

Senate Economics References Committee

Inquiry into Australia's sovereign naval shipbuilding capability –
07 September 2020

ANSWER TO QUESTION ON NOTICE

Department of Defence

Topic: SERC – Q17 – 07 September 2020 – 30 per cent increase in cost in the Future Frigate Program – Gallacher

Question reference number: 17

Senator/Member: Alex Gallacher

Type of question: Written

Date set by the committee for the return of answer: 21 September 2020

Question:

Please provide a breakdown of the factors behind the increase in the cost of the Future Frigate program by 30 percent in two years, from \$35 billion in 2018 to \$45.6 billion in the recently released 2020 Defence Force Structure Plan?

- a. Defence recently told The Australian that this increase was the result of a “longer, more feasible and sustainable vehicle build schedule”? Please explain how the schedule is longer, by how much, when this decision was made and why it was necessary?
- b. On notice, please provide an indicative schedule for each of the key milestones of the project, reflecting this new schedule. Please indicate where and by how much each milestone has changed.

c. On 30 January 2020, in response to 2019-20 Supplementary Budget Estimates Question on Notice 460 (Portfolio Question Number 124), Defence provided the following nominal schedule dates for each Hunter class vessel: Please provide an updated version of these nominal dates for each vessel.

		Indicative Date
Ship 1	Cut Steel	End December 2022
	Vessel Acceptance Date	Q4 2029
Ship 2	Cut Steel	Q1 2025
	Vessel Acceptance Date	Q4 2030
Ship 3	Cut Steel	Q1 2027
	Vessel Acceptance Date	Q3 2032
Ship 4	Cut Steel	Q1 2029
	Vessel Acceptance Date	Q3 2034
Ship 5	Cut Steel	Q1 2031
	Vessel Acceptance Date	Q3 2036
Ship 6	Cut Steel	Q1 2033
	Vessel Acceptance Date	Q3 2038
Ship 7	Cut Steel	Q1 2035
	Vessel Acceptance Date	Q3 2040
Ship 8	Cut Steel	Q1 2037
	Vessel Acceptance Date	Q3 2042
Ship 9	Cut Steel	Q1 2039
	Vessel Acceptance Date	Q3 2044

d. On 30 January 2020, in response to 2019-20 Supplementary Budget Estimates Question on Notice 460 (Portfolio Question Number 124), Defence also stated that: “The expected Initial Operating Capability (IOC) acceptance date for Navy of the first ship is Q4 2031. IOC for the remaining ships would be expected to occur within 24 months of Vessel Acceptance”.

- i. What is the current expected IOC date for Navy of the first Future Frigate?
- ii. Does Defence still expect that “IOC for the remaining ships would be expected to occur within 24 months of Vessel Acceptance”?

e. At the Hearing on 14 August 2020, Mr Dalton said, “There is a cost to building the ships perhaps not at the most efficient tempo. We are building the ships at a very deliberate tempo so we can continue to build on a continuous basis. While there is a small premium upfront”.

- i. What proportion of the increased cost of the Future Frigates results from the decision to build the ships “not at the most efficient tempo”?
- ii. Please provide an estimate of the total additional cost premium for building the Future Frigates at less than the most efficient tempo.

f. Can Defence please explain how this ‘more feasible’ build schedule means Australian taxpayers are expected to pay \$10 billion more for the same number of Frigates, delivered later than promised?

g. Under this revised estimate, what is the average expected unit cost for the Future Frigates? It is expected that costs will decline with each ship built, but what is the projected average across the nine Frigates and how does that compare with the previous estimate?

h. Are these now the most expensive modern Frigates ever to be built at an amortised cost across the fleet of approximately \$5 billion per vessel? If Defence disagrees, please explain why and cite any examples of more expensive comparable modern Frigates.

i. How much of the \$45.6 billion cost of the Future Frigates is contained within the \$270 billion Force Structure Plan? In other words, how much of the \$270 billion is attributable to the Frigates?

ii. How does that compare with the 2016 Integrated Investment Program (IIP)? How much of the \$200 billion IIP was attributable to the Future Frigates?

Answer:

a. In the 2016 Defence Integrated Investment Program the Government flagged the investment in the future frigate program as greater than \$30 billion (out turned). The 2017 Naval Shipbuilding Plan flagged the future frigate program as more than \$35 billion noting the need at the time to protect the commercial position of the Commonwealth during negotiations. The actual out turned total acquisition cost estimate at approval in 2018 was \$44.3 billion. This out turned cost estimate factored in implementing a continuous shipbuilding program. The variation between this figure and the out turned estimate in the 2020 Force Structure Plan reflects changes in foreign currency exchange rates since 2018.

In 2018, the Government agreed to the implementation of a stable, deliberate and continuous shipbuilding drumbeat which considered the following:

- Prioritising the development a sustainable shipbuilding industry to end the ‘boom and bust’ cycle of naval shipbuilding, delivering sovereign capability and certainty for industry.
- Building the Hunter class faster would have created another ‘boom and bust’ cycle with a substantial gap between the end of the Hunter build and the commencement of the Hobart class destroyer replacement build.
- A gap between the two programs would have a very significant (catastrophic) impact on Australia’s shipbuilding workforce.
- A gap between the two programs would also drive significant additional cost into the Hobart class replacement program to rebuild the shipbuilding workforce (and cover the cost of idle facilities in the interim).
- Over the long-term, a continuous shipbuilding program is the most cost effective way to build complex destroyers and frigates in Australia.

b. The key milestones remain unchanged from that forecast at Government approval.

c. There has been no change to the dates as previously provided.

d.

i. Quarter 4, 2031.

- ii. Yes.
- e.
- i. The cost of building the ships at a tempo to support continuous shipbuilding was factored into the total acquisition cost estimate at Government approval.
- ii. There is no additional premium.
- f. The total acquisition cost estimate and schedule has not changed from that approved by Government in 2018.
- g. The total acquisition cost estimate includes aspects beyond the design and build of the frigates, such as facilities, land-based test sites, training and training development, spares, contingency allowances and project management costs, that are not attributable to the cost per vessel. A more accurate measure is the projected cost per tonne, which for the first three frigates is estimated to be \$257,000. This compares to the cost per tonne achieved on the air warfare destroyer of \$366,000.
- h. No. The estimated cost per tonne of the Hunter Class compares well with the Air Warfare Destroyer and international benchmarks.
 - i. Of the \$270 billion (out turned) planned investment detailed in the 2020 Force Structure Plan over the decade 2020-30, up to \$50 billion (out turned) is attributable to the Naval Shipbuilding Enterprise, which includes an element of the Hunter Class frigate program cost, noting that the program will run for 15 years beyond 2030. Given that the contracts for the construction of the frigates are yet to be put in place, the actual build cost estimates and distribution remain commercial-in-confidence.
 - ii. The Hunter Class frigate program when approved matched the funding profile that supported the public 2016 Integrated Investment Program. The Hunter Class frigate program funding profile supporting the 2020 Force Structure Plan is unchanged.