some of those boats being built to a different specification.

Senator CHRIS EVANS—Yes, I am really more interested in what Defence is saying about that, though. Obviously there are boat builders out there who will build you anything and have all sorts of suggestions about why you should buy what they build.

Senator Hill—It is not what the government has been seeking. The government has been seeking what was in the request for tenders.

Senator CHRIS EVANS—And you can provide reassurance that you will be seeking to fulfil that tender process?

Senator Hill—Yes.

Senator CHRIS EVANS—Without variation, in terms of the order?

Senator Hill—Yes.

Senator CHRIS EVANS—That is all I wanted to clarify.

Senator Hill—You would never say no, but it would mean government revising its current position and I know of no plan to do that.

Senator HOGG—On the same issue, how many tenderers are there now? Is it the same number that we had at the last estimates or has there been a reduction in the number of tenderers? Have some, naturally, pulled out?

Rear Adm. Scarce—Since the last estimates, I think we have excused two of the original nine, so seven remain.

Senator HOGG—Are any of those multiple tenderers? I think we were told on the last occasion that three were putting in either two or three tenders.

Rear Adm. Scarce—There were a couple of tenderers that put in different options, of essentially the same sort of vessel with different configurations.

Senator HOGG—So they are still in the melting pot, so to speak, and you have had a couple of tenderers pull out?

Rear Adm. Scarce—We have excused two tenderers who did not meet the essential requirements of the RFT. Seven remain, and our goal is to short-list that to three.

Senator CHRIS EVANS—Why has the Jindalee operational radar network been removed from your list of 20 major capital equipment projects?

Senator Hill—Hopefully because it is going so well.

Senator CHRIS EVANS—Nothing you have told me supports that assertion.

Mr Roche—I am not totally satisfied with the structure of this table, but it is on this-year-expenditure. It is the 20-major-projects-by-this-year expenditure. I think that, subject to what Ms McKinnie says, it is simply there because its expenditure this year has fallen below the threshold.

Ms McKinnie—That is correct.

Senator Hill—We are at the wind-up stage of that, aren't we?

Mr Roche—We are getting down towards the final stages.

Senator CHRIS EVANS—I thought you used to show them as a 20 major project figure. But now this is purely the current year expenditure for the top 20 projects. Is that right?

Mr Roche—No, it has been that way for a while. It is actually by forecast current year expenditure, and I think that is a weakness with the table. We probably need to try and find a better way to identify the major projects.

Senator CHRIS EVANS—It seemed a fairly big project not to be on your top 20 list, that was all. What does it mean, then, that we are going to spend on Jindalee this year?

Senator Hill—In the next year?

Senator CHRIS EVANS—Yes.

Senator Hill—In terms of the capital contracts? You have already got operational people, haven't you, so how do you distinguish that?

Ms McKinnie—I do not have the information with me, but I can get it in terms of our estimates for this coming year.

Senator CHRIS EVANS—Perhaps you could take that on notice. But what does that say then? Could someone give me a brief description of where we are at with the project.

Ms McKinnie—The project is currently going through its test and integration phase. We have currently scheduled operational release for early next year. Operational release is a point where Defence can start using the radar and effectively doing our operational testing on the system, with the view that we accept it by mid-2003.

Senator CHRIS EVANS—So mid-2003 is still your anticipated fully operational date, is it?

Ms McKinnie—That is the final acceptance date from the contractor.

Senator CHRIS EVANS—So the reason it has dropped off the list is, as you say, Mr Roche, the way you have ranked them. Somehow I found that a bit misleading.

Mr Roche—It has been done for some time.

Senator CHRIS EVANS—I guess it has always been there and then it dropped off. I wondered where the \$1.2 billion project had gone when it had not made the top 20. I would like to ask a couple of questions about the defence industry rationalisation process. Is it true that you have issued discussion papers on rationalisation in the shipbuilding, weapons systems, electronics and land systems?

Mr Learmonth—We have in fact issued a number of papers in relation to each of the sectors in which the Defence Industry Advisory Council set up working groups. In relation to the maritime sector, there has been a number of papers issued; also in aerospace, electronics, land and weapons.

Senator CHRIS EVANS—Am I wrong then? I thought you were working on the basis of four industry groups. Is it broader than that?

Mr Learmonth—No, principally four: maritime, aerospace, electronics, and land and weapons together.

Senator CHRIS EVANS—So a discussion paper on rationalisation in each of those areas has been distributed?

Mr Learmonth—A number of them and numbers of iterations of those, as we look at various issues associated with them.

Senator CHRIS EVANS—What does that mean, Mr Learmonth? Is there a discussion paper on shipbuilding out and about in the industry?

Mr Learmonth—There is not much out and about per se. There is a draft sector plan that has been through various iterations that has been circulated to the shipbuilding working group. There have been a number of other issues papers in relation to shipbuilding, contracting strategies, for example, that have similarly been circulated to that group.

Senator CHRIS EVANS—These papers are not broadly distributed; they are only distributed to members of the working group, are they?

Mr Learmonth—Correct.

Senator CHRIS EVANS—So all relevant industry players are not necessarily on that working group.

Mr Learmonth—In the case of shipbuilding, it is a comparatively small industry, so most of them are. The shipbuilding working group comprises basically chairman and managing director level from the Submarine Corporation, from ADI, Tenix, Forgacs, British Aerospace—or BAe Systems—and a representative from ABL.

Senator CHRIS EVANS—But clearly the other areas where there are much more diverse numbers of contractors and suppliers are not all represented, or have you got very large working groups?

Mr Learmonth—They obviously cannot all be represented. In electronics, we certainly have a large and diverse group. They are, I guess, represented broadly through individual members in the various tiers, plus through relevant industry associations.

Senator CHRIS EVANS—As I understand it, these are distributed with instructions that they not to be handed on or copied. Is that right?

Mr Learmonth—Correct.

Senator CHRIS EVANS—I use ‘discussion paper’ loosely for want of a better term, but they are limited circulation papers.

Senator Hill—Probably ‘working papers’ would be a more appropriate term.

Senator CHRIS EVANS—I am happy for you to use whatever the—

Senator Hill—I paused when you said ‘discussion papers’ because, as I understand it, there is not a preferred design for each of the sectors being issued either by the department or by government for final input. It has not got to that stage; apart from the work the department is doing in its relationship with the subgroups, it is still workshopping ideas and developing suggestions. As I said, that is why I use the expression ‘working papers’ rather than ‘discussion papers’.

Senator CHRIS EVANS—One of my concerns, and one of the concerns that has been raised with me, is the closed nature of that debate. I concede that not everyone is keenly interested in the issues, but there is obviously a whole range of people who are. I am trying to understand on what basis the circulation is determined. You tell me it is through the membership of the working group, but what opportunity will there be for other interested parties to join this discussion?

Mr Learmonth—There are a number of forums, and the working groups were established by industry for industry. The membership, composition and scale was determined by the Defence Industry Advisory Council subcommittee, so they determine the range, scale and representation. The papers per se—or those particular papers, certainly—are discussion papers designed to facilitate discussion within those working groups and to explore some different ideas. That said, there is plenty of discussion in the broader defence community about the concepts that are contained in them, both in speeches and presentations that people give in opportunities for people to interact—for example, with industry association groups and forums. There is also a very substantial process of one-on-one interaction with defence companies.

Senator CHRIS EVANS—How does that happen if they are not allowed to hand them a copy? You describe what sounds like a very open and inclusive process, but the feedback I am getting is that people are not allowed to hand them over and are concerned, quite rightly, about protecting the confidentiality that they have been asked to enter into by Defence. You describe for me what is a broad discursive process, but I hear that you make it very clear they are not to hand them on, not to copy, and this information is not to be made widely available. I am getting two different images of what is happening.

Mr Learmonth—It is levels of detail. There is a certain level of detail in the papers that we use to promote discussion within working groups and in order to maintain some sort of reasonable control over that process. We do ask for them to be limited. The papers are discussion papers. They carry no endorsement whatsoever as to a Defence view, let alone the minister’s view, and we like to retain some proper control over their circulation. The broader concepts embodied in the paper—the directions that we are heading or that we are exploring—are certainly made available in various forms to various audiences.

Senator CHRIS EVANS—Where do I go to find those, Mr Learmonth?

Mr Learmonth—To find what, Senator?

Senator CHRIS EVANS—Those ideas, those issues. I am interested, so how do I find them?

Mr Learmonth—Those particular issues papers?

Senator CHRIS EVANS—Yes.

Mr Learmonth—I guess the general way that industry does it is to ring us. The teams within each of the sectors spend quite a lot of time outside the working groups talking to

individual companies or others who have expressed an interest. There is a range of opportunities for them to have input, to understand what is going on.

Senator Hill—If you are interested, you are probably already in industry organisations. You are probably part of the process.

Senator CHRIS EVANS—Are the ACTU part of the process?

Senator Hill—Perhaps the wrong people come to me, but I have not been inundated with complaints about people being excluded from the process.

Mr Roche—I have not heard a single complaint.

Senator Hill—I do not recall any.

Mr Learmonth—We have had one request for inclusion and that was accommodated.

Senator CHRIS EVANS—That is fine. I am really trying to understand the process. I have had it raised with me that people cannot get hold of these discussion papers. Now I am told they are not discussion papers; they are—what did we decide upon?—working papers

Senator Hill—My concern with ‘discussion paper’ is that it almost sounds as if it is something that is widely distributed.

Senator CHRIS EVANS—Yes, for discussion.

Senator Hill—Yes. If it is a group, using the expression ‘working paper’ is probably more appropriate, but I do not think it makes a lot of difference.

Senator CHRIS EVANS—I am just trying to understand how people can get into that debate and what the process is. Where does this lead you? Does this mean that, from these working papers, you are going to create a discussion paper that will be made more widely available? Perhaps you can explain to me the breadth of the process.

Mr Learmonth—There are two parts to that question. The first part is: how do people become engaged in it or involved if they are interested? The answer is: doing what they are doing now. The broad concept is fairly well publicised and the minister has mentioned in a number of key speeches that there has been publicity about it, that it was an election commitment and so on. So there is a general level of awareness about it. Those who wish to participate do so in a number of ways. They may wish to join the working group. I am aware of only one request to do so beyond the scope that DIAC originally constructed and that request was accommodated. They can do so through their industry organisations and industry organisations occasionally have particular forums around this issue. For example, I spoke to one in Victoria a couple of months ago which had a very substantial turn up and degree of interest in it. They can engage in one-on-one discussions with the teams who are working on individual sectors, and frequently do so. As part of understanding those sectors in greater detail, there is a proactive visit program where teams have gone out off their own bat and spent quite a bit of time talking to different players within each of the sectors to try to understand them. So there are a number of ways into the process. The second part of the question is: then what? All these things are informing the development of policy advice which, in due course, we will put to the minister and government as to how we might look to implement that policy.

Senator CHRIS EVANS—So it is not intended to be a public process?

Mr Learmonth—Public in so far as I have described. It is hardly private.

Senator CHRIS EVANS—The way that you described it does not necessarily make what I would call a public process. How does the government see this progressing? I think your final point was that this informs policy advice that the department will give to the government. That is fine. That is perfectly appropriate. I am asking: is there a public component to this process or is it about the department testing the water, judging opinions, getting feedback and making policy advice? As I say, if you had put to me that there were to be discussion papers with the connotations that I think the minister and I share about what a discussion paper is, it would seem from what you have told me tonight that it is a slightly different process, that it is a much more in-house industry players' dialogue. I am trying to understand whether there is any intention to have a broader public process, among other things. Obviously, a lot of these decisions have quite huge regional employment and economy issues—as the minister from South Australia would be well aware. The shipbuilding one is at the top of the list on my pad. When will there be a public process or is there any opportunity for anyone other than those key stakeholders to be involved in that?

Mr Learmonth—There is any opportunity for people to come and talk to us about it, and they frequently do. Shipbuilding is an example of where we fairly regularly have the development authorities from the relevant states come and speak to us. It is not uncommon for people to take the opportunity—

Senator CHRIS EVANS—I guess I am asking: apart from the 'my door is always open' response, is there planned to be any public consultation or public discussion paper or anything that would involve seeking that?

Mr Learmonth—There are no plans per se. That is not something I have yet had the opportunity to raise with the minister.

Senator Hill—If you take shipbuilding, which is probably the most advanced to what we are expecting as a result of this process of consultation that has been taking place between the department and industry, there will be a series of recommendations from the department which will then be considered by government. Ultimately, government will have to determine the shape of these strategic alliances and the parties to the strategic alliances. It might be that the department recommends some further and more broadly based public processes as an interim step. That is still to be determined. I have said before that the implementation of this policy is more difficult than writing the policy itself. As you say, it is quite complex in terms of its consequences to various parties and various regions but, in the end, we are seeking to ensure the best defence industry capability in the longer term, and that should enhance defence industry in giving it the confidence that it needs to be able to back itself into the future in terms of investment, employment, research and the like. It seems widely accepted now that this reform is desirable in Australia. It is occurring throughout the world but the implementation of the principle is not easy, and we are basically taking it step by step.

Senator CHRIS EVANS—Minister, what do you say, then, about the timetable for this? You say the shipbuilding is most advanced and you say that, at the moment, there is no broader public consultation or discussion process planned and that that is something the government could consider.

Senator Hill—I was looking to recommendations regarding the department's shipbuilding this month.

Senator CHRIS EVANS—Does that mean that the government is likely to make a decision this month on the shipbuilding?

Senator Hill—I would prefer to see the recommendations.

Senator CHRIS EVANS—But is it your view that you would look to make a decision fairly quickly on that?

Senator Hill—It depends on how it is done. If the shipbuilding alliances are shaped around particular platforms, there can be a good argument for that. In other words, as you have already heard today, the department is ready to start a series of design studies in relation to the air warfare destroyer. Therefore, it seems to me that it would be useful to know at this time who will be the strategic partner or partners in that project, because they can be consulted at the very start of the project rather than some way into the project.

Senator CHRIS EVANS—Are you saying that model involves you having a different set of strategic partners on different projects?

Senator HILL—It could; that is one of the options. But I am wary of speculating in case it is misinterpreted.

Senator CHRIS EVANS—I am more interested in the process than in the possible permutations or outcomes, in a sense. I do not intend to draw you on that.

Senator Hill—It was commonly believed that the principal partner at the sharp end of naval shipbuilding would revolve around the purchase of the Australian Submarine Corporation. For the time being, the government has put that issue on the backburner while we settle a range of interim issues in relation to ASC—the disputes with Kockums, the proposed capability agreement with Electric Boat, the disputes between the government and ASC, the terms of the contract for the mid-cycle dockings—

Senator CHRIS EVANS—So you have formally put that on the backburner, Minister?

Senator Hill—Yes.

Senator CHRIS EVANS—What decision was taken then?

Senator Hill—Just to pause in that process while we settle what I would describe as interim issues; you will get a more confident sale process if these issues are settled rather than if they are uncertain.

Senator CHRIS EVANS—Are you now saying that there will not be any connection between the sale of ASC—

Senator Hill—No, what I am saying is that one argument would be to at the same time delay the appointment of the strategic partner in the sharp-end naval shipbuilding until the Submarine Corporation issue is settled. But it is not necessarily the only way to go forward.

Senator CHRIS EVANS—But you are still keen to make a decision on the structure of the shipbuilding industry quickly?

Senator Hill—For other reasons, as I have just said to you, yes.

Senator CHRIS EVANS—Yes, but you are keen to make the decision in terms of the principles of how the shipbuilding industry would be restructured but not the decision about who the key players necessarily are. Is that what you are saying to me?

Senator Hill—Again, it is not necessarily one way or the other. The path that seemed to be popular 12 months ago would really have determined the party rather than the design, if it were to revolve around the purchaser of ASC. But it does not necessarily have to be done that way. So I am saying that we do not have a firmly settled blueprint. We are allowing the

process to evolve. They are big issues—they are very important to Australia and they are very important for the industries concerned—but because we believe the principle is right we want to keep the process moving along.

Senator CHRIS EVANS—What do you say about the timetable for decisions on the other three areas?

Senator Hill—I think the electronics is the most complicated of all; land, perhaps not so complicated. Again, it is our desire to keep the process moving but the popular view has been that we would probably resolve the shipbuilding one first.

Senator CHRIS EVANS—You seem to be having some doubts about that.

Senator Hill—Only because, as things have developed, if government again forms the view that it should revolve around the purchaser of ASC, you might say that that has put the shipbuilding one back a bit so it might get overtaken by one of the others.

Senator CHRIS EVANS—When would you say the others would be brought to a head—six months, a year, three years? What sort of time frame?

Senator Hill—I think the goal was that the department would at least be producing recommendations for us during the course of this year.

Senator CHRIS EVANS—On all four areas?

Senator Hill—Yes.

Senator CHRIS EVANS—All right. Thanks for that. I will leave it there.

CHAIR—It being a couple of minutes to 11 p.m. we will adjourn. Before we adjourn, thank you Minister, Dr Hawke and Admiral Barrie.

Committee adjourned at 10.57 p.m.