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JOINT COMMITTEE OF PUBLIC ACCOUNTS AND AUDIT

**Reference: Financial reporting and equipment acquisition at the Department of
Defence and Defence Materiel Organisation**

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**JOINT STATUTORY COMMITTEE OF
PUBLIC ACCOUNTS AND AUDIT**

Wednesday, 9 May 2007

Members: Mr Barresi (*Chair*), Ms Grierson (*Deputy Chair*), Senators Mark Bishop, Chapman, Hogg, Humphries, Murray and Watson and Mrs Bronwyn Bishop, Mr Broadbent, Dr Emerson, Dr Jensen, Miss Jackie Kelly, Ms King, Mr Laming and Mr Tanner

Members in attendance: Senators Mark Bishop, Chapman, Hogg and Murray and Mr Baressi, Ms Grierson and Miss Jackie Kelly

Terms of reference for the inquiry:

To inquire into and report on:

Progress in implementing systematic reforms in the areas of financial reporting and equipment acquisition at the Department of Defence and the Defence Materiel Organisation (DMO), as identified in ANAO financial and performance audits, the Defence Procurement Review 2003 (the Kinnaird Review) and the Senate Foreign Affairs, Defence and Trade References Committee's 2003 Report on the Inquiry into Materiel Acquisition and Management in Defence, including the following:

- Progress in implementing Defence's financial remediation plans, relative to international best practice in these areas, and recommend any further measures that can be adopted;
- Progress in implementing the Kinnaird Reforms, relative to international best practice in these areas, and recommend any further measures that can be adopted;
- Review Australia's relative achievements in procurement and financial reform relative to international best practice in these areas of defence administration; and
- Assess progress in Defence's adoption of international business accounting standards relative to international best practice in this area of defence administration.

WITNESSES

**GUMLEY, Dr Steve, Chief Executive Officer, Defence Materiel Organisation, Department of
Defence 1**

**HURLEY, Lieutenant General David John, Chief, Capability Development Executive,
Department of Defence 1**

Committee met at 11.28 am

GUMLEY, Dr Steve, Chief Executive Officer, Defence Materiel Organisation, Department of Defence

HURLEY, Lieutenant General David John, Chief, Capability Development Executive, Department of Defence

CHAIR (Mr Barresi)—I welcome everybody here this morning to this public hearing for the inquiry of the Joint Committee of Public Accounts and Audit into financial reporting and equipment acquisition at the Department of Defence and Defence Materiel Organisation. The purpose of this hearing is to discuss the capability development process within the Department of Defence and its relationship with materiel acquisition. I advise witnesses that the hearings today are legal proceedings of the parliament and warrant the same respect as proceedings of the House itself. The giving of false or misleading evidence is a serious matter and may be regarded as a contempt of parliament. The evidence given today will be recorded by Hansard and will attract parliamentary privilege. I welcome Lieutenant General David Hurley from the Department of Defence and Dr Stephen Gumley from the Defence Materiel Organisation. Do you wish to make opening statements?

Lt Gen. Hurley—Thank you very much. Given that the committee is today essentially reviewing the relationship between my organisation and DMO and how we work together, I thought that if I gave a simple statement for a couple of minutes it might answer some of the frequently asked questions. Then you can get down to the meat of the issue. If that is not sufficient, I am happy to take your questions.

CHAIR—Fine, fantastic.

Lt Gen. Hurley—In 2003, the Defence procurement review addressed the breadth of the capability development and acquisition processes within Defence, particularly related to major capital equipment. The review recognised the critical nature of the decisions made within Defence prior to government approval of Defence capital investment projects. To improve the quality of decision-making information provided to government, the review made three major recommendations. Recommendation 1 was that Defence should present to government the following on a regular basis: an assessment of the type of contingencies; advice on the military force required and the capacity of the ADF to supply this force now and into the future; and advice on the capability to be sustained, acquired or retired to ensure that this can be achieved at acceptable cost. The second recommendation was to appoint a three-star officer to be responsible and accountable for capability definition and assessment and to establish the Capability Development Group. The third recommendation was that government should mandate and enforce, via revised cabinet rules, a rigorous two-part system for new acquisitions, with government considerations dependent on comprehensive analysis of technology, cost—both prime and whole-of-life—and schedule risk subjected to external verification.

I am a major participant in the implementation of recommendation 1, I lead the Capability Development Group and therefore am the three-star referred to in recommendation 2, and I am responsible for the implementation of recommendation 3 within the department. I achieve the review's requirements through the leadership of Defence's professional capability development

organisation, the Capability Development Executive, which I will abbreviate to CDE for future reference. CDE is a combined uniform and public service organisation of approximately 260 people. At its most basic, it prepares the Defence Capability Strategy, which is linked to recommendation 1; the Defence Capability Plan, which is linked to recommendations 1 and 2; and all major capital equipment acquisition business cases for government approval, which is linked obviously to all three recommendations. CDE was formally raised on 1 July 2004.

It is important to stress from the outset that our consideration of capability is not platformcentric. The DCP is only one expression of the changes of capability that are derived from our annual capability review processes. All the fundamental inputs to capability, such as personnel, facilities, training, doctrine and the equipment itself, are considered when solutions to potential capability gaps or new capability opportunities are considered. The fundamental inputs of capability are certainly considered for every acquisition proposal. The DCP concentrates public discussion on platforms, but this belies the extent of the work we do to shape the future capability of the ADF.

It is also important to note that our work is conducted in close association with many internal and external stakeholders. These are the DEPSEC Strategy for the provision of strategic planning guidance; the capability managers in the department, being the three service chiefs—the VCDF, Deputy Secretary I and S and the CIO—for whom I sponsor major capital projects; CEO (DMO), Dr Gumley, whose organisation works hand in glove with mine throughout the consideration of the development of capability proposals; DSTO, which provides both R&D and technical risk assessments; our allies for interoperability requirements; defence industry for solutions; and the central agencies of government for external independent review.

The organisation is approaching its third birthday, on 1 July this year. In terms of those recommendations, we have implemented what government has requested us to do and we report on a monthly basis to the Defence Procurement Advisory Board, which was established to oversee the department's implementation of the review.

CHAIR—Thank you very much. Dr Gumley, do you want to make a statement?

Dr Gumley—I will make one comment. The Kinnaird implementation has been rigorously undertaken inside Defence. It has been quite pleasing to me to see that all the recommendations have been adopted. The process has been very rigorous in making sure that there is a separation between the specifying writing organisation, which is CDE, and the implementer, which is DMO. That gap, that discipline, of ensuring that the scope of the project and the specifications are clearly written is one of the areas in which I think we will show a lot of dividends into the future. The outcome of all this is that we seem to be getting much better clarity of requirements. Once you have good clarity, industry has a much better chance of delivering those requirements on time and on budget. In my view, the Kinnaird process is certainly leading us in the correct directions.

CHAIR—General Hurley, I am not sure whether you have met everyone here before. There are a couple of new faces, so I will introduce the committee to you: Sharon Grierson, deputy chair, from New South Wales; Senator Chapman, who has just joined us, a Liberal senator from South Australia; Senator Andrew Murray from Western Australia; Senator John Hogg from

Queensland; Senator Bishop from Western Australia; Miss Jackie Kelly from New South Wales; and me from Victoria. Thank very much for that opening statement.

I have a general question to you, Dr Gumley. Since the last time we met, a couple of newspapers articles have been critical of the new contract proposals, mainly from the AIG. Do you have any comment to make about some of those criticisms and concerns, particularly about the transfer of risk and whether it has been reasonable? Do you think that might shut out quite a few Australian companies from putting their hand up?

Dr Gumley—No, I do not think it is going to shut out Australian companies. I think one of the important issues for Defence as a customer is to get the projects delivered on time and on budget and for the sustainment of fleets is that we allocate risk to the party best able to manage that risk. A basic principle of insurance, business, banking or whichever field of endeavour is that you should allocate the risk to the party who has most knowledge of it because they are the party best able to price that risk. We are attempting through the contracting improvements to redefine the risk allocations. There are some areas of risk which the Commonwealth should always retain, there are other areas of risk which clearly belong to the companies and there is a portion in between which can be debated from project to project.

It would be a more efficient allocation of Commonwealth moneys for the companies to take on more risk in some areas because they can look after them. There is an imbalance, for example, at the moment between the ability of the Commonwealth to levy liquidated damages in a contract versus the company's ability, if we do something wrong, to ask us to pay expensive excusable delay claims. It is a complicated area of contracting. We are working with industry to try to make it happen. Just last week I had all the chief executives of the main prime companies discussing with my senior people and me how we are going to do this better. At this stage it is a cooperative process and I am quite happy with the way it is going.

Ms GRIERSON—Lieutenant General Hurley, it seems the budget shows that they have taken into account some of your responsibilities in terms of personnel, have listened to your recommendations regarding future needs and have taken them very seriously. When we look at the operations of DMO and your department, we are really looking at expertise. Can you tell me the current staffing levels at executive levels 1 and 2?

Lt Gen. Hurley—I do not have the numbers to hand, but I can say that on the military side of the house there is me and one two-star officer, Admiral Matt Tripovich, who is the head of capability systems. That is the primarily military organisation that does the determination of the requirements for a project. They are the ones who develop the business cases and so forth in partnership with DMO. In that organisation, there are four one-star officers. Army, Navy and Air Force are represented there in aerospace development, land development and maritime development. The fourth one is integrated capability development, which is critical to making sure that we are not running off in stovepiped capabilities.

Ms GRIERSON—So that is your complete executive level staff?

Lt Gen. Hurley—No. That is in that division. I also have one one-star, who is the director-general of capability planning, who links with the deputy secretary of strategy in interpreting strategic guidance and preparing for me the defence capability strategy, which lays out how we

are going to deliver capability in the future. He runs a mixed military and civilian branch. Below them, there are obviously a number of colonels, or EL2 equivalents in the APS. On the civilian side, in the other major division in my organisation, run by Dr Ralph Neumann, which is called the Capability Investment Resources Division, I have two equivalents SES1, one-star level. One looks at investment analysis. He does independent analysis of the work on business cases. Another does cost analysis, looking at the cost basis for the proposals that go forward.

Ms GRIERSON—Are you satisfied with their abilities? Have you had to increase their abilities or have they been specially selected because of their expertise? What has been the process?

Lt Gen. Hurley—On the military side of the house, the vast majority of the officers who come into my organisation come in for their operational experience and ability to help us define what the capability solution is. Obviously many of them come in with tertiary qualifications. Quite a number of them are engineers and so forth and have that background. Very few of them have project management expertise. I have tried a number of approaches over the years I have been in this job to try to resolve those sorts of issues. I request them to come in with them if they can. That is a benefit, because I get many people from the Army, for example, who go through the Army technical staff officer course. They come with those skills sets. I get people who come back from DMO. Many of my people who cycle back through my organisation from DMO have that expertise. For officers who do not have that, we have some basic training when they arrive.

I have an arrangement with Dr Gumley whereby I embed project management staff from his organisation to provide guidance in the running of the projects. I also have an organisation that works for Admiral Tripovich, which essentially runs my process assurance and provides support and the help desk for each of the project officers as they move through a project. We try to build a fairly strong support system around them when they come in. Frankly, if I get a fellow for two years who has just commanded an infantry battalion and who has to drive some projects for me on the Army side of the house, for example, I do not necessarily have time to train him to become a professional project manager. But I can give him all the assistance he needs to get from A to B in a project from the time he is in the organisation.

Ms GRIERSON—Dr Gumley, are your staffing levels similar at executive level 1 and 2 and SES1?

Dr Gumley—I have 32 SES officers and 20 military star ranked officers at SES1 and 2 or military ranks band, or star rank 1 or 2. There are 1,512 people at EL1 and EL2, colonel equivalents. It is substantial. They are the figures that came out of the PBS which was published last night. They are figures for the year ahead rather than the year just gone.

Ms GRIERSON—How would you describe the relationship between your teams and DMO's teams?

Lt Gen. Hurley—It varies from excellent to turbulent at times, depending on your point of view on where we are at on a particular project.

CHAIR—You need the turbulence. You need it.

Ms GRIERSON—When the pressure is on, it is really on.

Lt Gen. Hurley—DMO is an organisation of about 6,000 now. I run to 260. But I am there framing the issue, looking at what the requirements were and doing the system engineering in conjunction with DMO to develop what the option sets are. I have to understand what the option sets are, interact with industry to see what the solutions are, bring that together in a business case that we have both worked on and take it across. I provide the sort of capability leadership, the direction in which we want to go. I talk to the services—to others who have those needs—and co-ordinate that argument, bringing it together, and I make decisions. One of the purposes of creating my position was to have someone who sat outside the chain of command of the three service chiefs. I am independent of that. I respond only to the secretary, CDF, and therefore to the minister through that route. That relationship is very important to help us to develop the project proposals.

Ms GRIERSON—Dr Gumley, do you want to comment on that?

Dr Gumley—To go to the resourcing, I think it is fair to say that CDE is doing an extraordinarily large amount of work with minimal resources. We have an obligation to government to get as many of the DCP projects through the system as we can. We have an informal arrangement whereby I loan CDE experienced project managers so that they can help the domain experts. CDE has all the domain experts with a military background. As I think we have said in previous places, you do not expect too many civilians with some of the skills that military officials have. But some of the skills we can add to help that are those in project management. We identified previously that project management was a skill deficit right through the Commonwealth, let alone inside Defence. We have also talked about how much work we are putting into developing and upskilling our own project managers. As they are getting better qualified and as we are creating a greater source of supply, we are using them in the CDE areas as well as the DMO areas.

Ms GRIERSON—I have a question for both of you: has that exchange of personnel succeeded in breaking down old cultures and old resistance? Is it working?

Lt Gen. Hurley—It takes its time, but it is working. When I first came into the job, in this appointment—because I had been a two-star and a one-star in this organisation previously, or in its predecessors—there used to be an analogy that my organisation or its predecessor used to throw dead cats over a wall to DMO.

Ms GRIERSON—Not blame shifting and all that sort of stuff? That never happens!

Lt Gen. Hurley—DMO would have to resuscitate them to turn them into capability. My original response to that analogy was, ‘Well, we have to give you live cats.’ But in fact the analogy is wrong. There is no wall.

Ms GRIERSON—No. There can only be victories.

Lt Gen. Hurley—We work hand in glove. I cannot do my business, because DMO handles the interaction with industry for me.

Ms GRIERSON—So your interaction with industry is the two-pass system.

Lt Gen. Hurley—I will just qualify that.

Ms GRIERSON—Okay.

Lt Gen. Hurley—I do a lot of work with industry in determining what the future needs might be for the Defence Force and broad requirements option sets and so forth to frame the Defence Capability Plan. Under the two-pass system, between first and second pass, when we go out for requests for tender to get tender-quality information for government to make a decision on, I use Steve. Essentially, I contract his organisation to run that part of the process with my people. For example, with the AWD, the air warfare destroyers, and the LHD projects and so forth, there are two-star equivalent civilians running those projects. But I have staff who sit inside that, keeping a close control on the capability requirement and making sure any changes that need to occur are approved at the right level. They run the interaction with industry for me. They will run the RFTs, run the competitions, do all the contracting side of the house and develop the acquisition strategy, which I take as part of the proposal back to government to say, 'To deliver this capability, here are the options. You can go A, B, C and D. Acquisition strategies for each of those options may be different or may be the same, depending on the outcome.' We do that together.

Dr Gumley—CDE takes the input of the service chiefs, the military input, from one side, and takes a commercial input, which we have filtered from industry on the other side, to marry the two together to see what can be achieved.

Ms GRIERSON—We come to the conclusion about many projects that, had the initial assessments and recommendations been made with more rigor at the beginning, we would have had a better outcome. How much of that can be pointed at your group?

Lt Gen. Hurley—It depends on how far you want to go back. From 1 July 2004?

Ms GRIERSON—You do not have to do a confession now, publicly.

Lt Gen. Hurley—If you go back to what the DPR was all about, the basic issues that Kinnaird put on the table were: the process from government strategic guidance to capability proposals was opaque to government. We needed to get that clarified. Hence recommendation 1: 'Come to us on an annual basis to explain that linkage.' We produce two key documents, Defence Planning Guidance, which is the interpretation of the higher level issues from government, and the Defence Capability Strategy, which is, from my point of view, the projects for which I need to be thinking about new capability to resolve those problems. The DCP in its current form had predecessors, but since Kinnaird started with us, or really since the 2000 white paper, we have locked that process, or that expression of the change we require, into place.

If you go back to before 2003, when the Kinnaird review occurred, for a couple of years there was a rudimentary first- and second-pass process. If you go back before that, it was really a one-stop process to get an approval from government. In those earlier decisions, we had not drilled down anywhere near to where we do at the present time with industry in terms of understanding the risks, cost, capability and schedule that we are going to take on. We certainly did not get the

fidelity of information to government at the time. Most of that discussion happened after government made the approval. I have to chuckle sometimes when I read papers that say 'cost blow-out in project X' when project X has not been approved by government. All we have done is refine an estimate.

Our catchery in this, although it is a bit cliched, I suppose, is to give them a good understanding of the technical risks. We do a technical risk assessment with DSTO. Dr Lough will be at our next meeting to talk about that with me. We have done the industry interaction. We have gone to the point of going through the tender process, down to selection, and often have gone through an offer definition refinement process with industry. That is essentially saying, 'If government approves this project on this solution, that is what the government will contract on.' We have moved the knowledge and our understanding of what is available and what is achievable a lot further than we had in the past.

Ms GRIERSON—On the staffing issue, the Proust review suggested IT and human resources were areas of deficiency. Have you recruited in those areas or responded to that?

Lt Gen. Hurley—They are two separate areas in the department. There is a head of Defence personnel establishment. I interact with him in terms of that high-level guidance. I am a participant in the decision about what the future workforce or force structure of the ADF might be like. His job is to look at the workforce to support that force structure. In each of the capability proposals that go forward, I go back to him to say, 'These are the influences this will have over future workforce requirements, skill sets, numbers, time frames to deliver them and so forth.'

On the ICT side of the house, we have a CIO who is fundamentally responsible at the moment for putting in place our IT infrastructure and managing that infrastructure, and who has an input into the capability issue. But that is one of the things that Proust was getting at about, 'What is that line?' In the DCP you will see there are many projects that deal with ICT-related projects.

Ms GRIERSON—Do you directly have any professional service providers?

Lt Gen. Hurley—Me?

Ms GRIERSON—Yes. How many of those would you have?

Lt Gen. Hurley—It varies depending on the number of projects.

Ms GRIERSON—And across all different areas of expertise?

Lt Gen. Hurley—Yes. But again I use the DMO panels to get, say, system engineers or those sorts of skills. If I need them I will go out through the DMO panel. We share similar skill sets.

CHAIR—I want to follow up on one of the lines of questions that Ms Grierson asked. In terms of accountability, you mentioned that, in the two-pass system, you have input from the DMO and his staff, in terms of the commercial considerations, and you have your own guys in the military. When you present the plan to government, either for consideration or approval, is

that plan submitted under your name, or is it a joint plan that is submitted? Where does the responsibility lie?

Lt Gen. Hurley—The majority of them are submitted under my name. The bid submission and the cabinet submission leave the department under my name, but it has been through the defence committee process. I am signing it off showing that I am the final one to sign it off, but if it has been through DCIC—the Defence Capability and Investment Committee—which is chaired by the secretary, he has actually agreed. I chair a committee called the Defence Capability Committee which looks at the majority of the proposals that go forward, but again the secretary and the CDF obviously need to be briefed and agree with the outcomes of that. But I am signing off those. In some of the bigger projects, either Stephen or I or the secretary of the CDF will sign it off for the minister, depending on the complexity and nature of the project.

Dr Gumley—The projects are approved or put to government by the secretary or the CDF, but the submissions are mostly prepared by CDE. Each of them has a paragraph in them that reflect other groups' involvement. For example, DMO will certify that the costs, schedule and commercial risk of the project are satisfactory, low, extreme or whatever. We will make the judgment on the commercial sides; ditto, DSTO will make the judgment on the technical risk by giving a technical index number. So, although it is mainly under a CDE presentation, we add to it at the bits where we have our expertise.

Lt Gen. Hurley—We have gathered in all those views and made sure they are coherent.

Ms GRIERSON—Can we request a copy of one of those submissions, even one that has gone, just to see the amount of information that is in them?

Lt Gen. Hurley—I cannot table this for you.

CHAIR—And that is one of the small copies.

Lt Gen. Hurley—Do not worry about the size.

CHAIR—That was to purchase new bios!

Lt Gen. Hurley—Actually, this is a very sharp biro that flies at a high speed! When I go to government, I am saying: 'There is the business case for one option we have been through.'

Ms GRIERSON—And that will have something in it from all these different people who have contributed?

Lt Gen. Hurley—Yes, and there is a preface to that. That says that these are the recommendations to government and these are the options we have looked at. Then we go through a standard set of considerations: capability risk, cost risk, schedule risk, Australian industry input, and technical risk assessments. Then we have to look at the financial implications—so, the programmatic from the chief finance officer's point of view and so forth. But underlying that document—and this is the reason that these are so big—is the operational concept document that explains how we intend to use it in the future. It becomes the basis on which we develop a functional performance specification, which is what we use as the basis to

tender to industry. So we can connect the dots from the operational concept document to strategic items, and explain how we think the new capability is going to operate in the future ADF and the connectivities it will have. This is the start of the 'black box' bit of the systems engineering side of the house. The FPS then describes what we think the key capabilities are—what the capability drivers will be—in this, so we can identify cost drivers. Industry can then come back and say, 'Yes, we can' or 'No, we can't meet these things.' We then make decisions on cost capabilities, trade-offs and so forth. So it is a fairly lengthy process.

Ms GRIERSON—So that one section, on the pointy thing that flies very fast: is that what the minister is going to look at?

Lt Gen. Hurley—The government will get a cabinet submission that sums up the strategic justification, the options that we want them to consider and the risks attendant on each of those. He does an assessment of each of those options for the government up-front. We get 10 pages to write that. Then we will have a number of attachments and included in those attachments is a business case for each option. Even if it is not our recommended option, it has to be provided with a business case because government may prefer to go in another direction.

CHAIR—I like the fact that all different players have to sign off on their particular area of expertise so you can trace it all the way back.

Senator MARK BISHOP—Is this the appropriate place to be asking questions about the productivity improvement program and Ms Marks, or is that for later on?

CHAIR—We are looking at defence capability at the moment so probably not; maybe later on.

Senator MARK BISHOP—When would it be appropriate to raise those matters? I asked some questions and I have not received answers as yet.

CHAIR—When did you do that?

Senator MARK BISHOP—In the last Senate session, on the accounts.

CHAIR—Apparently there are other hearings coming up where those things will be discussed. You can pursue the questions on notice.

Senator MARK BISHOP—Yes, I have pursued them on notice. I am waiting for a response. I have not had a response. I want to know when I am getting a response.

Dr Gumley—There is another week for those responses to be in. I checked this morning on where the questions on notice from your last hearing were; I think the hearing was 30 March. I think they are about a week away.

Senator MARK BISHOP—Have they gone to the minister's office yet?

Dr Gumley—No. They are still being prepared.

Senator MARK BISHOP—Thank you.

Miss JACKIE KELLY—I know you are probably going to say that Air 87 was before my time, but can you go through the Air 87 project since 2003 and your involvement or rescue thereof?

Lt Gen. Hurley—Air 87 was an approved project when I came back into the job. Because it is an approved project, it is primarily run now by DMO because it is in the acquisition phase. But my involvement is that I sit in oversight of that with Dr Gumley, Chief of Army and so forth.

Miss JACKIE KELLY—Is it specifically the training up of the personnel to reach a capability on that project?

Lt Gen. Hurley—Again, I am in an oversight position, but I do not deliver that training. It is the Chief of Army's responsibility to deliver that in conjunction with the provision of equipment that DMO provides: simulators and so forth.

Miss JACKIE KELLY—But also the level of training required for people for daytime and night-time ops?

Lt Gen. Hurley—Again, it is the Chief of Army's responsibility to train the force to deliver that part of their capability.

Miss JACKIE KELLY—One of the contract failures was in terms of its ability to deliver on time. Our capability, by the time we actually got the aircraft, was that—

Lt Gen. Hurley—We want to be responsible and accountable. My responsibility is to define the requirement to fly the aircraft by day or by night and to seek to have that included in the options that we go forward with and get industry's response to what they can deliver against that. When we have contracted with the preferred tenderer, they are required to deliver that. DMO holds them—

Miss JACKIE KELLY—So you had nothing to do with Air 87?

Lt Gen. Hurley—No, I am not saying that. I am saying that I delivered my part of the process and now I oversight the implementation, but I am not responsible for the implementation.

Miss JACKIE KELLY—Okay. Can you run me through your part of the process of Air 87 in particular?

Lt Gen. Hurley—Now?

Miss JACKIE KELLY—From 2003.

Lt Gen. Hurley—I have been involved in the senior leadership oversight of the delivery of that project against the contract in terms of adding wisdom, I suppose, to the process. Is it delivering what we want? Are there other ways of doing it to help DMO and Chief of Army try to deliver the capability? For a number of our approved projects, for which I am no longer

responsible in terms of delivery but I have a monitoring role to ensure they are delivering the capability against the requirement, I sit in to assist with that. If it starts to deviate sufficiently, I ask: is there anything I should be doing to try to address that?

Miss JACKIE KELLY—Can you take me through the Super Hornets?

Lt Gen. Hurley—In what sense?

Miss JACKIE KELLY—Your involvement with that.

Lt Gen. Hurley—Yes. We helped prepare the new policy proposal for government to make the decision.

Miss JACKIE KELLY—That went through first pass and second pass?

Lt Gen. Hurley—I will give you the journey. In November 2006 we provided government, as part of the NACC—New Air Combat Capability—with a first-pass proposal for that. We provided a number of documents to government. We provided the first-pass documentation—the business case for first pass. We provided government with a paper that took them through the transition from the current fleets, F18 and F111 to JSF, and the attendant capabilities which support that—where we were with AEW&C and all those other capabilities. Included in that was an initial business case for Super Hornets if government decided that the risk to the air combat capability transition was such that it did not want to take on that risk. Government then directed us to go away and firm up those costing analyses and so forth—the capability analysis in the business case—and come back in March, which we did. They made a decision to acquire the Super Hornet.

Miss JACKIE KELLY—In your assessment of that, given what you now know about Air 87 and that you were not responsible in terms of training and manpower for full operations—daytime and night-time conditions—did you put that into the Super Hornet equation?

Lt Gen. Hurley—In terms of what?

Miss JACKIE KELLY—The manpower required to fly a two-seater.

Lt Gen. Hurley—Yes, and that was accounted for. The Air Force runs an organisation called the Air Combat Transition Office. They are responsible for planning the transition from legacy fleets to new fleets.

Miss JACKIE KELLY—Are you confident that there will be no training shortages and we are going to get that capability?

Lt Gen. Hurley—There are no absolutes in this game, but we will transition out of the F111 and F18 through Super Hornet and the JSF with sufficiently trained crews. That is why there is a step process. There is always a squadron coming in and out of service as we do that transition process.

Miss JACKIE KELLY—You were not losing a lot of people out of the F111s who saw no future when you moved to the JSF, but when you pop in the Super Hornets—

Lt Gen. Hurley—I cannot answer that at the moment.

Miss JACKIE KELLY—Have you examined the manpower?

Lt Gen. Hurley—I do not have that fidelity of view of what Air Force's manning is.

Miss JACKIE KELLY—You can cost a project down to its through-life costs and manpower and training requirements, but you have no idea of how many people were required?

Lt Gen. Hurley—No, I did not say that. I do not know the fidelity of who is deciding to go and who is deciding to stay, based on the nature of the aircraft we have purchased. My job is to ask: what force do you need to sustain that over time—pilots, ground crew, training staff and whatever—and what is the cost of doing that compared to the cost of the current capability? Then I go and speak to the capability manager in terms of Air Force and say, 'Okay, your job is to meet that. Can you meet that?' If they come back and give me the data that says yes, they can meet that transition, and we win that extra cost—if there is a difference—from government, then we can proceed down that route. I am not responsible for saying pilot X will go from F111 to F18 or to JSF.

CHAIR—In your final consideration or submission would you take into account the feedback from the Air Force about the cost in that transition process?

Lt Gen. Hurley—Yes.

CHAIR—They might say: '10 of the existing pilots are going remain. We're going to have to get another five. It is going to cost us X dollars to train those guys up.' That is all taken into account?

Lt Gen. Hurley—Yes. We have a thing called NPOC, the net personnel operating costs. What is the net personnel operating cost difference between current capability and future capability? What is the cost of transition to there? All those costs are assessed and included in that submission.

Dr Gumley—When the government approve a project, they will approve: an amount of money to buy the platform; an amount of money to buy the weapons; an amount of money that might relate to basing, hangars or whatever the infrastructure is on the ground; and an amount of money for this NPOC, which talks about the extra maintainers you might need for a project, the extra pilots needed or whatever other skill codes are required. The 'N' for 'net' means you might be deducting off a platform that is about to retire. Occasionally NPOC can be negative, because you might be replacing something which uses fewer resources than the thing you are replacing it with. That is all part of the government approval process when it goes to NSC.

Lt Gen. Hurley—Recommendation 2 is that we are to provide a cost assessment based on prime and whole-of-life costs for the capability.

Miss JACKIE KELLY—It has been articulated at this committee as ‘scope creep’, getting back to Air 87—that the problems there were due to scope creep. What is something you can put in place to have that not happen on air warfare destroyers, the Super Hornets or the JSF?

Lt Gen. Hurley—If there is scope creep, it is because the governance arrangements are not working effectively.

Miss JACKIE KELLY—It is not our fault; it is your fault.

Lt Gen. Hurley—‘Governance’, not ‘government’—internal governance. In relation to each approved project, there is a project management steering group, normally at the one-star level, that oversees the project. I have a representative in that project management steering group and they meet on a reasonably regular basis, again depending on the nature of the project.

Dr Gumley—I think there is an important difference that the Kinnaird process has made here. I mentioned earlier that the scope creep was one of the problems with the earlier processes, because the entire project was wrapped up in itself. If someone had a good idea, it might suddenly find its way into scope creep. Now we have introduced this gap between the capability group and ourselves. It is like we have a quasi contract with CDE. If General Hurley’s people want to change the scope of a project—say they are being pressured by Chief of Navy, Chief of Army or somebody—then it has to be done through a formal documented process rather than creep. Now it is a block change rather than a creeping type of thing. That discipline will put us in good stead for the future. However, it would be wrong to think that scope creep or scope change is entirely unavoidable. We are getting some platforms that take 10 years to build. When the mean life of computers is perhaps two years between microprocessor upgrades and so on, you can have obsolete systems by the time you finish a project if you do not have some scope upgrades as you work your way through. Some scope change is inevitable—what I call the technological change. The one where people just want more may or may not be valid, but it should be thoroughly documented with a decent process so you know why you are doing it.

Ms GRIERSON—So is it?

Lt Gen. Hurley—Yes. I will go through the mechanics I was going to talk about. We have a project management steering group process by which they review any requirements to change the current scope of the capability. They will be given some yardsticks. You cannot say to a project manager, ‘To spend an extra \$500,000 you must go and get 16 signatures.’ He has to have some freedom to make some trade-offs in capability and cost. But again, depending on the nature of the complexity of the cost of the project and so forth, the PMSG is authorised to make some changes and then they can come back up through the senior levels in the department to authorise the changes. But what we do not want is people saying, ‘It would be a great idea if we added another step or seat to that and that will cost you.’

Ms GRIERSON—Does it finally go to you or to another level?

Lt Gen. Hurley—It could go up to the two-star level or it could go up to me, depending on the complexity of the issue or the nature of the project.

CHAIR—Just on that aspect of going through the process, are you happy that the new process you put in to deal with scope creep, whilst I understand that it is not totally unavoidable, is resolving a lot of those problems? Is it working?

Dr Gumley—I do not think it is perfect yet. We started putting in these processes a couple of years ago. As General Hurley says, there has been a tension between us in giving project management the authority to run the project in a commercially efficient way and not having to get 500 signatures on a little tiny change verses having a major change. There is a little bit of tension in that boundary at the moment. As we are getting more experienced with that, we are getting better and better at it.

CHAIR—Are your suppliers getting better and better as well at adjusting to the new process?

Dr Gumley—Our suppliers can do work only if there is a contract change proposal which is documented. Occasionally the supplier will come up with a good idea and initiate a contract change proposal. If it involves a change in capability, we take it through to the capability group and ask, ‘Is this a good idea or not?’ Quite often it is the suppliers who have more knowledge of the platforms than we do. You would expect that. You would expect Boeing to know a lot more about Super Hornets than we do, so you would hope to tap their expertise.

Senator HOGG—What is a tiny change? I was a little puzzled by what is a tiny change and what is a major change. What triggers it off? Some things that may be deemed tiny in the initial circumstance may well not be. I think it is important that we understand it.

Lt Gen. Hurley—The issue is recognising whether a change is a cost driver. You might make a change to a platform, such as changing the way a stretcher is fitted into a helicopter. That is a fairly stock standard thing. But if someone comes in and says, ‘We need to put a different switch here in the system to allow the pilot to do that’, you know that, as soon as you bite into system and go into the integration problems, you will have to have a cost driver that flows through that. It is examining, understanding and thinking through the implications of those change requests that determine whether we go ahead with it. Is the technical risk of taking that on higher than we want it to be? If there a cost risk that we do not understand, we will work that through further.

Miss JACKIE KELLY—How many annual reports have you made on the defence capability update process?

Lt Gen. Hurley—We have done three since I have been in the job.

Miss JACKIE KELLY—Can you take me through how the Super Hornets got slotted in between the F111s and the Joint Strike Fighters? Obviously you were scoping your capability, saying, ‘Here are the F111s; things change in the air force and they have to go out a bit earlier’, you looked around and no doubt talked with industry about the various options for replacement aircraft and came up with a description of the capability required. The government then chose the Joint Strike Fighter. Take me through the rest of that.

Lt Gen. Hurley—In 2002 the government decided that they would join the SOD program for JSF. In doing so, they said that they would halt the Air 6000 tender process because if they were going to make that investment they wanted to continue down that line.

Senator MARK BISHOP—And Air 6000 is the JSF?

Lt Gen. Hurley—No. Air 6000 is the next air combat capability project. JSF is a solution to that.

Senator MARK BISHOP—Got you.

Lt Gen. Hurley—As the department started looking at what the transition would be between F18, F111 and JSF, it looked at the time frame of continuing investment and return investment on the current fleet, the capability of the current fleet, the risk you are accepting as you take it forward, where you can legitimately take it out to, how to transition from two aeroplanes to one while maintaining a level of capability acceptable to government to do air combat capability and all the tasks that they want us to do, and how you bring the next aircraft in. People go on about an air combat capability gap. I doubt whether anyone can actually define it. It is a very emotive term. We looked at that process and our assessment to the government was, ‘We can take that journey through these two fleets to JSF with an acceptable level of capability being provided.’ Government’s view on that was, ‘You have that view, but we have another view of what the risk is. Is there another way of solving that problem?’ We said, ‘Yes, there is. You could bring in a bridging aircraft.’ We were asked, ‘What would those aircraft be?’ We said, ‘You have a couple of choices.’ They asked, ‘Which is the preferred one? We will go down that way.’ The government made that decision essentially because they had a different view of the risk than we did.

Miss JACKIE KELLY—But you said that all major cabinet acquisitions are required to go through the first and second pass approval process. Do all of them have to go through that process or can you do a one off?

Lt Gen. Hurley—The process is there to guide government. Many of my projects go through more than two passes, and some of them go through a combined first and second pass process, depending on the knowledge of the capability, whether the solution is military off-the-shelf and what the risk is that we are taking on in bringing it in. We are not straitjacketed; there is some flexibility.

Senator MARK BISHOP—In the final analysis, the government can choose to substitute its own decision and avoid the two-phase process if it so chooses?

Lt Gen. Hurley—It could, but if you go to the C17 process that we went through and this process, we were dealing with known quantities and military off-the-shelf capabilities, in production and in service, and understanding what the burden of proof was under the Kinnaird process. We can look at that and say, ‘We can provide you with the level of confidence and assurance that you need to move forward on that project if you want to make that decision now.’

Dr Gumley—I will just take that a bit further, Senator Bishop. In the first two second-pass processes, one of the Kinnaird recommendations was that we spend up to, say, 10 per cent of the project funds derisking the project between first and second pass. That is a very sensible thing to do because you understand your risks and you get a better project at the end. When you are buying off the end of a production line with the C17 or the Super Hornet, the Americans have effectively done all that for you. They have had their own first pass years ago. They have a fully

operational production line. The supply chain risk is low. So a lot of the work you would have done in the Kinnaird process has already been done for you by the other government. You reach a second-pass decision with probably even less risk than you would with the traditional process.

Miss JACKIE KELLY—At that stage though, you are talking about the technical capability of various platforms rather than Australia's defence capability and going through the process to get to the Joint Strike Fighter. There is \$6.6 billion. Why would the Navy not need that or, given what we are doing in peacekeeping, why not put that into a Hercules fleet or some other project?

Lt Gen. Hurley—If you go back to the white paper you will see that it was quite clear in stating that the primary defence requirement is to maintain air superiority in our region. Air combat capability is the highest priority capability for the ADF.

Miss JACKIE KELLY—You have this Joint Strike Fighter, though. So you come out from a situation where you can transition—

Lt Gen. Hurley—No. Air combat capability is the key requirement. Up until that decision was made by government, the department's point of view was that the transition to JSF could be managed with an acceptable level of risk. The government took a different view and required us to look at a different option to get there.

Senator MARK BISHOP—When they substituted their decision on the acceptable level of risk and how that was to be handled in the transition, that is when the entire process kicked into the sorts of things Dr Gumley was talking about—for example, buying at the end of the production line. Is that the key here?

Lt Gen. Hurley—We have always kept an eye on what other aircraft projects are doing. DSTO has the modelling capability to take that in and keep us abreast of the capabilities of different aircraft that we might be interested in. We are not going to waste our money by spending it on other things.

Senator MARK BISHOP—I accept all that. But you are generally aware of what is going on in the world at a whole range of levels.

Dr Gumley—The Super Hornets did not just appear from nowhere. We have been constantly looking at Super Hornets and other versions of aircraft since 1998-99—in other words, ever since NACC was a project. You might notice that it is called NACC; it is not called JSF. It has always been what is going to replace the classic Hornets and the F111s.

Senator MARK BISHOP—And the key decision came when government, in its wisdom, chose to substitute its decision on the significance of the air capability gap and the risk attendant to it from the recommendation made by the department.

Dr Gumley—Correct.

Senator MARK BISHOP—That is the kernel of this discussion, isn't it? I make no comment on the merit or otherwise of your position or theirs. Once they made a different decision, you then argue that the rest of this follows logically.

Lt Gen. Hurley—Yes.

Miss JACKIE KELLY—Industry has made a complaint that they do not get to talk to you before the description of the requirement.

Lt Gen. Hurley—I think that is a lot of nonsense. I would put my hands up now and say that if industry is telling you that they do not engage with us before we come to capability approval—

Miss JACKIE KELLY—Before they see the tender document.

Lt Gen. Hurley—Frankly, I would say that that is rubbish.

Dr Gumley—So what do their 500 football teams of marketing staff actually do then, if they are not engaging us?

Miss JACKIE KELLY—They are just telling you what they have got, but when they find out what you want—

Lt Gen. Hurley—The industry associations have helped us prepare functional performance specifications and the RFT. Dr Gumley and I are involved with the CEOs of industry in an organisation called the Capability Development Advisory Forum, where we lay out all that we are doing with the DCP and where we are going on issues. They engage with us on options, they engage with us in their marketing process and they come and talk to my people. I have industry in my organisation every day of the week.

Senator MARK BISHOP—Why did government change the decision, General Hurley?

Lt Gen. Hurley—Change which decision?

Senator MARK BISHOP—The recommendation came from Defence to go down a particular path in plugging the air capability gap leading up to the purchase of the JSFs. So the recommendation came from Defence. The government, in its wisdom, chose to plug the gap by purchase of the Super Hornets. A whole range of consequences flowed from that. Why did government choose to substitute its view for the recommendation that came from Defence?

Ms GRIERSON—Can I add to that? Does that mean you can—

CHAIR—People here do not speak for the government.

Senator MARK BISHOP—No, I understand that but I am asking—

Lt Gen. Hurley—All I can say is that we presented the information to the government, and the government in the National Security Committee had a different view of what they saw as the security needs of the nation.

Miss JACKIE KELLY—I think the delivery times of the Joint Striker slipped.

Ms GRIERSON—Different views are fine, and we understand that, but does it mean that both of your roles can be bypassed? Does it mean that the defence department, or someone else who has more clout than you do, gets the ear of government?

Lt Gen. Hurley—Bypassing meaning that the government could say, ‘We’ll just go and buy anything we want without having the department give any advice’?

Ms GRIERSON—No, bypassing in relation to prioritising or bypassing your recommendations.

Dr Gumley—We have a democratically elected government and they are the ones that make the decisions.

Miss JACKIE KELLY—They have ultimate decision making power.

Lt Gen. Hurley—Let’s go to the issue that was raised about industry’s involvement in the process.

CHAIR—We will move on. Senator Murray has been waiting patiently.

Senator Mark Bishop interjecting—

CHAIR—Senator Murray.

Senator MURRAY—I have the call. From a different direction, if I were to summarise the role of this committee I would say that it is our job and our interest to assess whether major defence projects are delivered on budget, on time and to specification. The agent we have for the independent appraisal of those three items is the Auditor-General. You would know that this committee has an interest in the British system of major project audit appraisal. Yesterday the chair referred to that in a rather good speech. The essence of the British system is that audit appraisal is an ongoing process as projects are developed and progressed. It is not a system of appraising a project once it is finished—once it is done and dusted. My question to you is: are your two organisations paying much attention to greater integration and better information flow to the Audit Office in the development and progress of your projects? That is a general question, but, specifically, do you think it is appropriate or useful if the Audit Office was invited to be there in an observer status to, for instance, your monthly updates to the defence advisory board, or other such information conveyance meetings?

Dr Gumley—I will start with the British system. I have talked with the British audit office about this and I have also expressed my views to this committee. It depends very much on how the Audit Office goes about its work as to whether it will add value. If we end up with a series of 30 or 40 performance audits every year, which typically take 2,000 hours of senior management time inside the DMO to handle, the place would stop. If we end up with a system where we cooperate and work with the Audit Office on a plan and we do it in a consultative way, the system could add a lot of value. The work at the moment is going on between DMO and the Audit Office about how to develop a work plan that is efficient and effective and gives the public the scrutiny that is desired but also does not become so intrusive that work stops.

Senator MURRAY—When will you be in a position to advise the committee about the conclusions you have come to with respect to that discussion?

Dr Gumley—The work is ongoing. I do not have an exact time with me. I can get you details as to when we expect to be moving forward on it.

Senator MURRAY—All right. Just go to the specific question that I put to you. Is it appropriate for the Audit Office to sit in with observer status, not participant status, in appropriate information conveyance meetings, such as to the defence advisory board?

Dr Gumley—I do not think so. I learned this lesson when I was working with Boeing about seven years ago. If you have a system where, every time you give bad information up the chain, and someone is going to take it and use it against you, then very quickly people stop giving you bad information; they report only good information. We need to have a system where there can be honesty up and down the management chain inside all of our organisations so that there is no fear in the system and people can actually show problems and then we can fix them. If you have external auditors over every single process in your organisation, I think everyone will become very politically correct and very guarded, and problems would get hidden for longer and longer. That is just human nature.

Senator MURRAY—Through the chair I make this request: I am not sure exactly when the report is going to come down, but before it comes down I think the committee would be assisted if you gave it an update on how far you have got with your discussions, consultations and decisions with the Audit Office with respect to their greater interaction with you. Otherwise we are left in the air about where you are and what the outcomes are in deciding on our position with respect to that matter.

Lt Gen. Hurley—I will make two comments. First of all, ANAO is not the only external organisation involved in our work. Since the introduction of the Kinnaird review our Department of Finance and Administration has established a defence review branch.

Senator MURRAY—You might recall that I said with respect to this committee. The ANAO is our agent.

Lt Gen. Hurley—Yes, but I was just saying there is another external agent at play that looks at the financial aspects and runs its finger over it. Secondly, I back up what Dr Gumley said about investment of time and what the measures of effectiveness are here. I do not want to denigrate the efforts of my counterparts in the United Kingdom, but that process has not necessarily improved their delivery of capability. They still have some projects of major concern.

Miss JACKIE KELLY—It certainly has short-circuited any 80-per-cent-paid-for, nothing-delivered issues. To me that seems to be getting picked up very early in the parliaments—

Lt Gen. Hurley—It has not, for example, circumvented laying up Royal Navy ships to pay for two aircraft carriers. We just need to be careful about what we are reading and interpreting on this.

Senator MURRAY—You are entitled to make whatever judgment your experience dictates, and we will respect that, but what we as a committee need to arrive at is a view as to whether your relationship with the Audit Office should change and the process should change. To arrive at that view, we will need to know how far you have got and whether you want to maintain the status quo or whether you see that there is a better way for that relationship. All I request is that before we report you give us an appropriate update.

CHAIR—Only this morning, prior to starting this hearing, we discussed the implicit criticisms in the Proust review regarding the perceived relationship between the defence department and the Audit Office, and I know that the auditor has a view about that. We certainly would like to hear your view, perhaps a substantiated view, about what that relationship is and how it can be improved.

Lt Gen. Hurley—Certainly.

Miss JACKIE KELLY—Obviously, we are interested mainly in the FFG and the Air 87. Again, that was all before your time. You have the ‘lessons learnt’ document. The primary lesson learnt in that document is that ‘shortfalls in early planning and resource allocation have disproportionate consequences’. Can you identify those shortfalls and what changes you have made to ensure that they do not occur again—and similarly for the Air 87?

Dr Gumley—Can I just confirm with the secretariat that you have the plain English version of that—remember that we talked about it? It appears that it has not yet been received.

CHAIR—It is the famous document that we never seem to have got.

Dr Gumley—A plain English version of that document is on its way to you. I think the lessons learnt are valuable. Basically they are saying you have to have enough staff capability up-front to do these projects. That is totally in accord with Kinnaird between pass 1 and pass 2. You need to put some of your very best people on your projects between pass 1 and 2 because that is when all the risks are being identified and retired. So that is absolutely true. If you go back to when that FFG project was put together in 1997 or 1998, you could probably argue that there were not enough good people on the project. This is one of our big challenges. A very substantial re-equipment of the ADF is coming up and we have to find enough people who have the domain knowledge and the commercial experience to be able to run all these projects. It is a challenge.

CHAIR—From where are you sourcing those people, Dr Gumley? Can you get them from Australia or do you have to go beyond?

Dr Gumley—One of the main areas of the up-skilling program is to train our own. We have been out to the market; we have seen what is there. It is a limited pool of qualified people. The industry, obviously, want exactly the same people. There are 7,000 people in DMO, but there are 26,000 people in the industry, and they need the same sorts of people.

Miss JACKIE KELLY—But don’t you think that, with a relationship like the UK has with its National Audit Office, a lot of those deficiencies, shortfalls or lack of resources in certain

areas would be identified earlier and, with the help of committees such as this one, highlighted? You would get the resources where they are required.

Dr Gumley—I think we are capable of identifying where we have shortfalls.

Miss JACKIE KELLY—Time will tell. I bet you that 10 years from now we will be here looking at a bunch of post-Kinnaird projects—major acquisition projects that can now finally be legitimately described as post-Kinnaird, finally.

Dr Gumley—If I could find another 2,000 qualified engineers and project managers, we could deploy them almost immediately.

Ms GRIERSON—So could every engineering firm.

Dr Gumley—So could every engineering firm—

Miss JACKIE KELLY—And mining company—

Dr Gumley—and mining company in the country.

Lt Gen. Hurley—The ANAO drawing our attention to that does not actually solve the problem.

CHAIR—We are coming close to the end of our hearing, but I know that there are a couple of brief questions left.

Lt Gen. Hurley—I would just like to offer the suggestion that one of the best things we could do to improve the relationship with the Audit Office would be if the audit reports that came out talked about solutions as well as just identified problems—in other words, to value-add. We are reasonably capable of identifying our own problems; where all of us could do with some more help is in identifying better solutions.

Miss JACKIE KELLY—But most of the ANAO recommendations are solutions in themselves. It is just that you disagree, hence—

Dr Gumley—I do not think that there are that many with which we disagree. There are a few—but not many. Most of the recommendations are accepted and implemented.

CHAIR—With these new audits that are to take place—30 audits under the new arrangements—do you have the resources to be able to fulfil that requirement from your end?

Dr Gumley—Not at the moment, no.

CHAIR—What do you need to achieve that? If you are going to have the Audit Office running around every corner on these 30 projects, tying up your staff, what implications does that have for the delivery of your own services?

Dr Gumley—I think it would substantially slow down capability delivered to the ADF.

CHAIR—What do you need? The 30 projects will not change; they will remain. What do you as a department need to fulfil that?

Dr Gumley—We need to negotiate with the Audit Office to come up with a system or a process so that the work gets done once and once only. If we prepare all the documents this way, they should be auditing the process. If they find there is something wrong, they can dive deep down into a particular project. But, if it is, ‘I want a list of 27 different documents and I will go through those line by line; that will generate a demand for me to look at another 1,000 documents line by line,’ the whole place will just stop. So we have to find a way whereby the Audit Office audits our processes rather than our transactions.

CHAIR—But, in saying that, the Audit Office has been allocated increased funds to achieve that objective of doing 30 audits. Are you therefore saying that, apart from the process issue between the Audit Office and you about how they go about their work, are you also requesting an increased allocation of funds to be able to meet that expectation?

Dr Gumley—We have not been allocated any extra funds to meet the audits.

CHAIR—Is that what you are after, though? Would you be after that?

Dr Gumley—I do not know what I am after until we determine with the Audit Office what the process looks like.

Miss JACKIE KELLY—The Audit Office are there to look at transactions—at specific transactions: ‘Why was that money paid over on that date when none of the requirements for that contract were met?’ That is a clear auditing responsibility. It is reported to government. ‘And we still have not found out who did it.’ Their responsibility is not to go into the process of how it has occurred; it is simply that the payment was made and it was not proper. Do you know what I mean? That is the function of an audit office, and that is the transparency to government. The trade-off is how transparent is it to the elected officials versus how fast Defence can do it.

Lt Gen. Hurley—There are two types of audits.

Dr Gumley—Yes, there are two types of audits. The relationship with the Audit Office on the financial audits, I think, is excellent at the moment. I am delighted with the co-operation on financial audits. They audit our processes and they do a bit of green-pen ticking of individual transactions to check that the processes are working. There is an open dialogue on financial audits. It is going well. We make some mistakes and they find them, and that is fine. We correct our mistakes and so on. On the performance audits, though, it is my view that they could be done a lot more efficiently and effectively, and a greater level of transparency could be given to the government and to the public if we went about them a different way.

CHAIR—Are you having a dialogue with Ian McPhee to resolve that?

Dr Gumley—I have talked to Ian McPhee about this several times and we are going to continue doing so.

CHAIR—Are you making progress?

Dr Gumley—Some progress is being made, but what is happening now is that a band 1 working group is getting together to work out how we do it.

CHAIR—Okay. Good.

Dr Gumley—I want to be clear: we are very accountable to the public. We know our obligations, but we do not want to meet them in a way where business is significantly affected and slowed down, because that does not help any of us.

CHAIR—No. We have to be very careful that that is not used simply as a barrier to further audits—which can be used by industry or other agencies.

Dr Gumley—Under the audit act, the Auditor has the rights to any document in the building at any time. If they feel that we are doing something wrong, they can just go and do an investigative audit in any area.

Ms GRIERSON—I want to go back to some of the things we discussed earlier. We have spent a lot of time in this inquiry looking at your processes and holding up your roles as a way to get improvements. We looked at all these failed outcomes, or outcomes that were unsatisfactory with cost overruns et cetera, or capability not delivered. We are committed to making sure that your processes are good ones, and we support them. We concede that government has the right to make its decisions taking into account other risks that are not your province—political risks and all other decisions. But, if your recommendations are bypassed in any decision making for major acquisitions, it has an implication that other people are bypassing you, either the defence department, service chiefs or industry, and influencing government decision making that way. I suppose that is part of the lobbying role, but is there a problem and where does it rest?

Lt Gen. Hurley—I do not think there is a problem of agents, a generic term, bypassing our capability development process to take approvals to the government.

Ms GRIERSON—But, if there were, you would want us to know about it.

Lt Gen. Hurley—Requests for approval for capability propositions of any form must come through a committee process in the department to get there. They cannot be lodged in the minister's office through any other means. They have to be considered by the Defence Capability and Investment Committee and signed off by the appropriate officers in the department to be considered to be lodged and go to the NSC. They are the rules. You cannot put a proposal in any other way. Other people might want to influence the passage of those decisions once they are lodged. Everyone knows that industry will call through these halls to see people and to put their point of view about what we are doing. That is not bypassing our decision. It is part and parcel of the business we are in; people want to put their positions. But the proposal that goes forward from us is the department's position, signed off, and it has gone through the appropriate governance arrangements in the department.

Ms GRIERSON—Do you agree, Dr Gumley?

Dr Gumley—Yes.

Ms GRIERSON—The only other question I have relates to the defence submission which referred to improved cost estimations through new systems development. Who does that apply to? Who is doing the new systems development for improved cost estimation? What is it?

Lt Gen. Hurley—When the group was formed in 2004 we did not have our own cost estimation cell or organisation within this particular group to help us do that. We drew on the resources of DMO and the chief finance officer. Since our foundation we have developed one of the branches I referred to, a cost analysis branch, which is developing all the databases, the international benchmarking, and is drawing on our relationships with allies and other partners. I have an exchange with the United States PA&E organisation to help us develop our techniques. I send a person there and they send a person to my organisation. We have developed certain tools to help us do a better predictive estimation. We have set out new frameworks for determining prime costs and whole-of-life costs that every project now must go through. There is a uniform process that people go through to get that assessed. An insight into that process is shared with the department of finance.

Ms GRIERSON—Is this duplication of DMO's cost estimation?

Lt Gen. Hurley—No. You have a cost estimation process that is building up the business case and then you have an independent analysis branch that goes in and says, 'I do not think you have asked the right questions,' or, 'These figures aren't right based on this historical trend,' and so forth. We try to have checks and balances to make sure that the estimate that goes to government has been scrubbed by someone who has no championship of the proposal. The department of finance sits outside that. There is an internal independent check and then there is an external independent check from the department of finance.

CHAIR—We will conclude the public hearing at this stage. Dr Gumley, I will just leave you with a thought—perhaps you can feed it back to us—based on Senator Murray's question. I appreciate that you are saying you really do not know what your resources are going to be until you know what the process requirements are in the relationship between you and the Audit Office over the 30 reviews they will do, but can you consider the additional resources that you may need? I do not think there will be a reduction in the number of audits that they will do. There may be improvements in the process and relationship, but there is also a resource issue that you want us to advocate as part of that process. We would certainly like to hear about that. You might not want to answer that question now; perhaps you can give it to us later.

Dr Gumley—We have not been funded to respond to any of these 30 performance audits.

CHAIR—I understand that. I understand that that is not counted. That is why I am saying that if you consider that a necessary requirement, I would like to hear about it. General Hurley, could you get back to us, put it on notice or give us information the next time you appear before us, which I think is the end of May, on your views about how the relationship between your office and the Audit Office can be improved?

Lt Gen. Hurley—Yes.

CHAIR—There are a couple of other questions that were put on notice by other members.

Dr Gumley—I want to go back to what is in *Hansard* from I think two or three meetings ago when this committee asked me what was my view about having the 30 top projects audited each year. I said that I thought it was a good idea if it added value and we would need to get the process right to make it happen. It is of concern to me today to hear that the language is now shifting to 30 performance audits. If that is where we are going, that is quite different from what was suggested to us two meetings ago.

Ms GRIERSON—In what way?

CHAIR—I cannot recall whether that was the performance audits, or was it just 30 audits?

Ms GRIERSON—Audits.

Dr Gumley—It is a review of the top 30 projects.

CHAIR—Let us be correct about that. That could very well be financial and performance or it could be a combination.

Dr Gumley—This is the process that we need to find out.

Ms GRIERSON—What you are telling us, Dr Gumley, is that there is no process for this initial phase to get this work done. You have a committee that will look at it; is that right?

Dr Gumley—We have a co-operative Audit Office. I am very pleased with the co-operation of the Audit Office. I do not want anyone to think that everyone is not talking. We are all talking, and now we have to come up with a process that can then be costed so that people understand what we are getting ourselves into.

Ms GRIERSON—We wanted that in this financial year as well so that when you start the process, it is ready to go. It seems to me that there is a lot of work to be done.

CHAIR—That was for the Audit Office.

Ms GRIERSON—He has no money for it either.

CHAIR—Let me clarify this. My understanding is that it is the top 30 capital projects. I am not fully aware of what that actually means.

Miss JACKIE KELLY—This committee kicked off because of the overpaid and can-you-not require types of things. It is just money-checking on the way through. I think that is what the ANAO is faced with.

Dr Gumley—Please let us understand the difference between the two. A performance audit usually gives you a book about that thick when it comes out. If we are going to develop 30 of them every year, that is an entirely different resource proposition than some process about the top 30 projects.

Ms GRIERSON—You would rather have the audits continue of your processes, your activities and your ongoing operations?

Dr Gumley—Yes, I am happy with that.

Ms GRIERSON—And yet have that targeted—

Miss JACKIE KELLY—I do not think it is generally random and they are generated after a media article or a recommendation or something, but if you know you are getting a performance audit on something every year, big deal.

Lt Gen. Hurley—We go through a process by which we determine which of the issues will work with the ANAO. With the coming year, it is a rolling program and we refine it through.

Resolved (on motion by **Ms Grierson**):

That this committee authorises publication, including publication on the parliamentary database, of the proof transcript of the evidence given before it at public hearing this day.

CHAIR—Dr Gumley and General Hurley, thank you very much for coming today and for giving evidence. Dr Gumley, I understand that you are not scheduled to appear before us again, but you do have a lot of questions on notice from Senator Bishop. Senator Bishop is waiting for those, and we are also waiting for the common language version of that document. General Hurley, we understand that you are coming back in two weeks time.

Lt Gen. Hurley—Could we have a conversation just to clarify a bit further what sorts of issues you might want to follow through? I know I will be appearing with the chief defence scientist.

Ms GRIERSON—It is more the technical rather than the scientific aspects of it.

Lt Gen. Hurley—How we work together on that sort of project?

Ms GRIERSON—Yes. That would be interesting for us.

CHAIR—If there is anything else we will get the secretariat to submit it to you. I declare this public hearing closed.

Committee adjourned at 12.47 pm