



## Joint Committee of Public Accounts and Audit

### Public Hearing on the Defence Major Projects Report 2020-21 and 2021-22 and Procurement of Hunter Class Frigates

19 May 2023

#### Opening Statement – Hunter class frigates

1. The performance audit report on the *Department of Defence's Procurement of Hunter Class Frigates* was presented for tabling in the Parliament on 10 May 2023.
2. The audit builds on previous ANAO work on Defence's acquisition and sustainment of ships for the Royal Australian Navy and implementation of the Australian Government's 2017 *Naval Shipbuilding Plan*. Since 2016–17, eight performance audit reports have now been tabled on naval procurement, maritime sustainment and related matters. The Hunter class frigates project, SEA 5000 Phase 1, has also been included in the annual Defence Major Projects Report since 2019–20.
3. The acquisition of nine Hunter class frigates is a key part of the Australian Government's substantial planned expenditure on naval shipbuilding and maritime capability and contributes to the ongoing capability of the Australian Defence Force. Construction of the Hunter class frigates is part of the Australian Government's continuous naval shipbuilding program intended to develop sovereign Australian shipbuilding and sustainment. The Australian Government's 2020 *Force Structure Plan* publicly reported that the cost of the Hunter class frigates was \$45.6 billion out-turned (MYEFO 2019–20 price and exchange).
4. This audit assessed the effectiveness of Defence's procurement of Hunter class frigates and the achievement of value for money to date.

5. The audit examined the limited tender process for the ship design undertaken by Defence, and Defence's advice to government at first and second pass (Chapter 2). The audit also examined the contracting arrangements established for the current design and productionisation stage of SEA 5000 Phase 1, contract monitoring and reporting arrangements, and Defence's expenditure to date in delivering on project milestones (Chapter 3).
6. Audit fieldwork was conducted at Defence offices in Canberra, the Osborne shipyard in South Australia, the Henderson shipyard in Western Australia, and Fleet Base West in Western Australia.
7. The audit did not examine related procurements associated with SEA 5000 Phase 1, including the selection of the Aegis combat management system, the acquisition of government furnished equipment such as the radar, the development of naval shipbuilding infrastructure and facilities, or the Australian Submarine Corporation restructure that preceded the procurement.
8. The audit reported on Defence procurement activity and developments in project SEA 5000 Phase 1 to March 2023. The government and Defence have reported publicly that the planned Hunter class capability has been considered as part of the Defence Strategic Review and related government processes.
9. Actual project expenditure at 31 January 2022 was \$2,225.9 million, with \$1,308.4 million spent on the head contract with BAE Systems Maritime Australia (BAESMA). The value of the head contract, when signed in December 2018, was \$1,904.1 million. At 31 March 2023, the value had increased by \$693.2 million, or 36 per cent, to \$2,597.4 million.
10. The audit conclusion was that Defence's management to date of its procurement of Hunter class frigates has been partly effective. Defence's procurement process and related advisory processes lacked a value for money focus, and key records, including the rationale for the procurement approach, were not retained. Contract expenditure to date has not been effective in delivering on project milestones, and the project is experiencing an 18-month delay and additional costs due in large part to design immaturity.
11. More specifically, the audit concluded the following.
  - Defence did not conduct an effective limited tender process for the ship design. The value for money of the three competing designs was not assessed by officials, as the Tender Evaluation Plan, or TEP, proposed that government would do so. The Commonwealth Procurement Rules (CPRs) and the Defence Procurement Policy Manual required officials responsible for procurement to be satisfied, after reasonable inquiries, that the procurement achieved a value for money outcome. Defence did not otherwise document the rationale for the TEP not requiring a value for money assessment or comparative

evaluation of the tenders by officials.

- Defence's advice to the Australian Government at first and second pass was partly effective. While the advice was timely and informative, Defence's advice at second pass was not complete. Defence did not advise that a value for money assessment had not been conducted by Defence officials and that under the TEP Defence expected government to consider the value for money of the tenders.
- Defence has established largely fit-for-purpose contracting arrangements for the design and productionisation stage, and largely effective contract monitoring and reporting arrangements to ensure adequate visibility of performance and emerging risks and issues. However, the contract management plan was established 44 months, or 3.6 years, after contract execution.
- Defence's expenditure to date has not been effective in delivering on project milestones, and the cost of the head contract has increased. Lack of design maturity has resulted in an 18-month delay to the project and extension of the design and productionisation phase, at an additional cost to Defence of \$422.8 million. At January 2023 the project was forecast to exceed the whole of project budget approved by government by a significant amount.

12. The audit report includes two recommendations, which were agreed by Defence.

- First, that Defence ensure compliance with its own records management policy, and with statutory record keeping requirements, over the life of the project — including capturing the rationale for key decisions, maintaining records, and ensuring that records remain accessible over time.
- Second, that Defence ensure its procurement advice to government on major capital acquisition projects documents the basis and rationale for proposed selection decisions — including information on the department's whole-of-life cost estimates and assessment of value for money.

13. We would be happy to answer any questions the committee may have.