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Serving Australia Control and administration of the Department of Defence

by Mark Thomson

The Army is not like a limited liability company, to be reconstructed, remodelled, liquidated and refloated from week to week as the money market fluctuates. It is not an inanimate thing, like a house, to be pulled down or enlarged or structurally altered at the caprice of the tenant or owner.

It is a living thing. If it is bullied, it sulks; if it is unhappy, it pines; if it is harried, it gets feverish, if sufficiently disturbed it will wither and dwindle and almost die, and when it comes to this last, serious condition, it is only revived by lots of time and lots of money.

—Winston Churchill, 1905

Executive summary

After more than a decade on active service, the Australian Defence Force (ADF) is better prepared and more experienced than at any time since the Vietnam conflict. And after more than a decade of steadily growing budgets, the Department of Defence (Defence) is better funded than at any point over the same period. Yet, somehow, Defence continues to be a source of profound frustration to the government and an endless delight to journalists looking for headlines.

Consider what's happened this year, alone. In January, it was reported that the Navy could only put a single submarine to sea. In February, the entire ADF amphibious fleet went unexpectedly AWOL as Cyclone Yasi

approached the Queensland coast. The government revealed that \$40 million had been spent building six landing craft that weren't fit for service (and wouldn't fit in the vessels that were supposed to carry them), and the initial report into goings-on aboard HMAS Success described behaviour as 'out of control'. March was quiet.

In April, the Australian Defence Force Academy Skype sex scandal broke, leading to multiple reviews of ADF culture. In May, Defence handed back \$1.5 billion of funding that it couldn't spend as a result of widespread delays in acquisition projects and poor internal budgeting, and the \$8.5 billion air warfare destroyer project encountered major problems in basic module fabrication, forcing a twelve-month delay. If all that weren't enough, it finally became clear in May that the schedule for modernising the ADF laid out in the 2009 Defence White Paper had fallen so far behind as to be implausible.

It's clear that something's badly amiss. Over the past decade, Defence has advised successive governments to boost defence spending to prepare for uncertain times ahead, and successive governments have agreed and dug deep into taxpayers' pockets for the wherewithal. But while some progress has been made, there remain serious problems with the delivery of today's defence force and there's been decidedly lacklustre progress in building

tomorrow's. If Australia's defence matters at all, if armed force has any role in protecting our interests in the 21st century, the present situation is beyond intolerable.

So, what should be done? This report attempts to answer that question through an exploration of the control and administration of Defence. A lot of what's covered is explanatory—any prescription for what ails Defence needs to appreciate how it works, or doesn't. But Defence is a sprawling and complex organisation that operates under unique constitutional and legislative arrangements, and there isn't much that can be readily summarised in this regard. Those readers interested in a background understanding of the issues will need to read the rest of the report. For others who are pressed for time, below are four key recommendations.

Devolve authority and accountability

Like a giant exercise in central planning, Defence employs matrix management on a grand scale. Goods and services flow from one part of the organisation to another according to plans conceived in Canberra. The chiefs of the three services directly control only a fraction of the resources that go into the military capabilities they're nominally in charge of. The result is manifest inefficiency and clouded accountability. The services have few incentives to moderate their demands, and the divided control of activities means that nobody's accountable for final outcomes.

No better example exists than the collapse of the ADF's amphibious capability earlier this year. In a two-page explanation of the unexpected demise of the fleet provided by Defence (and subsequently released to the public by the government), no person or entity within Defence was identified as being responsible. To be clear: a critical capability costing the taxpayer hundreds of millions of

dollars a year fails without warning and we're told that it's nobody's fault. The worst part is that accountability is so amorphous within Defence that it's a plausible claim.

The command economy model of Defence administration has failed. Authority and accountability for the delivery of Defence capability should be devolved to the chiefs of Navy, Army and Air Force. Where there's no strong argument for pooled delivery (as there is, for example, with IT services), the activities should be returned to the services outright. In those areas where economies of scale or specialist expertise are relevant, a more businesslike relationship needs to be developed to enable the services to control, and be accountable for, the resources they consume.

Strengthen central strategic control

To be effective, the devolution of authority and accountability to the three services needs to be accompanied by stronger central strategic control. By any measure, Defence lacks a governance infrastructure commensurate with its size and complexity. At present, Defence administration is not so much exercised as it is an emergent property of processes and committees.

Two steps should be taken. First, the current sixteen-member Defence Committee should be replaced (not augmented) by a smaller body that brings together real expertise rather than representatives of organisational fiefdoms. Second, a headquarters needs to be created, bringing together all the planning and reporting activities currently spread across the organisation. The headquarters would report to the Secretary of the Department of Defence and the Chief of the Defence Force (CDF) and be run on a day-to-day basis by a Chief of Staff or Chief Administrative Officer.

With a headquarters in place, the Secretary and CDF could then impose a regime of performance management and accountability

over the organisation. The services would be given budgets and performance targets to meet, principally focused on preparedness.

At the same time, there's an urgent need to remediate Defence's financial and management information systems. Recent events have revealed that Defence has an unacceptably poor understanding of its costs and non-operational business.

Re-establish internal contestability

The underlying rationale for joint civilian–military administration of Defence has been lost. While it's appropriate for military and civilian personnel in Defence to work together cooperatively in most instances, some level of creative tension is needed as a counter to military self-interest. If this is not the case, the role of Secretary can be done away with and the military can be left to run the show.

Three things need to happen. First, independent civilian analysis of force structure plans and individual capability proposals should be reintroduced. No plan or proposal should go to government without having been robustly contested and 'red teamed' within Defence. Second, an independent microeconomic analysis unit needs to be established within the new headquarters under a Chief Defence Economist. Its job would be to record, measure and benchmark the efficiency of ongoing Defence activities. Third, a greater effort needs to be put into the professional development of and succession planning for civilian officers—at least commensurate with that for military personnel at similar levels. The goal should be to ensure that senior civilian positions in Defence are filled by people with a strong understanding of the complexities of defence policy and the defence force. The ongoing tendency to appoint departmental secretaries from outside shows how poorly civilian talent is nurtured and developed within Defence at present.

Increase transparency and strengthen external scrutiny

No matter how robust contestability becomes inside Defence, there'll always be a need for external scrutiny. To conclude otherwise would be to ignore the ideas that our system of government is built on.

On the whole, the effectiveness of external scrutiny is limited mainly by the availability of information rather than by the number or size of the actors involved. For a country our size, we don't need any more defence think tanks or better funding for academic research on defence. Instead, we need reliable information about Defence's costs, performance and activities. Make that available and all the rest will follow. By allowing unnecessary secrecy about Defence, the government robs itself of the benefits of independent analysis, and leaves itself captive to acting on what Defence chooses to reveal to it.

Driving reform

These four recommendations would be difficult for any government to drive through. Many of the changes would see power within the organisation shift significantly, resulting in bureaucratic winners and losers, and tighter checks would be placed on the ability of the military to set its own agenda. Perhaps most difficult for the government, greater openness would almost certainly result in greater embarrassment—at least in the short term.

But if the government is serious about Australia's defence it needs to take decisive action. Critical capabilities like the Collins class submarine and amphibious fleet have become fodder for cartoonists. Acquisition projects worth billions of dollars are running years behind schedule, and the much-lauded plans to build Force 2030 announced in the 2009 Defence White Paper look more fanciful by the day. The time to act has come to shake off complacency and enact fundamental reform to the way Defence is managed.

1 Violence and the state

The march of human civilisation has been accompanied by a diminishing licence for violence. Already in the fifth century BC, the Greek historian Thucydides extolled the progress of Greek civilisation by recalling that the ‘whole of Hellas used once to carry arms, their habitations being unprotected and their communication with each other unsafe.’ By allowing the citizens of Greece to lay down their swords, the ancient Hellenic states enabled the blossoming of art, science and philosophy that underpins our own civilisation.

But limiting the franchise for violence did not eliminate violence entirely—as the Peloponnesian Wars (the subject of Thucydides’ writing) showed. Instead, the continuous anarchy of the pre-civilised world was exchanged for periodic wars between states.

More than two thousand years later, it’s surprising how little has changed. While civilisation has been extended to most corners of the globe, war between states remains a credible possibility. Neither the signing of the United Nations Charter in 1945, nor the advent of nuclear weapons in that same year, has rendered war unthinkable. And while there has been some progress—there hasn’t been a war between major powers in more than 60 years and conflict around the world has been in decline since 1992—global military spending still accounts for 2.7% of all that humankind produces today.

It’s worth dwelling on how extraordinary this is. While violence is tightly proscribed within states, violence between states remains *de rigueur*. Military force is hardly viewed as even a necessary evil. To the contrary, the profession of arms is revered in many societies—including our own. But irrespective of how accustomed we are to

having armed forces in our midst, there are important differences between civil society and the military.

No other part of the state exists to purposefully kill, wound and destroy property, no other part of the state demands higher potential sacrifices from its members, and no other part of the state can plausibly lay claim to such highly exclusive expertise. The last point bears explanation. While many areas of public policy are highly complicated, pertinent expertise is usually available from a variety of sources. In contrast, deep knowledge of military affairs is rare outside of armed forces. As a result, armed forces have close to a monopoly on advising their governments about military matters. What’s more, modern armed force is a highly complex large-scale enterprise demanding the organisation of diverse and specialised inputs. These characteristics generate special problems for governments, and societies more generally, in the practical administration of their armed forces. This paper explores those problems with a focus on Australia.

Civil–military affairs

The first problem is that of control. It’s been a long time since direct military command was routinely coincident with civil government. The last person in the English-speaking world to simultaneously govern and directly command a foreign military campaign was Henry VIII in the 16th century. Even the highly authoritarian fascist and communist regimes of the last century maintained a clear distinction between civil government and the military. Thus, apart from those countries currently suffering under the ignominy of military rule (Burma, Fiji and Mauritania), governments of all ideological complexions face the problem of controlling their armed forces.

In some places, such as Pakistan and Thailand, civil rule literally occurs at the sufferance of the military. In many others, the military is too weak and civil society too strong for legitimate government to be usurped for more than a very limited interlude. As a result, most attempted *coups d'état* either fail or are short-lived.

In Australia, as in other mature democracies, the likelihood of the military coercing or usurping the elected government is vanishingly small in all but the most exceptional of circumstances. Not only is the very notion abhorrent to the values and ethos of Australia's military, but it's likely that strong societal and institutional resistance would rapidly render any such attempt futile.

Yet, even without the spectre of combat boots tramping mud into the Lodge, important questions remain about the relationship between the military and the civil government. They include:

- to what extent should the military be treated as an independent institution?
- how should the government deal with 'professional military advice'?
- when, if ever, should the government interfere in the conduct of military operations?
- what practical arrangements are needed for the government to exercise effective control over the military?

These and related questions are explored in Chapter 2.

The challenge of Defence administration

History shows that a country's defence depends on many things; alliances, strategy, tactics, diplomacy, morale, leadership and plain luck all play a part. Somewhat

less exciting, but no less important, is the day-to-day management of the wherewithal to conduct military operations. In Australia, that's the work of the Department of Defence.

The scale of the enterprise needs to be appreciated. Defence is one of Australia's largest employers, with a workforce of over 100,000 personnel. It has a presence in every state and territory, including 700 leased or owned properties, 25,000 built assets and 3 million hectares of land. Defence operates fleets of advanced aircraft, ships, submarines and fighting vehicles, as well as multiple intelligence, surveillance and command and control systems. The total value of Defence's assets and inventory amounts to \$73 billion, and its annual budget of \$26.5 billion is equivalent to around 1.8% of our gross domestic product.

While many would be aghast at the suggestion that Defence is a business, it has many of the characteristics of any large corporation. At the very least, a number of identical activities occur in each, including budgeting, reporting, procurement, research and development, public affairs and people management. Defence shares two other important characteristics with a corporation: they both seek to shape their environment through marketing and lobbying, and they both face the temptation to subvert the interests of shareholders (and the community more generally) in favour of their own institutional interests.

But the similarities go further. Corporations deliver goods and services to customers in order to generate value for shareholders. Defence delivers services to the government, which acts as both customer and shareholder. The essential point is that both are in the business of *production*. They each take human, financial and physical inputs and transform them into products. Defence produces five products or outputs:

- military operations
- preparedness for military operations
- defence diplomacy
- intelligence
- advice to government.

Everything that Defence does—from the training of new recruits to the conduct of exercises with foreign forces—is ultimately directed towards one of those five goals.

Every year, Defence also invests substantial amounts in military equipment and facilities. While strictly speaking those investments count towards the delivery of future preparedness, in practice they represent a largely separate activity.

At some point, however, the analogy with a corporation breaks down—not just because of the particularity of Defence’s products and the absence of a profit motive, but because Defence is more diverse than any private or public entity in the country and its component parts are more interdependent. Far from being a network of similar parts—such as the Woolworths and Coles retail chains—the constituent parts of Defence are vastly dissimilar. And, unlike a diverse corporation such as BHP Billiton whose petroleum, aluminium, iron ore and other divisions are quasi-independent businesses, military operations demand the close orchestration of every arm of the defence force and its supporting elements. For military success, the whole must be greater than the sum of the parts.

It follows that the administration of Defence is at least as complex as that of any public or private entity in Australia except the government itself. Chapter 3 examines this challenge. To keep the scope of the discussion manageable, the command and conduct of military operations is excluded, as are the many important issues in the management of military personnel. Each of those areas

deserves an extended paper of its own. But even with these exclusions, there’s still a wealth of material to cover; the effective and efficient administration of Defence depends on the interaction of a number of factors, including organisational structure, infrastructure, governance, accountability and processes.

Oversight and scrutiny

Most Australians have an immediate grasp of the effectiveness, if not the efficiency, of government services such as education and health, either through direct experience or by knowing someone with direct experience. Few people are more than one or two degrees of separation from a recent interaction with a teacher or doctor. As a result, the public debate on those government services is extensive and largely well informed. There is unbroken feedback between consumers and the state and federal governments responsible for service delivery. And for those interested in the efficiency of service delivery, the Productivity Commission produces an annual comparative benchmarking of costs and performance running to 1,756 pages.

Other areas of government activity are more tenuously linked to their ultimate customers in the electorate—especially those that deliver public as opposed to private goods. Defence falls into that category. Most Australians aren’t in a position to judge the efficacy of our defence efforts first hand. Instead, they have to rely on what they’re told by the media. The media, in turn, rely on a range of sources of varying reliability, all of which are hampered by the veil of secrecy that surrounds almost every aspect of what Defence does. Apart from operational matters—which have been subject to increasing openness in recent years—the gap between what’s kept secret and what can plausibly be kept secret on the basis of

national security and commercial confidence is yawning.

The result is that Defence is a source of endless surprises. Problems fester undisclosed for extended periods until an audit report or leak propels them into the newspapers. In the meantime, apparently persuaded that bad news improves with time, media officers issue an endless stream of upbeat yet anodyne press releases to assure us that all's well on Russell Hill.

By unnecessarily limiting disclosure of Defence's performance, the government does itself a great disservice. The breadth and complexity of the organisation are such that no minister, irrespective of the extent of his or her experience and skills, can hope to be across the details of the leviathan they're responsible for. Nor can or should they rely exclusively on the advice they receive from the department. More so than probably any other national department, Defence has a vested interest in the issues on which it provides advice. Indeed, most of the advice that Defence provides is about itself. Moral hazards abound. It's only by exposing Defence to external scrutiny that the government can hope to generate the informed public debate necessary for it to reach objective decisions on defence issues.

Chapter 4 explores the administration of Defence in the context of society as a whole, including the roles played by the media, the parliament, the audit office and public commentators in scrutinising Defence.

Reforming Defence

Defence has undergone many reforms over the past half-century. There's nothing unique about that: it's true of every other area of government activity at the state and federal levels. Just as in the business world, public institutions have to adapt to new circumstances and evolving expectations.

Broadly speaking, the changes have been overwhelmingly for the better. With few exceptions, the public and private sectors are now more effective (they provide better products and services than in the past) and more efficient (they produce their products and services more cheaply than would have been possible in the past).

Defence reform can be usefully divided into initiatives to boost either effectiveness or efficiency. On both fronts, Australia has moved in tandem or soon after the US and the United Kingdom.

The reforms came in two waves. The first wave, in the 1960s and 1970s, focused on improving the effectiveness of national defence through greater coordination of the separate arms of the defence force. In the US, Robert McNamara (Defense Secretary, 1961–1968) extended control over the single services by centralising planning and budgeting within his office. In the United Kingdom, the single services were absorbed into the Ministry of Defence in 1964. In Australia, it took until 1973 for a unified Department of Defence to come into being under a package of reforms designed by Sir Arthur Tange (Secretary of the Department of Defence, 1970–1979).

In each case, two factors were behind centralisation. The first was the need to establish stronger control over the military. As Tange put it, the first objective of the reforms was to create 'an organisation that will place control in the hands of responsible government'. Second, and just as important, it was recognised that the overall defence effort could be improved by 'strengthen[ing] central control of military operations and of resources allocated to defence activities'. This meant not just curtailing single-service aspirations in favour of national priorities, but also ensuring that the three arms of the ADF could support each other in joint operations.

The second wave of defence reform aimed to improve efficiency by reducing costs. Beginning in the 1980s as part of the ‘new public management’ reform of the public sector, defence organisations in many countries were required to become more businesslike. Some of the reforms—such as the introduction of accrual accounting—were largely cosmetic. Others were more substantive, like the privatisation of defence production and the outsourcing of support activities.

Among Australia’s allies, the United Kingdom showed the way by introducing a competitive approach to its procurement and support services in 1983. Since that time, all the means of British defence production and a large share of defence support have been transferred to the private sector. While most US defence production has always been in private hands, it was only in the early 1990s (following the call for a peace dividend after the end of the Cold War) that the US got serious about outsourcing support. With typical American vigour, the program has grown to include operational support by contractors, as seen in Iraq and Afghanistan today. Here in Australia, government-owned defence factories and shipyards were sold off in the 1990s concurrent with the outsourcing of a wide range of support activities previously done within Defence. By around the turn of the century, all three countries had significantly reduced the size of their military and civilian workforces by increasing their reliance on the private sector.

Whether directed at effectiveness or efficiency, defence reform in Australia and elsewhere is rarely initiated from within. The one exception is the development of joint command and control arrangements, an area where the military itself has driven change. More generally, the pattern is for the government (and sometimes the parliament) to initiate an independent review, which then

leads to reform under government edict. This is true of the last major reform program in Australia, the Defence Reform Program of 1997–2000, as well as the ongoing Strategic Reform Program that commenced in 2009.

So, what remains to be done? In one sense, there’s not much left to do. The big structural reforms of the 1970s can’t be repeated; nor can the extensive outsourcing programs of the 1990s. Consistent with this, the current Strategic Reform Program is more about the refinement of current arrangements than fundamental reform. Despite claims to the contrary, any comparisons with the profound changes wrought by its predecessor Defence Reform Program are as fanciful as the level of savings being claimed. Nonetheless, important work remains to be done.

In Chapter 5, the lessons from the preceding three chapters are drawn together in the context of the initiatives underway in the Strategic Reform Program. The results are mixed. In some cases, the planned reforms are both appropriate and adequate, but in several key areas they don’t go far enough. The chapter includes recommendations for how to proceed.

2 Civil–military affairs

Legal matters

It’s often said that defence of the nation is the first responsibility of government. From a constitutional perspective, it’s the only responsibility. Of the 128 sections in the 1901 Australian Constitution, only one explicitly assigns a responsibility. That occurs in section 119 and is a direct consequence of the transfer of the various colonial naval and military forces to the Commonwealth at the time of Federation:

The Commonwealth shall protect every State against invasion and, on the

application of the Executive Government of the State, against domestic violence.

Elsewhere, the Constitution focuses on processes and powers. It sets out the processes for electing the Australian Parliament and making laws, and it assigns powers to the Commonwealth. Relevant here is s. 51(vi), which gives the parliament the power to make laws with respect to ‘The naval and military defence of the Commonwealth and of the several States, and the control of the forces to execute and maintain the laws of the Commonwealth’. This is commonly referred to as the ‘defence power’, and it allows the Commonwealth to raise, maintain and use the defence force. Note that, consistent with s. 119, the defence power refers not just to defence from external threats but to the maintenance of domestic order.

The final section of the Constitution relevant here is s. 68:

The command in chief of the naval and military forces of the Commonwealth is vested in the Governor-General as the Queen’s representative.

From time to time, grievous confusion has arisen from this seemingly clear statement: specifically, that the Governor-General has a reserve power in relation to the defence force. As one defence minister put it: ‘This often leads to the misconception that the Governor-General could act independently to call out or deploy the ADF in the interests of the nation and without acting on the advice of the government of the day.’

Nothing could be further from the truth. The Governor-General’s role as commander-in-chief is unambiguously and entirely titular—and it was never intended to be otherwise. When the Constitution was drafted, the commander-in-chief role was firmly conceived in the context of responsible

government; that is, as acting on the advice of ministers. So why doesn’t the Constitution say so? In a seminal analysis of the history and meaning of s. 68, Sir Ninian Stephen, who served as both a justice of the High Court and as Governor-General, notes that it would have been more explicit but for ‘considerations of elegance of drafting and, perhaps, fear of being regarded in Whitehall as constitutionally naive’. Given the confusion that’s subsequently arisen, it might have been better to sacrifice elegance and pride for clarity.

In any case, there’s no confusion in the *Defence Act 1903*. Section 8 is abundantly clear: ‘The Minister shall have general control and administration of the Defence Force’, and the powers vested in persons by the Act shall be ‘exercised subject to and in accordance with any directions of the Minister’. This includes the command of the ADF by the Chief of the Defence Force (CDF) and the command of the Army, Navy and Air Force by their respective chiefs.

The essential point is that the defence force isn’t an independent institution. To the contrary, it’s under direct ministerial control just like a department of state. So, while some public institutions are constituted with a high degree of independence—for example, the judiciary and the Reserve Bank—no such latitude is afforded the defence force under law. Judges are expected to be impartial; generals, obedient.

The highly rigid hierarchies within Defence make any notion of independence especially problematic. Unless it’s made absolutely clear otherwise, members of the defence force can easily form the view that their responsibilities terminate with the chief of their service or the CDF. If they do, the Defence Minister then becomes nothing more than a feature on the terrain to be navigated.

Finally, it's necessary to be clear about the role of the parliament in controlling the defence force. It has none. The control of the defence force, including the decision to wage war, is an executive privilege. Proposals to rescind or limit that power through legislation arise from time to time, but such a move would be both impractical and unnecessary. It would be impractical because it would impose an unwieldy delay in taking military action. Here we can learn from foreign experience. Although the US constitution vests the power to declare war in the Congress, since World War II the President has been given the power to take unilateral action as a practical measure.

In any case, parliamentary control is unnecessary. Under the Westminster system, the government serves at the pleasure of the House of Representatives. If the government doesn't have the support of the House to take military action, the House can bring the government down. This isn't a merely hypothetical possibility—it came very close to happening to the Asquith government in the United Kingdom in the tense prelude to World War I.

Below the level of the minister, things get interesting. Section 9A of the Defence Act says that 'the Secretary [of the Department of Defence] and the Chief of the Defence Force shall jointly have the administration of the Defence Force' except with respect to 'matters falling within the command of the Defence Force by the Chief' (and likewise the command of the individual services) or 'any other matter specified by the Minister'. This dual arrangement is usually referred to as the 'diarchy', the rationale for which is explored below.

The role of civilians

Defence has more than 20,000 civilian employees—roughly one for every three

uniformed personnel. There are three reasons, or at least three reasons given, for employing civilians in Defence. The first is financial. Uniformed personnel are paid more than civilians at similar levels of seniority because of the rigours of military service. In addition, unlike civilians, military personnel receive extensive (and costly) training and education throughout their careers. So, unless an employment position is in the military chain of command or is liable for deployment on military operations, it will usually make sense to place a less costly civilian in the role. On this account, a great many administrative and support jobs are filled by civilians.

The second reason sometimes offered is practical. Some skills needed by Defence can only be developed and maintained through a long civilian career. But this turns out to be a surprisingly small group. Doctors, dentists, nurses, lawyers, accountants, psychologists, engineers, musicians, chaplains and tradespeople all serve in uniform. So what's left? Scientists, of which Defence has more than a thousand, presumably fall into the category. So too, perhaps, do those public servants who develop and coordinate policy advice—though this is a tenuous claim, given that serving and retired military officers routinely fill such positions. In reality, the practical constraints on the roles performed by uniformed personnel are very few.

The third reason is by design. Civilians are employed in Defence to oversee and dilute the power of the military. And it's for that reason alone that the defence force is jointly administered by a Secretary and a CDF—no constitutional impediment prevents the defence force from being solely administered by the CDF. And, clearly, whatever special skills and experience the Secretary brings to Defence could equally be provided by a subordinate to the CDF. There's even a precedent of sorts; the Australian Federal Police is run by a Chief Commissioner

without a civilian counterpart. But such an aggregation of power by a military chief would be highly anomalous in a modern democracy.

Although the details vary, joint administration is common under the Westminster system and occurs in Canada, Ireland, India, Malaysia and the United Kingdom. In New Zealand and Singapore, the defence department and defence force are separate entities. Nonetheless, the essential point is that in all those countries the military chief is balanced by a civil servant counterpart. Similar arrangements exist in much of Europe, including France and Germany. Under the US system, the Defense Secretary effectively fills the roles of secretary and minister simultaneously (and is accompanied by an extensive politically partisan civilian staff spread across the Pentagon). One way or another, democracies empower civilians below the level of executive government to *at the very least* provide defence policy advice and often to directly administer the defence force in conjunction with a military chief.

The goal is *not* to impose a layer of civilian control over the defence force below that exercised by the elected government (that is, civil control). Rather, the intent is to ensure that the government has an independent channel of objective advice on, and independent oversight over, the development, management and employment of the defence force. Otherwise, the government would find itself in the invidious situation of having to rely solely on the defence force for advice about the force—much like a department of education run by a teachers' union or a health department run by a medical association.

It's important to note that there are no restrictions on the purview of the Secretary under the Defence Act beyond 'matters falling within the command of the defence force'; the powers of administration are held jointly. So,

while the Secretary can't exercise command, that doesn't place any limits on the range of issues—operational matters included—that he or she can offer advice on, unless directed otherwise by the Defence Minister. And those recent ministerial directives to the Secretary and CDF that have been made public place no limits on the powers and responsibilities of either the Secretary or CDF beyond that set by legislation. However, Defence declined to provide copies of the extant directives for the purposes of this study, so it's impossible to say whether things have changed.

Critiques of the administration of Australian defence often cite the diarchy as a central problem. This is understandable. Not only is it rare to find anything like it in the private sector, but the potential for confused authority and dispersed accountability appears to be high. In reality, however, neither of these latter concerns has emerged as a serious problem over the thirty-five years the diarchy has been in place. As explained in the next chapter, although authority and accountability are seriously dysfunctional across much of Defence, the diarchy is neither the source nor part of those problems. In fact, it's perhaps the place in the organisation where authority and accountability are clearest. Moreover, the record shows that successive secretaries and CDFs have generally worked together well.

Nonetheless, the question remains: would things be better if the ADF and the Defence Department were separate entities? The clear advantage of separation would be a civilian voice to advise the government on defence matters, fully independent of the military. This has some attractions. Under present arrangements, there's a risk that the Secretary and his or her attendant civilian cadre will become captured by the military's agenda. To an extent, that might already have occurred: civilians are now playing a much diminished

and less independent role in some critical areas than they did in the past.

There are two factors at play. First, the higher levels of the organisation have evolved into what could best be described as a joint civilian–military entity. On one level, this is a favourable outcome: to function smoothly, the civilian and military parts of the organisation must cooperate closely. On the other hand, some degree of creative tension between military and civilian views is desirable. Otherwise, the *raison d'être* for joint civilian–military administration is lost.

The erosion of an independent role for civilians began in 1997, when a major restructure of Defence removed the explicit civilian–military structural counterbalances within the higher levels of the organisation. The problem is particularly acute when it comes to the most important long-term decisions made about defence—the acquisition of multi-billion-dollar equipment. Until 1997, proposals for new equipment were actively contested by civilian analysts, and advice on such matters to the government was formulated by a senior civilian executive. Today that role's performed by a military officer, and civilian oversight has morphed into little more than the facilitation of proposals through the intricacies of financial compliance and Cabinet paperwork. When it comes to the development of the defence force, civilian oversight has been replaced by a division of labour in which civilians are relegated to administrative roles. The tendency of ministers to demand a single line of advice has exacerbated the problem.

Second, the military has simply become more powerful within Defence and more influential within government. In part, this is a consequence of the natural tendency for greater military influence to arise when the defence force is on active service, as has been

the case now for a little over a decade. And the trials and tribulations arising from the qualification of Defence's financial accounts exacerbated matters by distracting at least one Secretary for an extended period.

More critically, the recent pattern of appointments of secretaries and CDFs has undoubtedly undermined civilian influence. Over the past fourteen years, there have been five permanent secretaries (and one extended acting appointment) in a period covered by just three CDFs. What's more, while every CDF comes to the role with around three decades of experience, only two of the past six secretaries had any experience in Defence before taking up the role, and in one of those cases that experience amounted to a single previous appointment. To make matters worse, over the same period there have been seven defence ministers. So, on any given day for more than a decade, chances are high that an invariably experienced CDF was working with a relatively neophyte departmental secretary, minister, or both.

None of this should be taken to suggest that civilians don't play an active role in the formulation of defence policy in many areas. For example, no Defence Minister would attend a meeting with an international counterpart without a comprehensive brief prepared by the civilian policy specialists in Defence. But it's important to focus on what really matters. Key advice about the size and shape of the ADF—the main determinant of defence effectiveness for decades ahead—is largely formulated by the military; civilians are left to manage the finances and draft White Papers that, as often as not, provide *ex post facto* justification for the force structure.

Notwithstanding the limits of civilian influence under current arrangements, carving off a separate Department of Defence

is no guarantee of a strengthened civilian perspective. Although the entity so created would be more independent, it mightn't necessarily be heard. The very real possibility is that a separate department would end up having no greater influence than the departments of Finance, Treasury and Prime Minister and Cabinet do today. On balance, therefore, it's almost certainly better to have a Secretary inside the defence force tent than outside. Options to make the role of civilians within Defence more effective are explored in later chapters.

The service chiefs

It may be surprising to some readers that the three service chiefs—Army, Navy and Air Force—have barely rated a mention in the discussion so far. Certainly, the Defence Act gives them a prominent role: s. 9 of the Act assigns each not only command of their arm of the defence force but the role of adviser to the minister on matters relating to that command. The reality is a little more complicated than might be inferred from the Act.

To start with, the command of military operations isn't the responsibility of the service chiefs. Instead, the CDF delegates operational command authority to the Chief of Joint Operations (of whom no mention is made in the Defence Act), to whom military forces are temporarily assigned for specific missions and exercises. The Chief of Joint Operations runs a dedicated headquarters (HQ Joint Operations Command) with around 500 staff about 30 minutes drive from Canberra, near Bungendore, New South Wales. Those forces not assigned to operations under the Chief of Joint Operations remain under the command of their respective service chiefs for ongoing training, including preparation for future operations. Figure 1 outlines the command

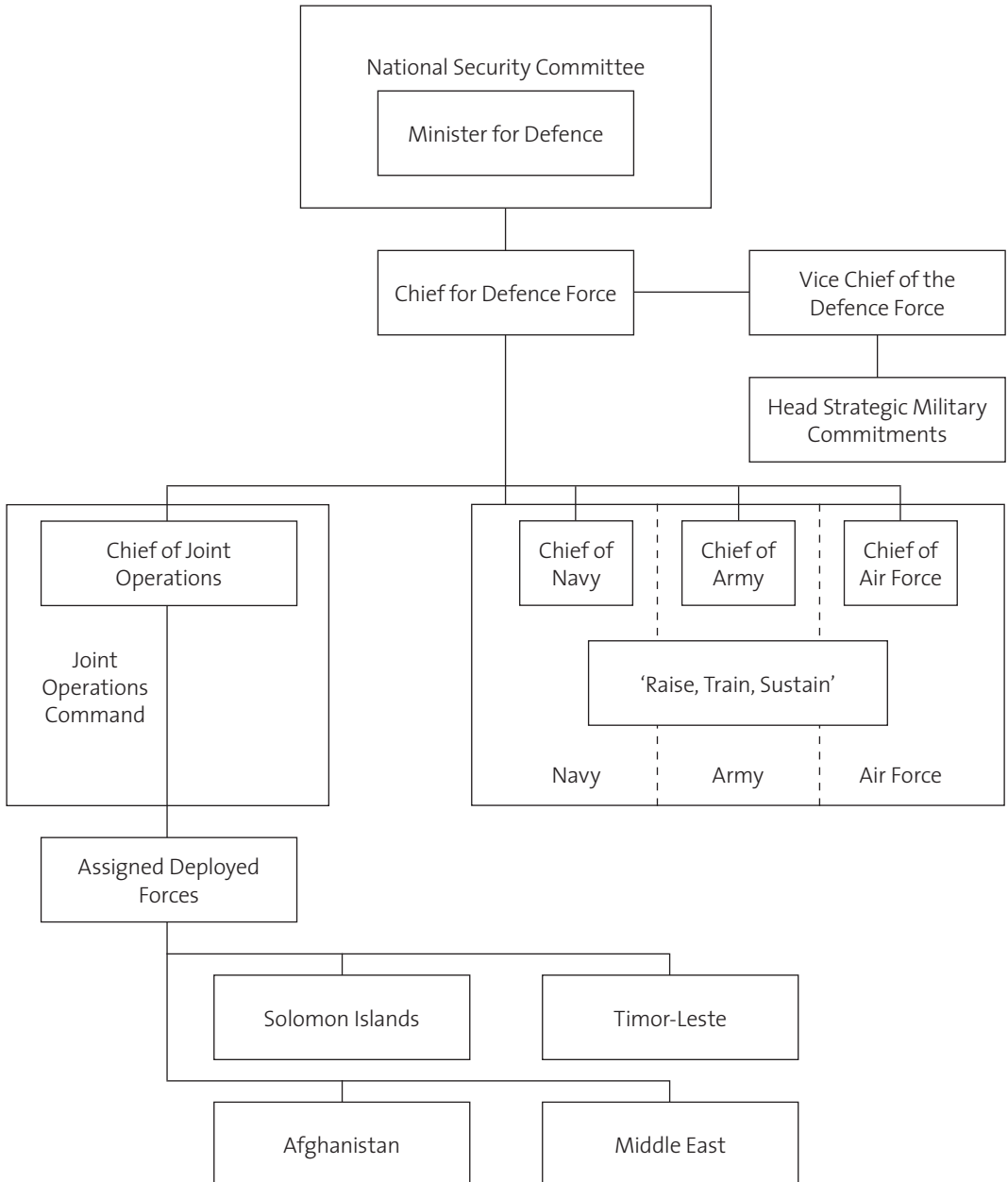
arrangements in the ADF. After a decade of continuous deployment, every indication is that those arrangements are effective. This no doubt reflects close and effective cooperation between the three services and the HQ Joint Operations Command. Whether these multiple military headquarters (there are several others not mentioned here) are necessary or efficient is beyond the scope of this report.

Even when it comes to the command of those forces not on operations, the role of the service chiefs is something less than might appear in the Act. As the next chapter makes clear, the service chiefs control only a limited share of the resources necessary for the delivery of the capabilities that they're nominally responsible for. What's more, they're but three of the sixteen voices around the table of Defence's central management committee.

Nonetheless, it's a mistake to view the service chiefs as merely residual limbs left over from a primordial era predating the evolution of joint operational command and integrated defence management. Not only do the chiefs set the tone and ethos of their services, but they're highly influential in shaping plans for the future development of their forces.

It's inevitable that from time to time differences will arise between the advice tendered centrally from Defence to ministers and that which might otherwise have been tendered from the individual services—especially on matters of force development. And it would be naive to think that service chiefs (and other senior officials) don't sometimes lobby ministers (and on occasion prime ministers) directly. Indeed, many a long VIP flight has been spent profitably doing so. To the extent that this complicates or undermines coherent policy development, it's up to the minister to set the ground rules.

Figure 1: Command arrangements for military deployments



Advice

A critical question for every government is how it should treat the advice it receives from Defence. On a great many matters, the answer is 'no different from advice in any other portfolio'. A request for an extra administrative building on Russell Hill, for example, can be treated in the same way

as a request from Treasury for additional office space in its corner of the parliamentary triangle; the minister can discuss with advisers, consult with colleagues, solicit opinions from third parties, and use common sense to reach a decision. On other matters, particularly those involving operational deployments and military capability, the situation is different.

It's not simply that most defence ministers come to the portfolio with close to zero experience in defence issues, nor even that there are fewer alternative sources of advice than in areas like health, education and economics; it's that advice on military matters is frequently perceived as the unique preserve of the military. There's even a term-of-art, 'professional military judgment', that's used to capture the special provenance of military advice. How then should ministers and the government deal with the advice they receive from the military?

One model that's popular in military circles in Australia and the US is 'objective control'. At the risk of oversimplification, objective control envisages a clear demarcation of responsibility between political control and military command. Put simply: politicians identify objectives for the military to deliver and the military delivers those objectives. Implicit in the model is that the military leaves politics to the politicians, and politicians leave military matters to military professionals. To justify this division of labour between the elected government and the military, objective control assumes a high degree of autonomous military professionalism. While the concept is most usually posited in terms of military operations, it's often taken to apply equally to any predominantly military matter, such as force structure, discipline and training.

Perhaps the best analogy for objective control is that of a patient seeking the help of a medical specialist. While it's up to the patient to decide whether to undergo treatment to remove a tumour, it's for the surgeon to plan and execute the operation.

The appeal of objective control to the defence force isn't simply that it gains a sphere of action free from interference; it's also consistent with the way objectives are often set within the military. Few officers make it through staff college without having studied

the remarkable poetry of the 1944 directive issued to Eisenhower for what became the Normandy invasion:

You will enter the continent of Europe and, in conjunction with the United Nations, undertake operations aimed at the heart of Germany and the destruction of her armed forces.

But much has changed about warfare since World War II, and even then the demarcation between military action and political policy was far from distinct. Today, the 24-hour news cycle and instantaneous communications unavoidably embroil politicians in the details of military operations. And it's not just that objective control is based on a highly artificial model of how things might work—it's simply a poor idea.

Objective control presupposes military professional expertise of unparalleled excellence and unswerving certainty. Neither can be counted on. As in any other profession, there are significant differences of opinion on matters within the military. Indeed, on any given issue professional military judgment can and does vary greatly depending on who is asked. There's no one true 'professional' judgment, only that of a particular person on a particular day. For that reason alone, unquestioning passive acceptance of military advice is inconsistent with ministerial responsibility.

Returning to the medical analogy, what's required is informed consent. Advice and consent are the opposite sides of the same coin. While patients aren't generally competent to judge which scalpel should be used for an incision in their abdomen, they're perfectly able to discuss options with their doctor, to seek a second opinion, and even to compare the merits and risks of alternative procedures based on independent research. What's more, patients are usually able to judge the merits of a course of treatment

over time and seek a new doctor if they're not satisfied. Precisely that sort of due diligence and attentive oversight should be expected from ministers on all defence matters, including operational issues.

Some politicians learn this lesson too late. Writing some fifteen years after the end of World War I, Lloyd George lamented that he hadn't been more active in interfering in the conduct of the conflict. More poignantly, he observed that whatever potential military leaders of quality Britain might have possessed 'were consigned to the mud by orders of men superior in rank but inferior in capacity'.

Dissent

Civil control of the military is an essential to the health of a democracy, but it provides no guarantee of good policy, let alone effective defence. So, what happens if the government of the day ignores the advice it receives from Defence and pursues an alternative course of action? In the vast majority of cases, nothing happens. Just as in any other portfolio, the government is free to pursue any lawful course of action it deems appropriate, irrespective of the advice it gets from the relevant department of state. In fact, there's little doubt that this occurs hundreds of times a year across government. Secretaries (and the CDF in the case of Defence) simply get on with the job of implementing the government's policies, mindful that it's ultimately the job of the electorate, not them, to judge the merits of the government's decisions.

The option of resignation is always available to public servants and military members if they disagree with government policy. Nothing in the law prohibits it. But for the government's most senior advisers—departmental secretaries and military chiefs—resignation is only appropriate in the most extraordinary of circumstances.

For the public service and defence force to be apolitical, they must remain above politics. Resigning or, worse still, threatening to resign over a policy issue is manifestly a political act, and in the case of defence it would be corrosive to proper civil control. Given the substantial political damage that a resignation by a secretary or military chief would cause the Defence Minister, a threat of resignation over a policy issue is tantamount to subversion of civil authority through blackmail.

Such extraordinary circumstances can arise. In February 1942, the then Chief of the General Staff, Lieutenant General Vernon Sturdee, offered his resignation to Prime Minister Curtin unless the two Australian divisions in the Middle East were brought home to defend against the Japanese. History has commended Sturdee's actions on that day because of the grave threat to Australia's safety (even though there's no suggestion that Curtin contemplated doing otherwise).

Other circumstances that might reasonably be met with resignation (or disobedience) would include a direction to employ the defence force unlawfully or contrary to the laws of armed conflict to which Australia is bound by treaty. Less clear, but possibly relevant, is a situation where the government directs a course of action in which the human costs manifestly outweigh the benefits. When resistance is futile, history looks more kindly on commanders who surrender than on politicians who demand they do otherwise. This is certainly so in the case of Field Marshal Friedrich Paulus's surrender to the Soviets in defiance of Hitler in February 1943.

Comment from within

The vast majority of people with an up-to-date understanding of defence issues reside with Defence. Given that an active and informed public debate is a necessary

precondition for quality policy, the following question arises: when, if ever, is it appropriate for serving members of the defence force or defence civilians to make their views public?

Official guidelines reflect the considerable sensitivities and complexities that this question carries. Space prohibits a recounting of the guidelines and their numerous caveats, but a commonsense reading of the Australian Public Service Code of Conduct reveals that public servants can express personal views provided that they only rock the boat a little bit. No doubt, a similar constraint applies to military personnel.

Nonetheless, in its own quiet way, Defence finds ways for its personnel to put their views forward on a range of issues. Each of the arms of the ADF has its own centre for research. The Navy has its Sea Power Centre, the Air Force has its Air Power Development Centre, and the Army has its Land Warfare Studies Centre. Apart from producing formal military doctrine and historical studies, each of the three centres produces publications dealing with current and future defence issues. In addition, the *Australian Defence Force Journal* publishes papers on a broad range of topics.

These various avenues provide an opportunity for the structured discussion of defence issues by military professionals and the communication of their views more broadly. Even though the end result is ultimately constrained by the limits on public comment applying to defence personnel, it's better than nothing.

The US, in contrast, has a more permissive view, as exemplified by the article 'A failure in generalship' by Lt. Col. Yingling in the *US Armed Forces Journal* in 2007. Although the title is self-explanatory, the article is worth reading to see just how frank and fearless commentary by serving officers can be in the US. It's unlikely that so unflinching a perspective by an ADF member would have

been allowed to see the light of day. If this seems an overstatement, it's worth noting that the only robust critique of Australian defence policy published by a serving military officer in recent times came from John Angevine, a colonel in the US Army.

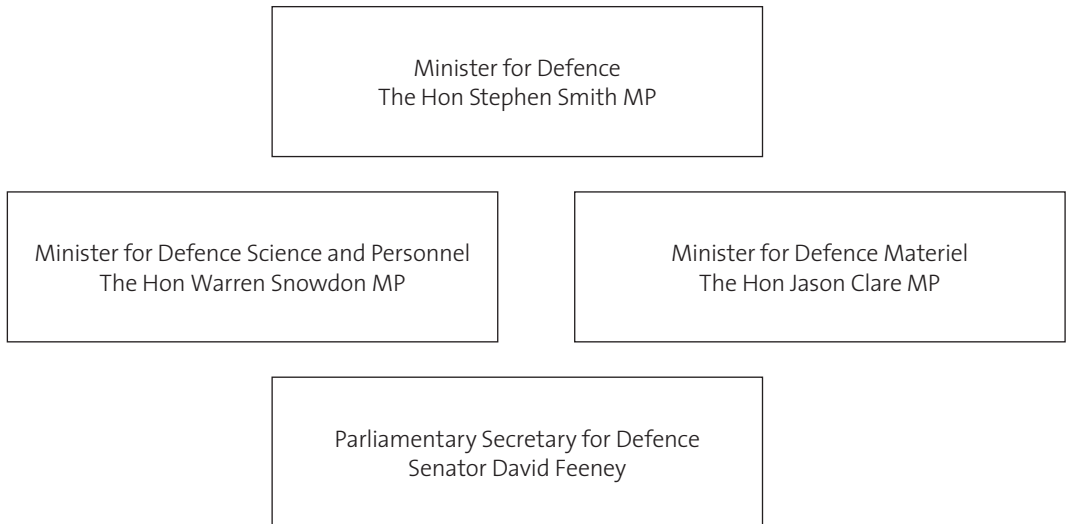
Present arrangements reflect the inevitable tension between Defence as both a servant of the government and a key repository of informed thinking on defence matters. And while a more liberal approach might lead to a better informed public debate on defence issues, it's unlikely to occur so long as Defence continues to embarrass its political masters at the alarming rate it does. What minister would want to invite further trouble?

Ministers

The role and responsibilities of ministers under the Westminster conventions are well understood and needn't be recounted here, but the Defence portfolio brings particular challenges for ministers that merit discussion. For one thing, the size and complexity of Defence makes it difficult for any single minister to track its activities in adequate detail. To alleviate this problem, it's become common practice to appoint one or more junior ministers and parliamentary secretaries to work with the Defence Minister. On the whole, these arrangements have proved workable despite less than perfect cooperation within the ministerial team from time to time. Current arrangements appear in Figure 2.

Even with two junior ministers and a parliamentary secretary, the sheer volume of work falling on the Defence Minister can be prodigious. In the first eleven months of last year, no less than 2,200 ministerial submissions were lodged by Defence to its senior minister. In contrast, in the late 1990s the annual number of submissions was only 690. This change merits exploration.

Figure 2: Defence ministerial appointments, March 2011



Source: Defence Portfolio Budget Statements, 2011–12.

In part at least, the increased flow of submissions is a response to the series of embarrassments suffered by various ministers over the past decade due to inaccurate or untimely information from Defence—from ‘children overboard’ in 2001 to the unheralded collapse of the ADF’s amphibious lift capability in 2011. Such events erode the trust of ministers and naturally lead them to demand ever more information from the department. Uncertain of how far the threshold of ministerial trust has been lowered, officials then have little choice but to push ever more minor matters up to the minister. Each new embarrassment renews the cycle and submerges the minister in ever more minutiae.

To complicate matters further, the 24-hour news cycle has increased the ‘velocity of government’ so that ministers often find themselves managing the ephemeral issues of the day at the expense of more substantive matters. The combination of a mountainous in-tray and a distracted (and often new to the job) minister is a recipe for slow decision-making, or worse.

Effective control (by the minister) and effective administration (by the diarchy) can’t be based on a river of paperwork. It’s pointless for a minister to try to micro-manage a department of the size and complexity of Defence. Not only does it waste the minister’s time, but it can grind the department to a virtual standstill. Instead, a workable day-to-day demarcation between the roles and responsibilities of the minister and those of the diarchy must be found—a demarcation that allows the minister to focus on key strategic and operational issues. None of this will stop problems from emerging in an organisation the size of Defence, but neither will a rising tide of ministerial submissions on minor matters.

When things go wrong—and they will—every Defence Minister faces dual dilemmas. The first is whether to take responsibility for what’s happened, or to sit at arm’s length and let Defence take the blame. Most ministers begin with the former approach, but many slip into the latter when the going gets tough. The temptation of ministers to distance themselves from Defence when things go

wrong is understandable, and in some cases the action is fully expected. Many of the problems that emerge are either 'sprung' on ministers unexpectedly or are due to actions taken long before their appointment (this happens frequently, given the rapid turnover in defence ministers), but such an approach can only be sustained for a limited period. The onus eventually falls on ministers to fix the problems they identify.

This raises the second dilemma: what to do. The usual response is to initiate a review. Often this means an internal review by Defence itself or, if the matter is especially serious, an external review by an expert or baron of industry. Eventually, some months later, the results of the review are made public and Defence is told to implement the recommendations. There's nothing intrinsically wrong with such an approach; it allows for careful and informed decision-making by the minister. That said, the unrelenting frequency of reviews has at times become a source of some cynicism among observers.

The question is often asked: why aren't Defence officials held to account when things go wrong? In part, the answer is that they are, but that such matters are dealt with discreetly. There's little to be gained by making the management of underperformance a spectator sport. Still, in contrast to sackings in the corporate world, dismissals of defence officials are exceedingly rare events.

This can probably be ascribed to two factors. First, diffuse and confused accountabilities within Defence make it difficult to know who to ultimately hold to account for anything. The 'system' more often than not is viewed as the culprit. Second, ministers have few palatable options available if they want to take action anyway. An all-out stoush would not only damage the minister's working

relationship with Defence but would probably be very damaging politically. To put it bluntly, a Prime Minister would surely find it easier to replace a Defence Minister than a CDF or Secretary. The sad reality is that defence ministers are caught in an invidious situation from the day they take up the job with limited ability to hold Defence officials to account.

The military–industrial complex

In his final televised speech as US President, Eisenhower warned his countrymen to 'guard against the acquisition of unwarranted influence, whether sought or unsought, by the military–industrial complex' and cautioned that 'only an alert and knowledgeable citizenry can compel the proper meshing of the huge industrial and military machinery of defense with our peaceful methods and goals, so that security and liberty may prosper together.' Serious words indeed.

At the time, the US was locked in an arms race with the Soviet Union and defence spending accounted for 8.2% of GDP. In Australia today, no such imminent threat exists and defence spending is below 2% of GDP. Nonetheless, no analysis of civil–military affairs would be complete without a few words to describe defence industry and its influence on policy.

Defence spends roughly \$5.8 billion each year on military equipment and another \$4.7 billion on repairs and maintenance. Of the total of around \$10.5 billion, about 52% is spent in Australia; the remainder goes overseas. The top 10 defence materiel contractors in Australia—those involved in specialist military equipment—had a total annual turnover of \$5 billion in 2010. Of the top eight firms, all but one is a subsidiary of an overseas-based multinational, and the one Australian firm is owned by the government. Below that level, there are several other large firms and myriad small-to-medium enterprises that are subcontracted by the big players. According

to the government, in 2010 there were approximately 29,000 people employed in defence industry within Australia.

Many state governments are active in promoting themselves as destinations for defence work. New South Wales, Victoria and South Australia all have dedicated defence advisory councils, each boasting retired military officers and defence civilians of very senior rank. South Australia alone spends more than \$16 million a year to promote itself as 'The Defence State', and has invested around \$300 million in state-owned infrastructure to help entice naval construction to the state.

Although the latest financial disclosure records held by the Australian Electoral Commission reveal no donations from major defence contractors, vigorous lobbying occurs. Six of the top ten defence contractors are listed as clients on the Australian Government Lobbyist Register (along with the US Navy).

Across the defence industry sector, there are hundreds of former Defence employees, and there's a constant flow of personnel from Defence to defence industry. Moreover, retired senior military and civilian officers routinely take up jobs as advisers and executives in defence firms. In one instance, the deputy head of the Defence Materiel Organisation (DMO) transferred directly into the CEO position of the then largest defence contractor operating in the Australian market. In another, a retiring Defence Minister took up a position as adviser to another large firm. And, as recent media reports made clear, key decision makers in Defence routinely enjoy the hospitality of the defence industry in the form of meals and entertainment. The head of the Capability Development Group in Defence topped the list with 28 instances of hospitality, including dinners, theatre shows and sporting events.

None of this should be taken as a sign of corruption. On the contrary, proven cases of malfeasance are relatively infrequent and typically occur at a low level in Australian defence procurement. Of course we can't be sure, especially given that there's no equivalent to the New South Wales Government's Independent Commission Against Corruption overseeing the sector. In any case, the fact remains that there's a well-funded and well-connected lobby of vested interests vying to influence the government on defence procurement decisions. Although the extent of its influence is hard to judge, it's unlikely that such efforts would continue if they brought no reward.

One impact has been that governments have been induced to favour options that involve work being done in Australia more than would be justified on strategic or rational economic grounds. Of course, the Australian Government hardly needs encouragement in this regard—defence is one of the few areas where the government can directly take credit for so-called 'jobs creation'. Consistent with this, it's routine for firms to offer domestic work packages even when it means adding the cost of duplicated assembly facilities to their bids. The end result has been that the taxpayer has paid more and the ADF has received less than would have otherwise been the case, while at the same time scarce skilled labour has been diverted from more productive activities.

3 Defence administration

Defence is full of people at all levels who are passionate about their jobs. For many, it's not just a matter of professional pride but of a sense of mission. According to the last Defence attitude survey, 81% of ADF members and 72% of Defence civilians are proud to tell others that they're a member of their service. Military separation rates are at a four-decade low. And there's no reason

to believe that there's anything wrong with the quality of the people working in Defence. The military has a commitment to education, training and development unparalleled in the private sector, and Defence is as competitive as any other government agency in attracting qualified civilians.

Yet, somehow, the organisation manages to be something less than the sum of the individuals who make it up.

At this point (in what is an oft-told story), it's usual to introduce the caveat that while Defence might struggle administratively, it's nonetheless capable of 'operational excellence' in the field. But to do so would express unwarranted complacency. While the defence force has successfully undertaken a series of difficult operations over the past decade, those operations have tested only limited parts of the force in a limited range of circumstances. In reality, the ADF remains largely untested in its primary role of defending our air and maritime approaches—probably for the better, given the ongoing problems with the submarine and amphibious lift fleets.

Ultimately, it's impossible to separate the operational capacity of the ADF from the effective administration of Defence. That's why it's critical to get administration right.

Sound defence administration demands both effectiveness and efficiency; Defence should deliver what the government asks of it, and do so at least cost. There's no conflict between effectiveness and efficiency: within a given budget, greater efficiency allows for greater capability and hence greater effectiveness. Several factors shape Defence's effectiveness and efficiency; organisational structure, business processes, budgeting and planning, accountability and governance are all important. Those factors are examined in turn below. The chapter concludes with an examination of capability planning and

acquisition, including a look at Defence's acquisition and materiel support agency, the DMO.

Structure and processes

The structure of Defence is closely bound up with its business processes, and it's impossible to understand one without the other. Far from being an aggregation of the three services and a central headquarters—as one might expect—Defence is made up of thirteen separate programs (of which the services are but three) and a quasi-independent agency (the DMO). Although they're not referred to as such, it's useful to divide the fourteen component parts into three categories based on the primary role they perform: output, support and administration. As will be explained, some overlap of roles occurs.

There are five programs directly involved in the delivery of outputs. The Army, Navy and Air Force deliver *preparedness for military operations* by 'raising, training and sustaining' military capabilities; Joint Operations Command delivers *military operations* under the framework explained in the previous chapter; and the Intelligence and Security program delivers *intelligence* while also overseeing security within Defence. The remaining two outputs, *military diplomacy* and *advice*, are generated from around the organisation at a minor cost.

Many of the inputs needed to generate Defence's outputs are provided by four support programs. The Defence Science and Technology Organisation (DSTO) provides scientific and technical advice, the Chief Information Officer provides information technology and telecommunications services, and the Defence Support Group provides a range of non-materiel support services, including catering, cleaning, security, gardening, legal services, maintenance,

social work and payroll. The DMO provides two types of services. First, it provides repair, maintenance and provisioning services to the people and equipment fleets operated by the services. Second, it acts as Defence's acquisition agency for military equipment on behalf of the services. In a practical sense, this can be considered a sixth output.

Finally, there are five administrative programs. The Secretary and CDF program includes entities responsible for developing strategic policy and overseeing defence reform, and also hosts a range of statutory military legal functions. The Chief Financial Officer program manages budgeting, financing and reporting; the Capability Development Group plans and seeks government approval for major equipment acquisitions; and the People Strategies and Policy program is responsible for personnel policy and recruiting. Finally, the Vice Chief of the Defence Force program coordinates joint capabilities, including ADF preparedness, and includes a range of joint activities such as health, education and logistics. To some extent, all of the administrative programs are also involved in the delivery of support services.

So, how does it all work? Figure 3 tries to capture the main flows of money, goods and services within the organisation planned for 2011–12 to the extent that accrual accounting allows (a number of smaller internal transfers have been omitted for clarity). Setting aside the \$7 billion investment in new equipment and facilities for use in the future, the total planned cost of operations, preparedness and intelligence during the year is just on \$19.5 billion. Of that, around \$14.6 billion is nominally budgeted to the output programs. In reality, \$5 billion of this money actually goes to DMO under service-level agreements with the three services for sustainment.

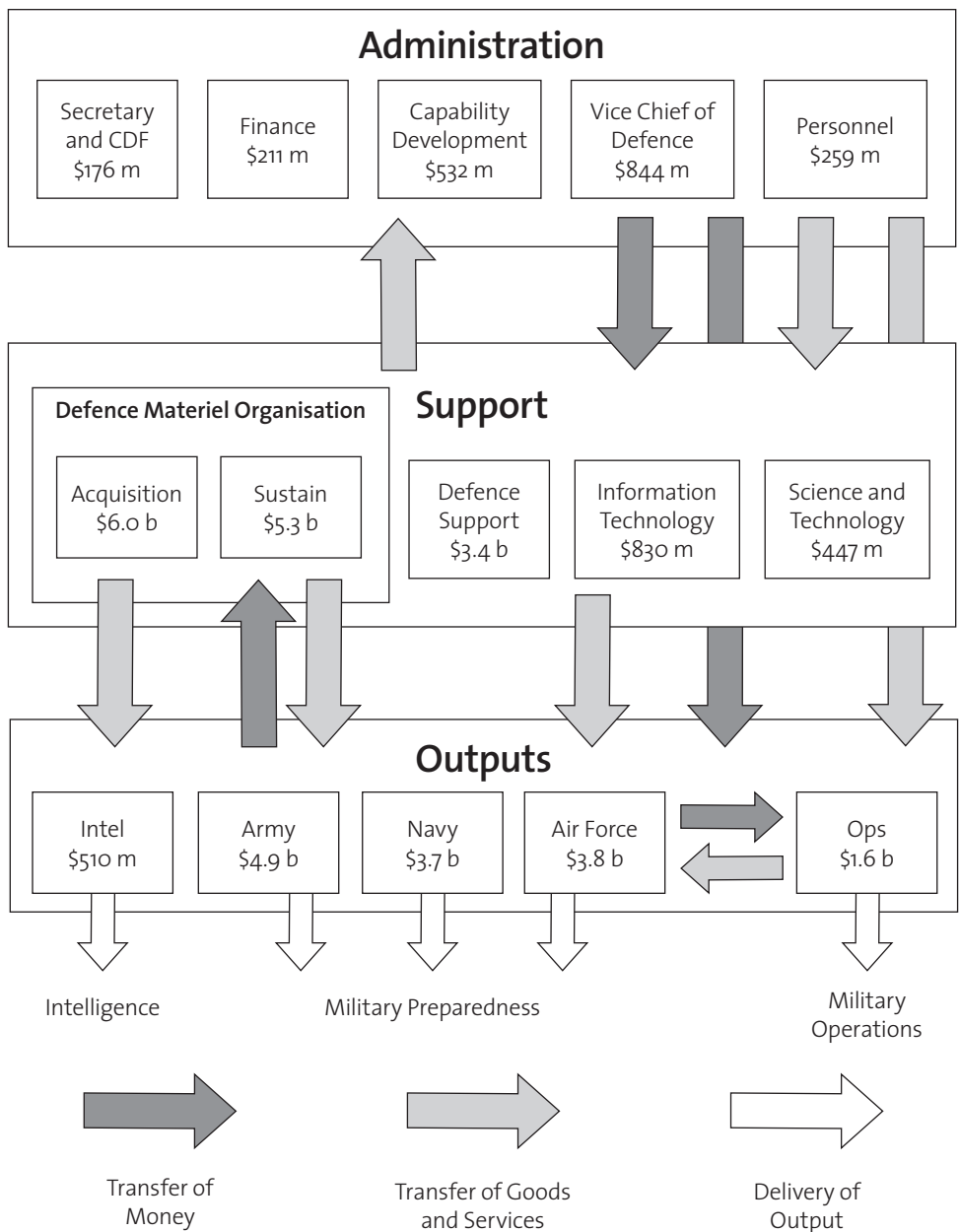
This is only the second year that this has occurred, and the services aren't yet in the

practice of actively managing these funds; nor have they developed the management infrastructure to do so. Indeed, there's no sense of an explicit commercial relationship between DMO and the services for sustainment. Whatever changes the services make are at the margins. Once this is taken into account, the output programs are left with direct control of only \$9.6 billion, but even that overstates the extent of their effective control. If the \$8 billion in military personnel expenses is subtracted, the discretionary funds controlled by the services diminishes to only \$1.6 billion, less than 10% of the non-investment budget.

This is matrix management on a grand scale. The decision to adopt such an approach was taken back in 1997 in the Defence Reform Program. Prior to that, the three services operated much more like self-contained businesses. The rationale for the change was simple enough: to save money by pooling like activities to create 'shared services' across the organisation. It was hoped that substantial savings could be achieved by removing the duplication of fixed costs and creating larger economies of scale. Nobody can say whether this turned out to be the case or not, because repeated changes to the accounting framework in the intervening years make comparisons all but impossible.

What we do know is that Defence now carries much higher managerial overheads than envisaged back in 1997. After initially paring back on executives and senior managers for the first couple of years, rapid and sustained growth in those areas began with the flow of new money generated by the 2000 White Paper—especially towards the latter half of the decade. Table 1 charts the changes from 1999 to 2010. The concern must be that any savings from consolidation have been wiped out by Defence would no doubt argue that the rapid increase in managerial positions was fully justified. To start with, the outsourcing

Figure 3: Follow the money



Source: Defence Budget papers, May 2011.

of support activities was bound to skew the workforce profile upwards. And it's true that the competition for talent has been strong in recent years—especially within the limited labour pool of Canberra. Defence has a relatively low management overhead compared with many agencies, but that's

hardly relevant given that many agencies are focused on policy advice and program oversight rather than program delivery, as in the case of Defence.

Comparing the growth in per capita management overheads in Defence and

Table 1: Defence workforce growth, 1998–99 to 2009–10

| | 1998–99 | 2009–10 | Growth |
|--------------------------------------|---------|---------|--------|
| Top executives^a | | | |
| Civilian | 11 | 16 | 45% |
| Military | 5 | 7 | 40% |
| Senior executives^b | | | |
| Civilian | 100 | 152 | 52% |
| Military | 110 | 173 | 57% |
| Middle managers^c | | | |
| Civilian | 2,772 | 5,534 | 100% |
| Military | 1,360 | 1,937 | 42% |
| Other staff | | | |
| Civilian | 13,769 | 14,372 | 4% |
| Military | 51,425 | 55,587 | 8% |

a Top executives are three-star military officers and above, and civilian deputy secretary and equivalent and above.

b Senior executives are star-ranked military officers and civilian Senior Executive Service employees.

c Middle managers are military colonel and lieutenant-colonel equivalent and civilian Executive Level 1 and 2 employees.

Source: *Defence annual reports, 1998–99 and 2009–10*.

the broader Australian Public Service (APS) helps put Defence's growth in perspective. Because the APS is subject to the same labour market pressures, and has also seen many activities outsourced, one would expect broadly commensurate growth rates. As Table 2 shows, that's not the case. Per capita senior executive positions in Defence grew four times faster than in the APS, and civilian middle management positions almost twice as fast. Only military middle management positions recorded growth below that in the APS. It appears as though Defence's

management overheads have enjoyed disproportionate growth.

In principle, at least, there are savings and benefits to be had from a shared services approach in some areas. Computing services and telecommunications, for example, naturally lend themselves to centralised delivery, as do the highly specialised work of DSTO and the acquisition of major capital equipment and facilities. It also makes sense to deliver a range of legal, personnel and financial services across the organisation.

Table 2: Per capita management, APS and Defence (managers per 1,000 employees)

| | 1998–99 | 2009–10 | Growth |
|----------------------------------|---------|---------|--------|
| Defence senior executives | | | |
| Defence civilian | 6.0 | 7.6 | 26.1% |
| Military | 2.1 | 3.0 | 44.2% |
| Military + civilian | 3.0 | 4.2 | 38.4% |
| APS senior executives | | | |
| APS | 15.9 | 17.3 | 9.1% |
| Defence middle managers | | | |
| Defence civilian | 166.6 | 275.9 | 65.6% |
| Military | 25.7 | 33.6 | 30.6% |
| Military + civilian | 59.4 | 96.1 | 61.7% |
| APS middle managers | | | |
| APS | 183.7 | 254.6 | 38.6% |

Source: *Defence annual reports, 1998–99 and 2009–10, APS Statistical Bulletins, 2002–03 and 2009–10*.

In other areas, the potential benefits are less clear-cut. There's no iron rule that the savings from consolidations of activities always exceed the additional cost of their central administration—especially when the activities are inherently local. For example, garrison support (cleaning, catering, building maintenance and gardening) could conceivably be managed just as well, and just as cheaply, by base commanders locally. The same may be true of the sustainment services currently provided by DMO. There are neither synergies nor economies of scale to be had from sustaining separate fleets of ships, aircraft and armoured vehicles. On the other hand, DMO maintains a central pool of contracting expertise and is able to extract some synergy from the overlap between acquisition and sustainment activities. We'll return to the question of sustainment later.

Budgeting and planning

The effectiveness of Defence's outputs, and the efficiency with which they're produced, depend critically on the ability of the administrative programs to orchestrate the flow of resources from the support programs to the output programs. Much like the old command economies of the Eastern bloc, the allocation of resources is determined by central planners rather than through market transactions. Running a command economy the size and complexity of Defence is an enormous challenge—a challenge that's complicated by three factors.

First, there's no single central planner in Defence. Nor is there anything that would pass as a single business plan (although a first attempt is apparently under development this year). Instead, loosely linked plans for preparedness, finance, personnel and investment are put together under what's known as the *Defence planning guidance* document. This 'planning by aggregation' approach reflects the fact that there's

no actual corporate headquarters in the department—the five administrative programs exist in parallel with, rather than above, the remaining nine programs. As a result, there's no single coordinating function or chief administrative officer below the Secretary and CDF. To the extent that the buck stops anywhere, it's with the diarchy.

Second, Defence's central planners have only a partial understanding of costs and performance across the organisation. As a result, they're poorly placed to estimate the costs of differing levels of activity or alternative approaches. In fact, on several occasions in the past decade, Defence substantially underspent its budget (independent of volatile acquisitions projects) while continuing to bemoan budget pressures. The problem remains unsolved. For the 2010–11 financial year, Defence handed back \$1.1 billion of unspent investment funds and \$500 million of unspent recurrent funding. In addition, close to \$400 million has accumulated in Defence's internal cash accounts over the past twenty-four months. As a result, \$3.9 billion of previously agreed funding was clawed back by government from across the forthcoming decade in the May 2011 Budget. Extraordinary as it may sound, it's clear that Defence asked for and received more money than it could spend back at the time of the 2009 White Paper.

Defence's incomplete understanding of costs has two sources: it relies on management information systems built around accounting compliance at the expense of management information, and the shared services model gives managers less incentive to understand their costs because they effectively receive 'free goods' from the supporting groups.

Third, even if the central planners were to have a complete understanding of every aspect of the Defence enterprise, they lack the economic and commercial expertise

to take advantage of that information. Although Defence has more than a thousand PhD scientists, only a handful of people are employed as economists (and then mostly in the intelligence arena). The 2008 independent audit of the Defence budget provided clear evidence that Defence lacks the expertise to manage its resources efficiently. From a budget of \$19.8 billion, the audit identified potential annual savings of between \$1.3 billion and \$1.8 billion a year plus one-off savings of between \$200 million and \$400 million.

Accountability

Accountability within Defence is determined by its business model. The output programs—and in particular the service chiefs—are put in an invidious situation. On the one hand, they're responsible for maintaining military capabilities ready for use; on the other, they have only partial control of the necessary inputs. The inevitable consequence is that responsibility is blurred and accountability is lacking.

To the extent that the current shared services model erodes accountability within Defence, the problem could be alleviated by giving greater control of resources to the output programs either by shifting activities back under their direct control where it's efficient to do so, or by allowing them to directly purchase goods and services from the supporting groups. In practice, some combination of the two approaches would probably be required. The result would be that the service chiefs could be held to account both for delivering the preparedness that they're nominally responsible for, and for the efficiency with which it's delivered. These possibilities are explored further in Chapter 5.

But there's more to accountability than coincident control and responsibility. Accountability is something that one person

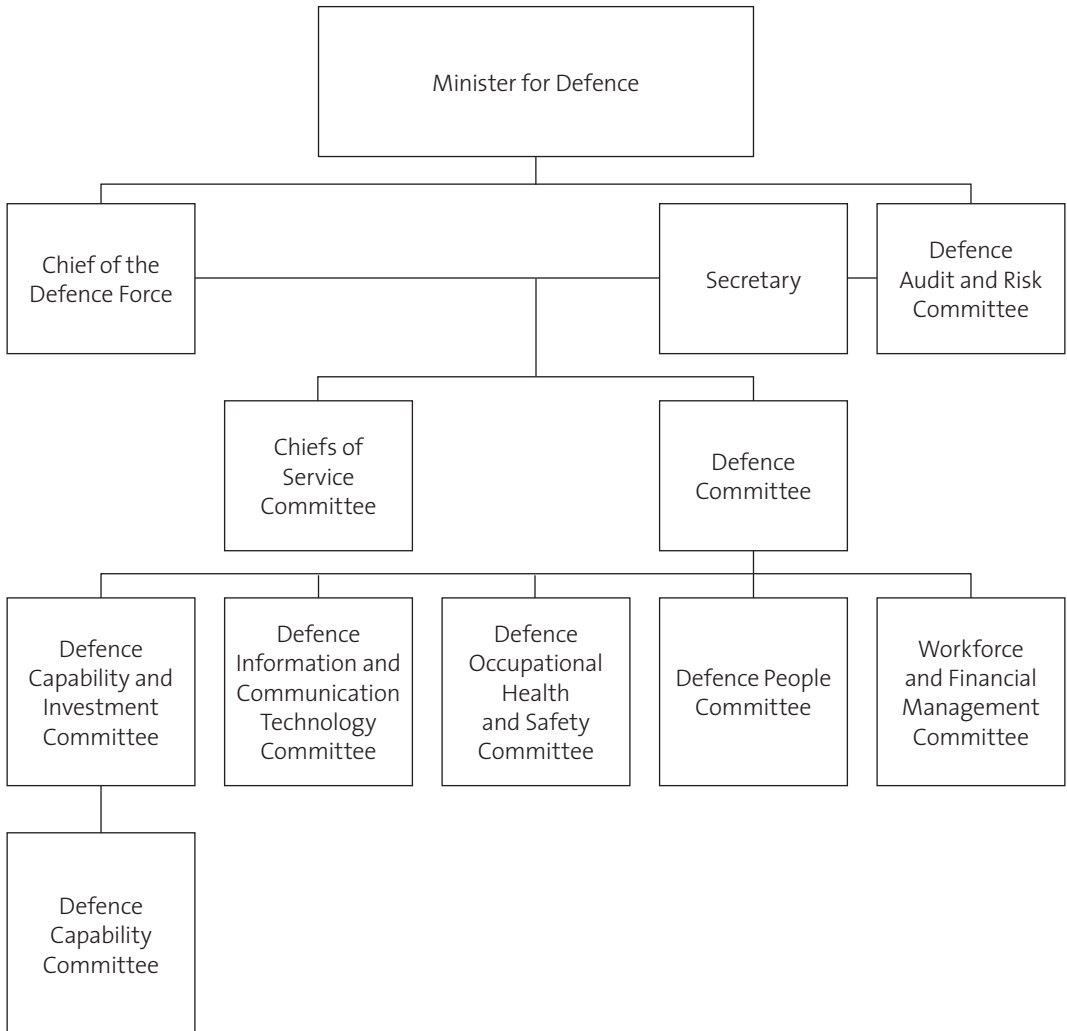
demands from another. As has already been argued, ministers are loath to hold senior departmental officials and ADF officers to account—and for good reason. Similarly, ministers have few ways to provide incentives for improved performance. And so it is throughout the department.

Although the military promotion and posting system provides an avenue for rewards and sanctions for uniformed officers, it acts with a time delay that separates cause from effect. In general, as a public sector agency, Defence lacks the incentives and sanctions available to the private sector. While there are provisions in the *Public Service Act 1999* for actively managing underperformance, a combination of cultural norms and administrative hurdles makes it an infrequent occurrence. Similarly, Defence has a limited ability to attract the sort of human capital available to the private sector at executive levels. That isn't the case at the middle-manager level, where public sector remuneration is typically generous.

Governance

There's a perception that Defence is a hierarchical organisation, and in many ways it is. Each and every person has a rank (or civilian equivalent level) that determines their authority and privileges. Cars, cooks, offices and private bathrooms are all apportioned on the basis of rank. But in a structural sense, Defence is much more like a loose federation. The Secretary and CDF exercise their joint administration with the advice of the eight senior committees shown in Figure 4; their roles can be inferred from their names. The primary advisory body is the Defence Committee. For matters pertaining exclusively to the command of the defence force, there's also the Chiefs of Service Committee. Below the eight higher committees are literally hundreds of subordinate committees, consultative forums and working groups. It's inevitable in such an arrangement

Figure 4: The senior Defence committees



Source: 2009-2010 Defence annual report.

that considerable resources are put into intradepartmental coordination—not to mention endless infighting.

The Defence Committee meets in one of the two pentagon-shaped buildings (no points for originality) on Russell Hill, around the table used by the War Cabinet during World War II at the St Kilda Road barracks in Melbourne. Things must be cosy: while the size of the War Cabinet fluctuated between six and nine members, at last count the Defence Committee had sixteen, or more-or-less one representative from each of the constituent

parts of the organisation. The membership of the committee implies its intent: to provide advice to the Secretary and CDF that captures the views of the stakeholders from around the organisation.

Few private sector firms have such an egalitarian approach to governance, or such an unwieldy executive committee. More usual is a relatively small team selected for their expertise rather than as representatives of internal constituencies. BHP and Woolworths each have seven-member management committees, and Rio Tinto has an

eight-member committee. The Reserve Bank board has only nine members, as does the Standing Committee of the Politburo of the People's Republic of China.

Alternative modes of internal governance are explored in Chapter 5.

Capability planning

The decisions that a government takes about the size and shape of the defence force are the most important decisions that it makes regarding the nation's defence in peacetime. Because a new capability can take more than a decade to plan and then remain in service for another three, capability planning requires forethought and foresight in equal measure. Consistent with this, the 2009 Defence White Paper adopted a twenty-year planning horizon for its Defence Capability Plan.

There's a lot at stake. Current plans include more than \$150 billion worth of equipment acquisitions slated for approval over the next ten years. Apart from the staggering initial price tag, the resulting operating costs will be several times that amount. What's more, these acquisitions will reshape almost every aspect of the ADF for decades hence. At best, poor planning wastes a lot of money; at worst, it can leave the country with inadequate defences.

Sound capability planning demands two things. First, the capabilities sought must be consistent with expected circumstances and our chosen defence strategy. There's no point building a proverbial Maginot Line or, as is sometimes suggested, 'preparing for the last war'. Second, the plan must be deliverable within the resources expected to be available. In this context, resources aren't just money but also the human capital and organisational wherewithal to acquire, develop and crew the capabilities sought.

It will be for history to say whether current plans are appropriate to our future defence needs. If public commentary is anything to go by, the verdict is mixed so far. Some argue that the plans are too ambitious; others believe that they're too modest. In terms of defence administration, the question is how much confidence we can have in the processes used to develop the plans.

Reading the last Defence White Paper, one gains the impression that plans for the defence force are the result of a long process of careful, precise deduction. That's an illusion. Not only are a great many unavoidable judgments made along the way, but there's often an air-gap between the ostensible strategic logic and the concrete capabilities proposed. Moreover, the reassurance offered—that capabilities were tested against secret 'plausible defence planning contingencies'—lends little credibility. It's easy to contrive planning contingencies to justify all sorts of purchases.

The outcomes of the process speak for themselves. Based on the patterns of the past thirty years, the core plans for the ADF are based on replacing what's already there, with some expansion and modernisation as technology and finances allow—exactly what one would expect from a federated organisation that colludes to share the available spoils. Despite the supposed innovations contained in the Rudd government's 2009 Defence White Paper, there is little to distinguish the resulting force structure from that agreed to by the Howard government—apart from an extra six submarines.

Defence effectively has the freedom to set its own course, and doesn't even pretend that it's otherwise. Perhaps from a lack of self-consciousness, Defence's *Capability development manual* relegates the government to the role of 'endorsing'

Defence's plans. So much for civil control. In practice, interventions by the government are rare (although the decision to purchase F/A-18 *Super Hornets* provides a counterexample in which the government saved Defence from its own poor planning and inflexibility).

Moreover, the central agencies of Treasury, Finance and Prime Minister and Cabinet have only a limited influence on defence planning, mainly through limiting the amount of money available. This reflects not only the limited resources they have available, but also Defence's tactical use of the Cabinet process through tardy submissions, voluminous attachments and a heavy veneer of technical jargon.

Whatever the strategic merits of the plans that Defence prepares for itself, they've never come close to being delivered for at least the past quarter-century. One factor has been that governments sometimes renege on promised funding, as occurred soon after the 1987 White Paper and again recently. But that's far from the main cause, especially given that funding was largely kept in line with (or above) expectations from the early 1990s to the late 2000s.

On the contrary, the principal problem is that despite frequent revision Defence's plans have remained financially unaffordable and practically undeliverable: unaffordable because of a systematic tendency to substantially underestimate future acquisition and operating costs, and undeliverable because of unwarranted optimism about the progress of acquisition projects. The result is that Defence is constantly under pressure as it struggles to attain levels of capability that are beyond its reach, and the nation's defences are constantly below what's planned and promised.

The usual excuse for failing to properly anticipate future costs is that it's hard to predict what something will cost before it's

properly and fully specified, but that doesn't explain the sustained bias towards cost underestimation. If costs were simply hard to predict, the result would be a spread of errors that converged on the average. Clearly, something more is happening.

It's likely that costs have been underestimated because of the interplay of three factors. First, industry deliberately misleads Defence about the prospective costs (acquisition and operating) so as to make its products more attractive. Second, Defence misleads itself through the pervasive 'optimism bias' of its executives and project planners (a phenomenon observed equally in private and public sector planning elsewhere). Third, and most important, there are perverse incentives at play that encourage the underestimation of costs.

The game for the military is simple enough: get a project into the plan and chances are that it will someday be brought to fruition. Once a project has been announced—even at the planning stage—governments are loath to incur the political cost of announcing that it will be abandoned. Instead, as cost pressures rise, projects are simply deferred into the future. The air warfare destroyer began as a less than \$4 billion glimmer in the eye of the Navy, and was finally approved as an \$8 billion goliath in South Australia that involved too many parochial interests for any government to reverse.

Given the long gestation of defence projects, those responsible for planning at any point in time are long gone before the effectiveness of their efforts is tested. Then a new generation of planners mumbles something about having to deal with 'legacy projects' and the cycle begins anew. No-one is ever held to account, and the taxpayer is left to pick up the bill.

It was probably in an attempt to curtail that sort of behaviour that the government introduced a 'capped budget' arrangement in

2009 whereby ‘shortfalls against the White Paper funding plan will be offset by Defence’. This is silly. If Defence can somehow find extra money without detriment to capability, it should do so without delay and return the cash to the Treasury. More realistically, it won’t work. Not only does Defence know that the budget is subject to periodic revision as part of a set five-year cycle, but the risks arising from poor planning are ultimately and unavoidably borne by the government. It’s fanciful to think that the government would allow the defence force to wither on the vine to somehow ‘punish’ Defence for poor planning.

As to the affordability of the 2009 White Paper, the signs so far are mixed. Last September, Defence said it had budget pressures, but then handed back \$1.5 billion. Fact is, Defence doesn’t know. In the longer term, however, the situation is less encouraging. Based on historical trends in Australia and other Western countries, the planned long-term annual rate of growth in defence funding (4.7% nominal) is below that needed to maintain, let alone expand, the force.

Force development and acquisition

Few areas of defence activity encounter as many problems or cause as much concern as the acquisition of new equipment. From the saga of the *Collins* class submarines to the cancellation of the *Seasprite* helicopters, governments have had to endure embarrassing headlines about multi-billion-dollar failure. Two major independent reviews in 2003 and 2008 yielded a number of recommendations, most of which were accepted by the government. The most significant and contentious issue arising from the reviews concerns the relationship between DMO and Defence—a topic explored at the end of this section.

To understand the challenges of defence acquisition and the attempts to overcome them, some understanding of the process is needed. In outline, the process has two parts. First, individual projects in the Defence Capability Plan are prepared for government consideration by Defence’s Capability Development Group (CDG). Once a project is approved, the quasi-independent DMO then takes responsibility for working with industry to deliver the equipment to the services that will operate it. In practice, there’s significant overlap between the two parts of the process—usually referred to as the pre- and post-approval phases—and CDG, DMO and the sponsoring service work closely throughout. The reforms resulting from the 2003 and 2008 reviews affect both the pre- and post-approval phases.

In the pre-approval phase, the major innovation has been the creation of a ‘two-pass process’ that ensures that each project is considered at least twice by the government. At ‘first pass’, approval is sought for the broad parameters of the proposal. This includes approving a suitable range of options to develop in parallel, including at least one off-the-shelf option. Well, at least that’s the theory. Until the government reiterated the demand for an off-the-shelf option in mid-2011, Defence routinely watered down the requirement to be an ‘off-the-shelf benchmark’.

At ‘second pass’, final approval is sought to proceed with the acquisition. Between first and second pass, industry is engaged to collect information about the costs, risks and relative advantages of the different options. It’s recognised that substantial amounts of money may have to be spent to achieve this, and approval for this initial expenditure is sought at first pass.

At a minimum, the two-pass process has imposed much greater rigour and discipline

on the development of projects than occurred in the past. For that reason alone, it's been worthwhile. On the downside, the approval of projects now takes much longer than before. And, despite the two-pass process being in place for more than six years, Defence hasn't adjusted its planning accordingly, resulting in mounting delays. It's now clear that the schedule of acquisitions set out in 2009 as part of the White Paper will never be met. Over the past two years, a mere ten projects have received first-pass approval from the government, whereas more than three times that number were planned. To get back on schedule, around fifty-eight projects will have to be approved over the next two years. Given past experience, any hope of that is nothing short of delusional.

Changes to the post-approval phase have centred on the re-establishment of DMO as a quasi-independent agency, which occurred in 2005. Although several benefits were anticipated, the key goal was to free DMO from the bureaucratic strictures of the public service so that it could take a more commercial approach to its work. To some extent, this has been successful. DMO has made progress in boosting the professional qualifications of its workforce, and some key personnel—including the CEO—have been recruited from the private sector. More generally, however, the adoption of commercial practice has been impeded by the retention of a largely public service workforce that is managed as such.

Both the 2003 and the 2008 reviews of defence procurement recommended making DMO a fully independent agency. Although that would allow the organisation to take a more businesslike approach, it would have the serious drawback of complicating close cooperation with Defence. It's not surprising that governments have twice rejected this proposal. Frustratingly, it hasn't so far been possible to find a middle path that keeps DMO

close to Defence but gives it the freedom to manage its workforce and actions in a manner more akin to the private sector.

But some realism is needed. Even if a more businesslike approach were achieved, defence projects would continue to falter, all other things being equal. For every defence project that runs off the rails, there's a private sector company that bears *at least* half the responsibility for the problem. Remodelling DMO along private sector lines would at most ensure that it struggled on a par with its manifestly fallible private sector suppliers. The inescapable reality is that many defence acquisitions are inherently risky endeavours, and no amount of tinkering with DMO will change that. Make no mistake: it's worth continuing with reforms to the DMO, but it isn't a path to nirvana.

The experience of the past two decades is remarkably clear: developmental and 'Australianised' defence projects are much more risky and costly than off-the-shelf purchases from overseas. For that reason, the vast bulk of the risk in a project is predetermined before it gets to DMO. Recent experience with the rapid and successful acquisition of the *Abrams* tanks, C-17 transport aircraft and F/A-18 *Super Hornets* contrasts markedly with the long and costly struggles with bespoke projects such as the *Wedgetail* airborne early warning and control aircraft, FFG frigate upgrades and the upgrade of the high-frequency communications network.

If the government wants to equip the ADF on time and budget, the solution is simple: eschew developmental and politically expedient local projects in favour of proven equipment from overseas. And sophistry about the meaning of 'off-the-shelf' has to end. To draw an analogy, consider buying a car. 'Off-the-shelf' means buying a proven car from an existing factory; 'based on an off-the-shelf design' means building a

new factory to build a car adapted from an existing design. This is what we're doing with the air warfare destroyer, at a very substantial premium.

Finally, there's the issue of contestability. In the past, acquisition proposals were analysed and actively contested within Defence. That no longer occurs, for the reasons explained above. Nor are any of the central agencies able to provide effective oversight of projects submitted for approval. In theory at least, DMO provides independent advice on the project and commercial risks attendant to proposals, but it's hard to confirm whether that continues to be the case because the last publicly released ministerial directive to DMO dates from 2008.

4 Closing the loop

The secretive agent

It's unlikely that US economist Joseph Stiglitz has many friends at the Pentagon. In 2008, he published an estimate of the cost of the Iraq War that came out at an eye-watering, headline-grabbing \$3 trillion. More recently, he's been lobbying for a big cut in defence spending to help balance the US budget. But it's his earlier work, for which he shared the Nobel Prize in 2001, that's relevant to the control and administration of Defence.

Stiglitz and his colleagues explored the consequences of imperfect and asymmetric information in markets. Stiglitz, in particular, argued the importance of what's become known as *information economics* to the public sector, including defence. In doing so, he's built upon work going back to the 1960s on what's known as 'the principal-agent problem'.

Problems arise when one party (the agent) undertakes a task on behalf of another (the principal) and two conditions are met: first, the principal and the agent have different

priorities; second, the principal cannot easily monitor the agent's characteristics or performance. The latter condition amounts to 'information asymmetry' in the agent's favour.

When a principal-agent problem arises, the lot of the principal is an unhappy one. To start with, they risk choosing the wrong agent, paying too high a price, or both. Economists call this 'adverse selection'. Then, having chosen an agent, the risk becomes that incomplete monitoring will tempt the agent to pursue their own goals at the principal's expense. Economists label this evocatively as 'moral hazard'.

Principal-agent problems arise frequently in the private sector, for example between shareholders and company executives, customers and suppliers, employers and employees, and home sellers and real estate agents. In each case, agents have the opportunity to exploit an information asymmetry to take advantage of the principal. Understandably, therefore, agents strive to increase information asymmetry by withholding information and, where possible, promoting disinformation. Society tries to check this power where it can. For example, consumer law works to reduce information asymmetry by enforcing the disclosure of information and prohibiting misleading claims. In the same vein, financial regulators strive to ensure timely disclosure and prohibit insider trading.

Principal-agent problems can also arise in the public sector, and Defence is a prime candidate. Not only does Defence escape the direct public scrutiny afforded to portfolios such as health and education, but it's further insulated by the inherent difficulty of measuring its performance. And, to make matters worse, a great many aspects of Defence's costs and performance are shrouded—rightly or wrongly—in secrecy on

the grounds of either commercial confidence or national security.

As a result, Defence is like a Russian *babushka* doll of principal–agent problems: between the government and the diarchy; between the diarchy and the services; between the services and the support programs; and between the support programs and external suppliers. Moreover, although principal–agent problems routinely arise between the electorate and the government, they can be especially acute when it comes to defence matters. No clearer example has arisen recently than the questionable justifications given by the Australian, British and US governments for the invasion of Iraq in 2003.

Before discussing what can be done to mitigate principal–agent problems, it’s worth pausing to understand why the problem can be expected to arise in a defence context—if only to make sure that we’re not tilting at windmills. In some cases, the problem is clear because of the essentially commercial nature of relationships. This applies within Defence and between Defence and its external suppliers. What’s less clear is why priorities might differ between the government and Defence.

The first reason is laziness. In the commercial world, agents seek to maximise the benefits they get from trading with principals. The benefits need not be restricted to financial profits. For example, in addition to high profits, monopoly suppliers enjoy the benefit of not having to strive for efficiency or even to maintain quality. They can choose the mix of rewards they want.

So, while it’s undoubtedly in the government’s interest for Defence to be efficient, the converse is true within Defence. It’s always easier for managers to do less with more than the other way around. And, given the opportunity to evade monitoring, the easier course of action will be chosen every time—

a trend reinforced by the absence of a profit motive in the public sector. If there was ever any doubt about Defence’s indifference to costs, the egregious inefficiencies revealed by the 2008 Defence budget audit stand as testament to it.

A further misalignment of priorities arises because Defence and the government will often weigh both costs and benefits differently. Consider the purchase of a piece of military equipment. For the government and the community, every dollar spent on defence equipment comes at the opportunity cost of an alternative benefit, such as better health, better education or reduced taxes. Things look rather different from Defence’s perspective. Although it faces an opportunity cost in the form of alternative defence purchases forgone, this is softened considerably by the prospect of securing additional funding from the government at a later date. All other things being equal, Defence will be willing to pay more for any given purchase than the government. And, as explained in the previous chapter, a ‘capped budget’ will at best only be partially effective as a countermeasure.

Differences also arise in judging prospective benefits. Every defence purchase has to balance costs against the additional ‘capability edge’ that better (and invariably more expensive) equipment provides. In most cases, a compromise is reached between cost and performance. Despite reassuring claims to the contrary, the ADF doesn’t get the best equipment that money can buy. If it did, decisions about defence purchases would be much easier than they are. Instead, and consistent with government policy, the military get what’s ‘best value for money’. But value for money depends critically on the value placed on the marginal differences in performance between competing options, and the perceived value of better performance grows with proximity to the use of an item of military equipment in action.

The combined effect of each party weighing costs and benefits differently is that the military will usually pick a point much further along the curve of diminishing returns (and rising costs) than the government would if it were given access to all information. Hence the succession of very risky projects pursued to the government's retrospective frustration.

Finally, the defence services often have their own goals and aspirations, independent of broader strategic priorities and the government. In a way, it would be disappointing if that were otherwise. The Army, Navy and Air Force are all proud organisations with long histories and legacies to protect, and those characteristics are essential to their effectiveness as fighting forces. But that also means that they're far from indifferent to any plan affecting them. In general, they're inherently averse to reductions in the size, diversity and sophistication of their capabilities and equally attracted to growth on all three fronts, not just because they want to be ready to do what might be asked of them—though that's important in their thinking—but also because of 'self-respect' relative to foreign armed forces. As one officer put it to the author recently, if the RAN did not have submarines, it would be a laughing stock, quite apart from whether there was a strategic imperative to be met.

The critical role of information

By its very nature, the principal-agent problem can be ameliorated by either aligning interests or by reducing information asymmetry. Greater alignment of interests can in principle be achieved through tighter control and incentives—possibilities explored in the next chapter. The remainder of this chapter focuses on how the information asymmetry between the government and Defence can be reduced. As it turns out,

fixing the problem at that level necessarily entails reducing information asymmetries elsewhere, including between the public and the government. Specific issues about information asymmetries and the monitoring of performance within Defence are deferred to the next chapter.

What follows rests on two propositions. First, although greater openness on defence issues is critical, it must be accompanied by analysis to be effective. Opening the floodgates currently holding back data will not solve the problem unless sense can be made of the torrent. Second, the government can't hope to properly monitor Defence's performance by itself, and should therefore make use of third parties wherever possible to assist with analysis.

The importance of external monitoring is hardly a revelation. It's rare for more than a few months to pass before the Defence Minister announces yet another external review of some aspect of Defence. Moreover, our system of government has evolved interlocking layers of monitoring, from the central agencies within government through various statutory authorities to the parliament itself. The government's ability to control Defence effectively hinges on how well those and other external bodies assist it. The remainder of this chapter surveys the various avenues that can assist the government to monitor Defence's performance. The limitations facing the central agencies won't be restated here. Suffice to say, they have very limited scope to counterbalance Defence at the Cabinet table.

Beyond a certain level, questions about Defence's performance are indistinguishable from questions about the government's performance. This is especially true from the perspective of the parliament, to which we now turn.

The Australian Parliament

In the Westminster system, governments can be called to account in the chambers of the parliament. Questions can be asked and statements can be made under the protection of parliamentary privilege. In practice, parliamentary debate is often unruly and at times unedifying, although when it comes to defence matters a higher standard of decorum sometimes prevails. In recent times, the Australian Parliament has directly engaged itself on the subject of Australia's involvement in the Afghanistan War. Beginning in 2008, the Defence Minister has made several formal progress reports on Afghanistan, and in late 2010 a parliamentary debate about Afghanistan was held over four sitting weeks. In each case, the public and the parliament were given the opportunity to reach a more informed view on Afghanistan than had previously been the case—an information asymmetry was reduced.

More generally, scrutiny of defence matters occurs through three parliamentary committees: the Parliamentary Joint Committee on Foreign Affairs, Defence and Trade and the two Senate standing committees (References and Legislative) on Foreign Affairs, Defence and Trade. The joint and Senate references committees conduct inquiries into matters referred to them by parliament. In the case of the joint committee, the referral occurs in practice via the relevant minister. The joint committee also examines matters arising from annual reports of agencies and reports from the Commonwealth Auditor-General.

In addition to conducting inquiries into specific legislation referred to it by the Senate, the Senate legislative committee oversees the performance of agencies by scrutinising their Budget estimates and annual reports. It's through that mechanism that the parliament directly oversees Defence on

an ongoing basis. Two or three times a year, officials from Defence assemble in one of the committee rooms in Parliament House to answer questions from the committee. Each session typically stretches for one or two days, sometimes longer. Much of what's known about Defence's performance and spending comes from the inquiries undertaken.

But the process isn't perfect, and it certainly doesn't compare with the forensic scrutiny of the committees in the US House of Representatives and Senate, which are supported by dedicated staffs. Consequently, the Australian committees begin each hearing with at best an incomplete picture of what the important issues are, and hearings often take the shape of a fishing expedition. At other times, leaks or official disclosures allow a much more efficient and directed inquiry.

In their dealings with the committees, Defence officials are scrupulous in their honesty but almost never forthcoming with more than they are asked for.

Committee inquiries resulting from references are much more focused affairs, beginning with formal terms of reference and ending in tabled reports in parliament. Table 3 lists some recent inquiries by the joint and Senate committees pertinent to Defence. Because the inquiries are referred by the parliament, they reflect what are perceived to be the important issues of the day. Moreover, by seeking evidence from a wide range of sources, the inquiries are usually well informed.

As a general observation, committee reports tend to have a much greater impact when dealing with personnel matters than they do when they deal with strategic or force structure issues. Perhaps this is because it's more difficult for the government and Defence to claim secret knowledge or unique military insight when it comes to treating people fairly. Whatever the reason,

Table 3: Current and recent parliamentary committee inquiries into Defence

| Parliamentary Joint Committee on Foreign Affairs, Defence and Trade | Senate standing committees on Foreign Affairs, Defence and Trade |
|--|--|
| Inquiry into RAAF F-111 deseal–reseal workers and their families (Completed June 2009) | An equity and diversity health check in the Royal Australian Navy—HMAS <i>Success</i> (Underway) |
| Inquiry into Australia’s regional strategic defence requirements (Lapsed on the prorogation of the 41st Parliament) | The Department of Defence’s request for tender for aviation contracts and associated issues (Underway) |
| Inquiry into Australian Defence Force regional air superiority (Completed September 2007) | Procurement procedures for Defence capital projects (Underway) |
| Australia’s defence relations with the United States (Completed May 2006) | Australia’s involvement in peacekeeping operations (Completed August 2008) |
| Report of the delegation: Visit to Australian Defence Forces deployed to support the rehabilitation of Iraq—22 to 28 October 2005 (Completed May 2006) | Blue water ships: consolidating past achievements—Inquiry into naval shipbuilding in Australia (Completed December 2006) |
| Australia’s maritime strategy (Completed June 2004) | Duties of Australian personnel in Iraq (Completed August 2005) |
| Rough justice? An investigation into allegations of brutality in the Army’s parachute battalion (Completed April 2001) | Inquiry into the effectiveness of Australia’s military justice system (Completed June 2005) |

Source: Australian Parliament House website

the committees have had a real influence over defence personnel issues. The best example is the 2005 Senate committee inquiry into military justice; almost all of the recommendations it made were accepted by the government and translated into legislation. Four subsequent hearings by the committee then oversaw the implementation of the new arrangements in Defence.

The question is: could greater parliamentary oversight be useful in other areas? The obvious candidate is defence procurement, and the terms of reference for the current inquiry into procurement procedures for Defence capital projects asks that very question. Given the billions of dollars and the defence outcomes at stake, the case for dedicated parliamentary oversight is strong.

Call in the auditors

The Australian National Audit Office (ANAO) provides the parliament with independent assessments of public sector financial reporting, administration and accountability.

This is accomplished through two largely separate activities: performance audits and financial statement audits. Financial audits provide assurance that the financial statements of agencies are materially correct. From 2001–02 to 2006–07, Defence suffered the embarrassment of having its financial statements qualified by the ANAO. In the absence of independent financial auditing by the ANAO, it’s unlikely that Defence would have taken the remedial steps it has to fix its accounts (although, as noted above, the issues were less pressing than first appears).

The performance audits undertaken by the ANAO are even more relevant to this discussion. Performance audits examine activities within agencies in detail to determine whether they are efficient and effective. The ANAO annual audit program is developed in consultation with parliament, and individual audits result in reports to parliament. Recent and current performance audits of Defence are listed in Table 4. In addition, an annual audit of the top major defence projects results in the *Major projects report*.

Table 4: Current and recent ANAO performance audits of Defence

| Audit | Status |
|---|-------------------------|
| Operational release of Navy major systems | Underway |
| Mechanisms for capturing and communicating lessons from operational activities in the ADF | Underway |
| Explosive ordnance services contract | Underway |
| Accountability for explosive ordnance held at ADF units | Completed April 2011 |
| Information and communication technology strategic planning | Underway |
| Defence's management of health services to ADF personnel in Australia | Completed June 2010 |
| Contracting for defence force recruiting services | Completed June 2010 |
| Army Individual Readiness Notice | Completed June 2010 |
| Lightweight Torpedo Replacement Project | Completed May 2010 |
| Procurement of explosive ordnance for the Australian Defence Force | Completed March 2010 |
| Garrison support services | Completed November 2009 |

Source: Australian National Audit Office website

The ANAO is able to undertake performance audits to a high level of detail because it has extensive powers of access. Its officers can literally go through files to see how decisions were reached and confirm whether processes were followed or ignored. It's common for ANAO reports about Defence to make headlines. For example, last year's audit of the Lightweight Torpedo Replacement Project led to the headline 'Defence bungles \$400m torpedo project' in the *Adelaide Advertiser*.

Despite the embarrassment routinely caused by ANAO performance audits, Defence often concurs with their conclusions and the government frequently accepts their recommendations. Even so, the ANAO has its limitations. To start with, it has the capacity to cover only a limited number of areas in Defence in any given year. Moreover, it faces the inherent difficulty of penetrating the often technical and always arcane realm of the military. And, as with parliamentary committees, Defence is cooperative rather than forthcoming in its dealings with the ANAO.

Academics, think tanks and commentators

Unlike the US, Australia has relatively few independent think tanks or similar entities working on defence issues. Apart from ASPI, the ones that come most readily to mind are (in alphabetical order) Air Power Australia, the Australian Defence Association, the Kokoda Foundation, the Lowy Institute and the Williams Foundation. In addition, several university-based bodies take an ongoing interest in defence affairs, including the Strategic and Defence Studies Centre at the Australian National University, the National Security Institute at the University of Canberra, and the Centre for International Security at Sydney University.

As a result, the opinion pages of Australian newspapers rarely want for wise counsel on what's right and wrong about Defence and defence policy. If nothing else, the enthusiasts, ex-officials and academics who make up the field keep the public debate bubbling along. Contributions of genuine quality borne of careful research and analysis emerge from time to time.

Nonetheless, the amount of independent work actually done on Defence's performance and defence policy, as opposed to larger geopolitical issues, is limited. Almost all of the think tanks and academic centres mentioned devote some if not most of their energy to issues such as foreign policy and international affairs.

But probably the greatest impediment to informed independent analysis comes from the paucity of information. In most cases, academics and think tanks depend on official disclosures and revelations from parliamentary committees and ANAO audits. This contrasts markedly with the situation in the US, where independent analysts are often given access to information and assisted to take fact-finding tours in conflict zones.

The media

It's unlikely that many members of the public eagerly await the next instalment of Hansard from the Senate Legislative Committee on Foreign Affairs, Defence and Trade, or race to download the latest ANAO report on army boots. Equally, it's unlikely that more than a couple of thousand people will ever read the words on this page (though I live in hope). Instead, most people rely on the media to sort through the mountains of published dross to find out what's important and to tell them. Of course, the media do more than that. They also utilise leaks—deniable official disclosures and malicious tip-offs alike—and they solicit answers from politicians and officials to the questions of the day. Ultimately, the media tell the public what's happening.

In addition to the general media, there are also a number of specialist defence publications, often referred to as the 'trade press'. They include the *Australian Defence Magazine*, the *Australian Defence Business Review* and the *Australia–Pacific Defence Reporter*.

Sometimes the media get things wrong about defence, but mostly they get things right. Over the past decade, there have been surprisingly few outright deliberate 'beat-ups' about Defence, although there have been some. Most of the time, Defence is a rich source of newsworthy stories requiring no embellishment or exaggeration. Troubled acquisition projects are rarely far from the headlines, and once problems emerge in a project, the media and Senate committees take turns uncovering the details, to the dismay of Defence and the government.

Of course, the most newsworthy issue of the day is the war in Afghanistan. Over the past few years, access for Australian journalists has improved, although compared with the level of access accorded journalists embedded in US military units the Australian media is less able to report on the day-to-day life of our troops in Afghanistan.

Relations between the media and Defence are rarely smooth. Journalists have even been known to write about the unresponsiveness of Defence Public Affairs out of frustration. Stories of long waits for answers to even the most trivial questions are legends among journalists. Such delays have nothing to do with the expertise or attitude of those at the end of the phone; rather, they reflect the extraordinarily tight control of any statements emanating from the department. In many instances, stories would be more balanced, or at least better informed, if Defence engaged more closely with the media.

Defence, for its part, complains that the media focus only on negative stories at the expense of the many real achievements there are. In part, Defence has a point, but only because negative stories are intrinsically more newsworthy than positive ones. It's naive for Defence to think that it's going to get traction from the opening of a vehicle wash point on an army base, or by creating a dedicated

web page for Sarbi the long-lost explosives detection dog who found her way home in Afghanistan.

The media perform an essential role. They're the glue that connects the many disparate sources of information about Defence, and the lens through which the public learns what's happening. More than either of those things, they're the critical nodes in a network of oversight that underpins civil control of the military and the accountable administration of Defence.

Officials' secrets

The ability of any third party to oversight Defence depends critically on the availability of information. Apart from the powers of access granted to the ANAO, and to an extent parliamentary committees, none of the entities mentioned so far have the ability to look behind the curtain of secrecy enveloping Defence.

To some extent, that's inevitable. Many things going on within Defence are concealed for good reasons. Sometimes, it's to preserve our operational advantage against potential adversaries by withholding sensitive details about our military capabilities. In other cases, concealing our true thoughts and intentions allows us to avoid diplomatic embarrassment—a reality all too apparent from the recent Wikileaks experience. And sometimes it's to preserve commercial confidences that have been shared in good faith.

Even with these restrictions in place, Defence manages to produce a lot of public information, both on its own account and on behalf of the government. In recent years there have been notable improvements in several areas. The progress of approved major defence projects is now reported more comprehensively and in greater detail than in the past. The Defence annual report has also

grown over the past decade to include, among other things, a wider range of personnel statistics. Recent changes to freedom of information arrangements have also improved access to documents by the media. And even with the heavy-handed redaction that tends to take place (see Figure 5), the public is better informed as a result. Yet we are left to wonder why the public can't be apprised of Defence's management of financial pressures and concerns about its 'body image'.

Without doubt, the most noticeable improvement has occurred in transparency about operational matters. Apart from the already mentioned periodic statements to the parliament by the minister about progress in Afghanistan, the department provides ongoing updates about operations soon after events transpire. This can't be easy; the correct balance between personal privacy, operational security and the public interest is rarely obvious.

Yet, despite these many improvements, it's hard to escape the conclusion that Defence also uses secrecy to conceal errors, hide inefficiencies and more generally evade scrutiny. In fact, in recent years disclosure has diminished in a number of areas critical to judging Defence's performance. Specifically, it's very difficult to assess both the year-to-year costs and the performance of the ADF, as well as the affordability and progress of long-term plans for the force. In each case, critical pieces of information that used to be available are now withheld.

To begin with, the level of detail on the performance of the three services has fallen since 2009. Rather than report on each of the constituent parts of a service (such as, for example, submarines and surface combatants in the case of the Navy), reporting has been aggregated up. As a result, we've moved from twenty-two capability output reporting

Figure 5: An inexplicably redacted page from the 2010 Incoming Government Brief released under freedom of information guidelines

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Defence Funding Over the Long Term

Chapter 6


Operating Expenses

6.20 ~~(C)~~ Defence's operating budget represents the non-personnel/non-capital cost of delivering Defence capability. The majority of expenditure relates to the maintenance and support costs for Defence assets. The remainder relates to garrison support, estate management costs, information technology, delivery of intelligence capabilities, research and development costs, Human Resource management and financial management costs. There is little flexibility in this element of the budget. Additional Release

STRATEGIC REFORM PROGRAM (SRP)

6.21 (U) Defence has initiated a major reform program that will deliver gross savings of around \$20 billion over the decade. SRP savings will be supplemented by further savings initiatives, reprogrammed funds and by new funding from the government to provide nearly \$45 billion in total for investment in new initiatives.

MANAGEMENT OF DEFENCE'S FINANCIAL PRESSURES

 S47C(1) & 47D
The CFO Group will continue to support effective budget management across Defence and pursue significant reforms across the finance functions. Additional Release

'FAT AND BLOATED' PERCEPTION OF THE DEFENCE BUDGET

6.23 (U) Defence consumes approximately 9 per cent of government outlays and is typically seen either as largely discretionary spending or at least more capable of being financially reshaped than other government agencies. Indeed there still exists a view that despite the \$44.9 billion of funds reinvested in the 2009 Defence White Paper, \$20 billion (gross) of which were identified in the Pappas Audit, there still is "plenty of fat" within Defence. These views, although ill-conceived, render Defence an obvious a target for any major budget reshaping.

 S47C(1)

streams to three. Even prior to 2009, the level of reporting was sparse: basic information, such as the number of days vessels spend at sea, was lost in 1997, leaving only the less revealing ‘unit ready days’—the number of days a vessel *could* have been taken to sea.

The situation isn’t much better when it comes to understanding costs. Repeated changes to the structure of the public Defence budget have made it all but impossible to track how costs are changing over time at other than the highest level. And it’s impossible to know how much money is being spent on domestic travel or reserve training, for example. Apart from making it difficult to assess the efficiency of the department, this prevents the external verification of more than \$20 billion in savings being claimed under the Strategic Reform Program.

Despite repeated claims that the 2009 White Paper is fully funded and affordable, basic financial information about long-term funding and about the cost of proposed major capabilities—even in broad terms—is also kept secret. (For example, there’s no official estimate of the cost of the future submarine project beyond the Defence Capability Plan’s figure of ‘greater than \$10 billion.’) Not only does this make it hard to assess the prospects of delivering the much-vaunted Force 2030, but it’s a marked departure from the transparency accompanying the 2000 White Paper.

A similar erosion in transparency occurred in the Defence Capability Plan over the period from 2001 to 2009, with progressively greater clouding of both schedule milestones and cost estimates. Although an independent external review in late 2009 recommended substantially greater transparency, only marginal improvements resulted. As things stand, the cost of a planned project can increase by hundreds of millions of dollars and its timing can slip by years, without the taxpayer being any the wiser.

Risk and reward

Defence ministers face a dilemma. If they encourage external scrutiny, they risk being embarrassed from the start. If they limit external scrutiny, they risk potentially greater embarrassment in the longer term. Neither course of action is risk free, but the former has the merit of uncovering problems earlier and generating a wider range of potential solutions. There’s much to recommend in that approach.

No minister can hope to be omniscient of all that’s going on across the length and breadth of Defence; nor can Defence be relied upon to give timely or dispassionate advice about itself on every occasion. As in any other area of public administration, openness will always yield better results in the long term. Woodrow Wilson, who before becoming US President was a scholar of governments and national constitutions, put it thus: ‘Government ought to be all outside and no inside.’

5 Defence reform

The most visible aspect of the Strategic Reform Program (SRP) is the decade-long \$20.6 billion savings program. On the surface, this would appear to be a massive impost on an organisation under pressure, but that needs to be put in perspective. Roughly \$5 billion of the claimed savings results from nothing more than shifting money from one budget category to another. Even taking the \$20.6 billion at face value, that’s about the same as would be delivered by a compounding annual budget cut equal to the 1.2% efficiency dividend imposed on the running costs of almost every other Australian Government agency.

When all’s said and done, Defence is probably under no greater budget stringency than the Department of the Environment or the National Gallery of Australia—especially once it’s remembered that Defence’s workforce

and budget are continuing to grow. So how are they going to make savings? Here lies the genius of the SRP: the savings represent hypothetical cost reductions relative to a counterfactual baseline that Defence constructed for itself. Of course, the fact that it's now handing back money hand over fist, above and beyond the SRP, makes a mockery of the baseline against which savings are being claimed.

Be that as it may, for the purpose of this discussion the size and credibility of the savings program is of only passing interest. What really matters are the substantive changes being made under the SRP to the way Defence does its business. Savings programs come and go; much like mowing the lawn or weeding the garden, they're something that needs to be done from time to time.

There are sixteen 'reform streams' in the SRP—eight savings streams and eight non-savings streams. All of the streams make sense, and there's even evidence that substantive savings are actually being made in several areas. Improvements are planned in activities ranging from preparedness planning to capability development, and in areas from IT infrastructure to logistics warehousing. All the signs are that Defence will benefit significantly from the initiatives underway, but the SRP holds less certain promise on the fundamental underlying issues of governance and accountability. In particular, the idea of moving to an 'output focused' budget model giving more control to the output programs appears to have foundered.

Reforming an organisation of the size and diversity of Defence is a potentially massive task with myriad possible detailed changes, but four key imperatives emerge from the preceding discussion—one each in the areas of accountability, governance, transparency and contestability. The remainder of this chapter outlines those imperatives before

concluding with some thoughts on driving reform in Defence.

Devolve authority and accountability

The command economy model of Defence administration has failed. Authority and accountability for the delivery of Defence's capability outputs should be devolved to those now nominally responsible.

Activities for which consolidation doesn't clearly result in reduced overheads or economies of scale should be returned to the individual services, along with all associated funding, personnel and infrastructure. Activities retained for shared delivery should be only those for which economies of scale are available or pooled expertise is needed. This would include equipment and facilities acquisition; legal, financial and personnel services; and most of what's currently done under the Chief Information Officer.

However, wherever possible, non-investment activities currently undertaken by support programs on behalf of the services should be put under the control of the services. Garrison support would be a prime candidate to return to the services, leaving the Defence Support Group to manage major capital facilities projects and assist the services to strike and manage garrison support contracts.

It's less clear what to do with materiel sustainment. There are clear advantages in integrating sustainment and acquisition activities, so even though returning materiel sustainment to the services would clarify accountability and allow DMO to focus on acquisition, it would be likely to add costs and reduce effectiveness overall. Care is required.

At a minimum, sustainment should be based on explicit financial agreements between the services and DMO that compel the services to take responsibility for sustainment-related

expenditure and outcomes. As a next step, the executives in DMO who oversee sustainment should be made ‘double hatted’—accountable to both the relevant service chief and the head of DMO. While such an arrangement is manifestly awkward, it’s preferable to the present situation that sees DMO and the services pointing fingers at each other as capability falls between the gaps. It would be better to double up on accountability than to continue with the amorphous approach that allowed the ADF’s amphibious lift capability to collapse without warning in early 2011.

More generally, devolving authority and accountability to lower levels would give commanders manageable spans of responsibility and the control of the resources needed to get the job done. It shouldn’t be assumed that the basic business units of devolved authority and accountability are necessarily the existing military services. Within the Navy and Air Force, and in parts of the Army, there are what’s known as ‘force element groups’, which are ready-made for direct local administration. Examples include the Army’s helicopter capabilities, the Navy’s submarine force, and the Air Force’s air transport fleets.

Strengthen central strategic control

The great irony of Defence is that it lacks a clearly identifiable corporate headquarters. Defence administration isn’t so much exercised as it’s an emergent property of processes and committees. This limits the ability of the CDF and Secretary to run the organisation and ultimately erodes ministerial control.

The SRP proposes strengthened internal control through the development of key performance indicators. That’s good, as far as it goes, but it needs to be accompanied by arrangements that put control of the

organisation directly into the hands of the Secretary and CDF. The problem is that Defence lacks a governance infrastructure commensurate with its size and complexity.

Two key steps need to be taken. First, the current Defence Committee should be replaced (not augmented) by a smaller body that brings together real expertise rather than representing organisational fiefdoms. Second, a headquarters needs to be created to bring together all the planning and reporting activities currently spread across the organisation. The headquarters would naturally work for the Secretary and CDF and be run on a day-to-day basis by a Chief of Staff or Chief Administrative Officer. The key job of the headquarters would be to allocate resources to and manage the performance of the rest of the organisation. Risk management would be a core discipline.

With a headquarters in place, the Secretary and CDF could then impose a regime of performance management and accountability across the organisation. Output programs (and, where applicable, force element groups) would be given budgets and performance targets to meet. For the military outputs, the performance targets would mainly relate to preparedness. Indeed, preparedness would become their organising principle. Then, to the extent allowed by legislation, individual rewards and sanctions could be used to drive performance.

The need for stronger central control is independent of any decision taken about devolving authority and accountability. In fact, if the current command economy is retained, the complexity of the task strengthens the argument for stronger central control and increases the extent of what’s needed. Whatever course is taken, there’s an urgent need to remediate Defence’s financial and management information systems. Recent events have revealed that Defence has

an unacceptably poor understanding of its costs and non-operational business.

Of course, any discussion of stronger central control raises the question of what's to be done with the currently quasi-independent DMO. Many external commentators—and two independent reviews of defence procurement—argue that greater independence is needed in order to allow DMO to develop the commercial acumen and skilled workforce it needs. Those closer to Defence tend to argue that DMO should be brought back into the department.

One thing's certain: making DMO more independent (that is, turning it into an executive agency) can probably be discounted from the start. There's significant tension built into the relationship between Defence and DMO at present, which greater separation would only exacerbate. Moreover, greater separation would impede the sort of close and successful cooperation between DMO and the services demonstrated in recent rapid acquisitions. The practical options are to either leave DMO as it is (that is, as a prescribed agency) or reabsorb it into Defence.

Whatever approach is taken, the focus should be on the outcome of building the skills and expertise in DMO to protect the Commonwealth's interests. A big part of that depends on being able to compete in the marketplace for legal, commercial and technical expertise. Although the Public Service Act provides considerable latitude to agencies to accomplish that, the upskilling of the workforce in DMO has been slower than most observers originally expected. It's unclear where the impediment has arisen, but it needs to be removed.

Moreover, the upskilling of DMO needs to be accompanied by a parallel program in the capability development area of Defence.

There's no point having a world-class acquisition agency delivering plans hatched by well-meaning amateurs. Unfortunately, that's what we have now. The projects making up the multi-billion-dollar acquisition program for the ADF are mostly developed by relatively junior military officers on short-term postings from their day jobs in the services.

Re-establish internal contestability

The underlying rationale for joint administration has been lost. All signs are that the military and civilian folks in Defence work in close cooperation under a mutually agreed division of labour. When put that way, it almost sounds like a good thing, and in most instances it is. A great many tasks can and should be pursued by bringing together the varied expertise of those in Defence irrespective of their uniform or lack thereof. But if that's all there is to it, the Secretary could be done away with tomorrow and the CDF left in sole charge.

Implicit in the notion of joint administration is the dilution of military self-interest through the presence of a civilian officer equal in authority to the CDF. That intent's been diminished greatly since the late 1990s for the reasons and in the ways outlined in Chapter 2. To redress the situation, three things need to occur.

First, independent civilian analysis of force structure plans and of individual capability proposals needs to occur. No plan or proposal should go to government without having been robustly contested and 'red teamed' within Defence. Further details on how that might be accomplished can be found in a recent ASPI publication, *Let's test that idea: contestability of advice in the Department of Defence*.

Second, an independent microeconomic analysis unit needs to be set up within the

(hopefully to be established) headquarters—probably under a Chief Defence Economist. The role of the unit would be to record, measure and benchmark the efficiency of activities undertaken on an ongoing basis in Defence. Naturally, the unit would play a key role in performance management. To be clear: the role of Chief Defence Economist is separate and distinct from that of the Chief Financial Officer.

Third, a greater effort needs to be put into the professional development of and succession planning for civilian officers, at least commensurate with that for military personnel at similar levels. There's little doubt that the long-held notion that generalist APS executives can take on any role fails in Defence. The goal should be to ensure that senior civilian positions in Defence are filled by people with a strong understanding of the complexities of defence policy and the defence force. Unless that occurs, it's impossible to achieve effective oversight or contestability. Unlike other departments such as Foreign Affairs and Trade, it's rare for Defence to have 'one of its own' appointed to the role of Secretary. Given the large number of senior executives in Defence, this says something worrying about the organisation's ability to nurture and develop civilian leadership.

Increase transparency and strengthen external scrutiny

No matter how robust contestability becomes inside Defence, there'll always be a need for external scrutiny. To conclude otherwise would be to ignore the underlying ideas that our system of government is built on. Because public scrutiny involves a network of actors who leverage each other's efforts, an improvement to any one of them helps all the others. A deepening of parliamentary scrutiny of defence acquisition projects would be a welcome development.

On the whole, the effectiveness of external scrutiny is limited mainly by the availability of information, rather than by the number or size of the actors involved. A country of our size doesn't need any more defence think tanks or better funding for academic research on defence. Instead, we need reliable information about Defence's costs, performance and activities. Make that available and all the rest will follow. By allowing unnecessary secrecy about Defence, the government robs itself of the benefits of independent analysis and leaves itself captive to acting on what Defence chooses to reveal to it.

Driving reform

The four recommendations set out above would be difficult for any government to drive through. It's a much more ambitious program than the Strategic Reform Program. Many of the changes would see power within the organisation shift significantly, resulting in bureaucratic winners and losers. In addition, tighter checks would be placed on the ability of the military to set its own agenda. Perhaps most difficult for the government, greater openness would almost certainly result in greater embarrassment—at least in the short term.

However, with a defence budget of over \$26 billion a year and the nation's defence at stake, something needs to be done. Present arrangements have led to gross inefficiencies in the delivery of today's defence force and faltering progress in building tomorrow's.

The time for tinkering is over. Bold steps need to be taken.

Sources

Hyperlinks to almost all of the sources can be found in the PDF of this paper, available at www.aspi.org.au. For that reason, abbreviated references have been provided for web-based sources. A number of entities and publications mentioned in the text haven't been reproduced below because they can be easily found with an internet search engine.

Chapter 1

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Chapter 2

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Chapter 4

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