



Defence Teaming Centre Inc
The defence industry association of South Australia
Relevant, Responsive and Reliable

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Senate Standing Committees on Economics
PO Box 6100
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Defence Teaming Centre Incorporated **Submission to the** **Senate Standing Committee on Economics Inquiry into** **Naval Ship Building – Part 1**

Introduction

Thank you for the opportunity to provide a submission to the subject inquiry on behalf of South Australia's defence industry.

The Defence Teaming Centre

The Defence Teaming Centre (DTC) is the peak defence industry body in South Australia. Founded in 1996 as an incorporated not-for-profit association with 24 member companies, the DTC has grown to a membership of 200+ companies that employ in excess of 17,000 workers. DTC members include Prime contractors (Primes), Small and Medium Enterprises (SMEs) and Professional Service Providers (PSPs).

The mission of the DTC is to represent the South Australian defence industry as part of the 'Defence State' and support its members to maintain and enhance their capabilities in order to maximise opportunities in the defence and related industry sectors. The DTC's vision is to be nationally and internationally recognised as a model industry body that is relevant, responsive and reliable to its membership.

The Peaks and Troughs of Naval Ship Building

A significant barrier to improved productivity in Australia's naval ship building capability is the peaks and troughs of Defence contracting. Diagram 1 below is an indicative representation of the peaks and troughs of naval shipbuilding in Australia. In the 1990s the nation generated a workforce of in excess of 15,000 workers building three different fleets of naval vessels simultaneously. At the end of those build programs the workforce and associated skills and building experience were dissipated. In the 2000's a new workforce had to be generated to build the Air Warfare Destroyers (AWD) and fit-out the Landing Helicopter Dock (LHD) ships. Due to a lack of ongoing contracts, it is highly likely that these workforces will also dissipate at the end of the build programs. A new workforce will have to be generated again in the late 2010's to build future frigates and submarines.

It is time to break the paradigm of discussing naval ship and submarine build programs in terms of a total number of vessels to be made in a discrete project. It is better to speak of a sustainable and innovative industry that will produce, for example, a warship and a submarine every two years in a continuous spiral development construct. Continuous build programs allow industry to improve its productivity and evolve innovative solutions that enhance their capacity to export.

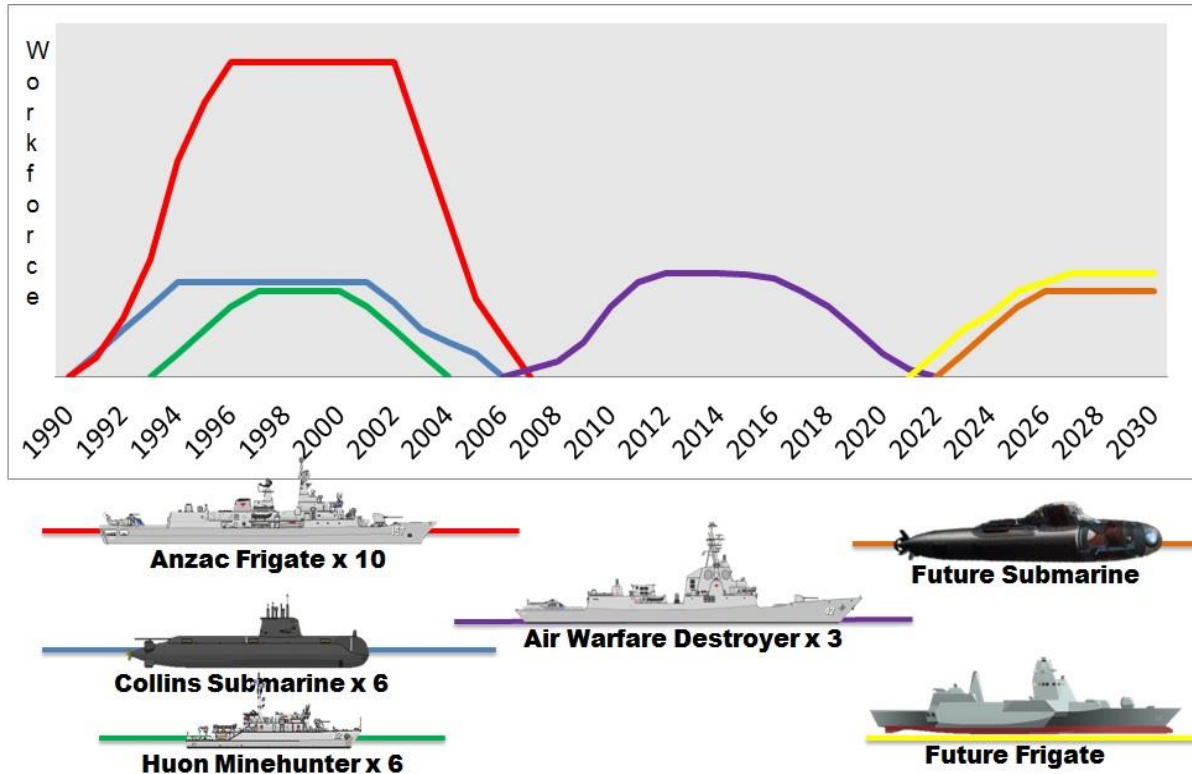


Diagram 1: Indicative representation of the peaks and troughs of naval shipbuilding in Australia

The impact of the electoral cycle and politics on the Government's Defence capability acquisition and sustainment decisions has had an increasingly debilitating effect on defence industry. The constant changing and cancelling of projects and successive Government's lack of commitment to its acquisition plans have led to a loss of confidence that has curtailed investment and growth.

Announcement of the Replacement Replenishment Ships Project

On the 6 June 2014 the Minister for Defence provided the following media release:

"Replenishment vessels are essential to support sustained naval deployments. Navy's current replenishment ship HMAS *Success* is in urgent need of replacement. And HMAS *Sirius* only provides limited replenishment capability.

In light of the urgent need to forestall a capability gap in this crucial area; the **current low productivity of shipbuilders** involved in the AWD program; and **value for money considerations**, the Government has given First Pass approval for Defence to conduct a **limited competitive tender process** between Navantia of Spain and Daewoo Shipbuilding and Marine Engineering (DSME) of South Korea for the construction of two replacement replenishment vessels based on existing designs.

“Navy is in urgent need of large support vessels that we assess are beyond the capacity of Australia to produce competitively at this stage. In this instance it would not serve anyone if we were to provide a challenge to industry that was beyond its capabilities.”

“Competition between these two experienced shipbuilders is the best way to ensure delivery of capable, cost effective vessels in the time frame required.”

This submission will focus on the statements in **bold** above.

Current Low Productivity of Shipbuilders

The Government and Defence have made a number of statements recently about the productivity of Australia's naval ship building industry based on the results of the Winter review of the AWD program. It is unfortunate that the Government has not released the review report in order that industry can analyse its findings and focus on addressing the concerns it apparently raises. As industry does not have access to the report that forms the basis to the Government's decisions and criticisms, it is left to ask questions of the inquiry rather than provide substantive responses.

Based on the Winter review, the Minister has criticised the productivity of Australia's naval ship building industry quoting an international standard of 60 hours per tonne, a 'generous' aspirational allowance of 80 hours per tonne for the AWD program and a current level of productivity of 150 hours per tonne within the industry. Industry has posed the following questions in relation to these statistics:

- What is the basis for the international standard of 60 hours per tonne? Is it the standard of a foreign shipyard producing low complexity vessels on a regular basis? Or, does the statistic relate to a mature shipyard producing indigenous designed complex warships like the AWD on a continuous build basis? Or, is it the expectation of a new shipyard building a short run of three offshore designed, complex, first of class, warships like the Air Warfare Destroyer?
- What is the basis for the Government's 'generous' aspirational allowance of 80 hours per tonne for Australia's naval ship building industry? Is this the expectation of a mature shipyard building an indigenous designed complex, first of class, warships like the Air Warfare Destroyer after the first three ships are completed? How can the Government expect a standard of 80 hours per tonne from a new shipyard building a short run of three offshore designed, complex, first of class, warships like the Air Warfare Destroyer when the ship yard is yet to complete the first ship?
- What is the basis for the Minister for Defence's often quoted 'current' standard of 150 hours per tonne? When was the measurement taken, and what was the methodology used? Is the 150 hours per tonne an average of the four shipyards building modules for the Air Warfare Destroyers (Spain, Adelaide, Melbourne and Newcastle)? If so what are the productivity levels for each shipyard? How much of the 'current' standard of 150 hours per tonne is attributable to the reworks and remediation required due to deficient design drawings and redesign work? What is the reason why there has been a requirement for the significant reworks and remediation work?

On 15 July 2014 the Australian newspaper published a front page story apparently based on an exclusive interview with a 'Defence spokesman'. The story generated the following questions from industry:

- The story claimed that: 'HMAS Canberra arrived a month late because of fears of a pirate attack off the coast of Somali'. Is this the case? Or was it closer to two months late due to the Spanish ship builder not being able to complete the work it was contracted to do in time for the window for the transport ship to depart Spain? Was the need for the transport ship to avoid the piracy issue off Somali always planned for due to the Navy being unable to assure it would be able to provide security for the transit?

- How much work was required to be conducted in Australia due to the Spanish ship builder not being able to complete the work it was contracted to do in Spain prior to delivery. How many hours of work were required to be completed by Australian contractors and how much did the additional work contribute to the delay in final delivery?
- The story listed a number of faults identified in the original sea trials. What were the faults identified in the sea trials and how many are attributable to the work conducted by the Spanish ship builder prior to delivery? How much time has been consumed in remediating the faults identified in the sea trials and how did the need for this work contribute to the delay in final delivery?

Value for Money

A significant barrier or impediment to the growth of Australia's defence industry is the lack of consideration of the importance of an indigenous defence industry to the national economy. It is important that Government appreciates that the quantum and value of Australian Defence expenditure is such that it represents national revenue and decisions cannot be made on the basis of Defence imperatives alone.

Understandably, Defence is allocated a limited budget and its ambition is to gain the maximum benefit from a finite resource. When Defence is not compelled to consider the national benefits of its investments, unsurprisingly, it is motivated to acquire the least expensive options.

Government should be compelled to consider 'value for money' in the context of the holistic whole-of-life cost benefit to the nation. This would see a greater focus on recognising the full benefits to the nation of the acquisition and sustainment of Defence capabilities through a national indigenous defence industry capability and would ensure consideration is given to:

- maximising the return of Australian taxpayers' dollars to the Australian economy,
- assuring the security of our nation,
- growing innovation and inspiring our future workforce,
- enhancing technology transfers,
- securing intellectual property, and
- sustaining our nation's industrial capability.

In his response to a question in the House of Representatives on 15 July 2014 in relation to the Rossi Boots issue, the Assistant Minister for Defence made the following statements that generated the associated questions within industry:

- "There was no mandated requirement for Australian content, as it doesn't relate to the combat uniform." Does the Government/Defence have rules in relation to mandated Australian content in non-combat equipment? Conversely, does the Government/Defence have rules in relation to mandated Australian content in combat equipment? How does the Government/Defence measure/decide on the appropriate level of Australian content?
- "They were not successful tendering for the fawn industrial footwear due to overall value for money considerations, in other words, they were considered too expensive." Is this a statement by Government that value for money is directly and only related to price, no consideration of national benefit?

Limited Competitive Tender Process

Industry is confused as to why the Government elected to proceed with a limited competitive tender process with Navantia and DSME when 18 months earlier it had been presented with proposals from ASC and BAE to acquire replenishment vessels through those same shipbuilders. ASC partnered with DSME and BAE partnered with Navantia to offer similar 'hybrid' proposals whereby the hulls for the vessels would be built in South Korea and Spain respectively and transported to Australia for fit out similar to the Landing Helicopter Dock program. This has generated the following questions within industry:

- Why did the Government discount and not make any public mention of the ASC and BAE 'hybrid' proposals?
- What is Navantia and DSME's history and experience in building naval replenishment ships?
- What is the Government's plan for through life sustainment of the vessels given that there will be no Australian industry involvement in the construction phase?
- Does the government believe it is appropriate to approach the foreign partners of Australian companies directly and then establish a limited competitive tender process that specifically excludes the Australian countries?

Support Given to Defence Industry by Governments of Comparable Nations

Australia's defence industry is increasingly encouraged by the Government to pursue opportunities and compete in the global marketplace. Unfortunately, it is difficult for them to compete on a level playing field. It is a global practice that many countries use policies and programs to preference and protect their indigenous defence industries. In contrast, Australia adopts an open market approach, with no hurdles for foreign suppliers to compete for its Defence acquisitions.

Programs implemented by other governments to protect their indigenous defence industries are offered under many titles including offsets, industrial cooperation and industrial participation. When challenged on these, the Australian Government stands lonely on the moral high ground that practices such as offsets contradict free market principles and contravene its commitment to Free Trade Agreements.

It is understood that Australia's Free Trade Agreements have specific 'carve-outs' for national security issues. In addition, it is also understood that Australia is soon to commit to the World Trade Organisation's Agreement on Government Procurement which prohibits the use of offsets in government procurement generally, but explicitly exempts actions necessary for the protection of its essential security interests relating to the procurement of arms, ammunition or war materials, or to procurement indispensable for national security or national defence purposes.

In judging Australia's defence industry performance when competing globally and exporting, the Government needs to be mindful that they are not competing on an even playing field. A second order effect is that foreign companies must focus on fulfilling their offset obligations in other countries before they can consider using Australian industry, which serves to further compound the dilemma for Australian industry.

Conclusion

The essence of this submission is to voice the concerns of South Australia's defence industry in relation to the Replacement Replenishment Ships project. It is important to highlight the following points in relation to that industry:

- It is an industry that is reluctant to speak publically against the government for fear of retribution and repercussions.
- It is an industry that is not looking for handouts from government or charity in the awarding of contracts.
- It is an industry that wants to be recognised and respected for the significant role it plays in the development and delivery of Australian Defence Force military capability.
- It is an industry that wants the opportunity to compete under the construct of holistic whole of life benefit to the nation and on a level playing field where the cheapest price is not the determinant of value for money.
- It is an industry that would rather collaborate and partner with the Government and Defence rather than be subjected to orchestrated campaigns to discredit it in order to justify going offshore to acquire low risk hardware at the cheapest price.
- It is an industry that truly questions if the Australian Government and the Department wants an indigenous defence industry.

Thank you on behalf of all DTC members for taking the time to consider the views and concerns of defence industry in South Australia as presented in this submission.

Yours faithfully,

Chris Burns, CSC

Chief Executive Officer