



AIDN

SME participation plan for
defence and national security

November 2013

SME participation plan for defence and national security



In recent years AIDN National has noted, with increasing concern, the reduction in the number of commercial opportunities for Australian small and medium enterprises (SMEs) in both Defence capital procurement and sustainment. Despite the general objectives and specific initiatives set out in the Defence and Industry Policy Statement 2010 Building Defence Capability: A Policy for a Smarter and More Agile Defence Industry Base, AIDN considers that current Defence industry policy is failing Australian SMEs. AIDN also believes that current Australian Government procurement practices in many cases operate to the disadvantage of vibrant local SMEs. By comparison, other countries including the USA and Canada are more supportive of their local defence small business sectors.

In addition to these defence industry policy issues, AIDN also has some ongoing concerns with the maintenance of ethical business standards, protection of intellectual property and compliance with Australian Industry Capability (AIC) plans.

In response to these challenges, AIDN published its SME Participation Plan for Defence and National Security in March 2012. It has now revised the Plan to meet today's challenges for the defence industry. The main features of this revised Plan are:

- Revised guidelines for the definition of value for money in Defence projects to ensure that appropriate weight is given to a range of issues including Australian Industry Capability (AIC) Plans and Priority Industry Capabilities (PICs) and Strategic Industry Capabilities (SICs);
- In the absence of broadly based support for inclusion of Australian industry in Defence projects, the development and implementation of a Strategic Sourcing Program to inform priorities for AIC Plans in projects, and to enhance self-reliance;
- More comprehensive and strategically-based implementation of PICs and SICs, including mandatory inclusion in AIC Plans where appropriate; and
- The effective implementation and scrutiny of AIC Plans in Defence projects, with strengthened provisions to ensure compliance.

AIDN commends this Plan to Government as a major step in the journey.

A handwritten signature in black ink that reads "Alan Rankins". The signature is written in a cursive, flowing style.

Alan Rankins
President, Australian Industry & Defence Network

Proposal

To address the increasing loss of Australian owned and/or based defence and security oriented SME capabilities, to protect and develop a key source of innovation, responsiveness and flexibility in support of Australia's national defence and security, and to more effectively support overall defence capability development and sustainment, AIDN calls on the Australian Government to implement a comprehensive Defence and National Security SME Participation Plan.

This SME Participation Plan for Defence and National Security has the following key elements:

- A reconsideration of the definition of value of money in the assessment of both defence capability and sustainment source selection options and defence industry programs to take into account long term maintenance of PICs and SICs and a range of national interest considerations.
- An Australian Government and Defence/DMO commitment to the establishment and implementation of ongoing support for Priority Industry Capabilities (PICs) and Strategic Industry Capabilities (SICs) programs with clear objectives and milestones, appropriate public reporting of implementation status and a strategic approach to implementation through comprehensive requirements in the AIC plans for individual projects.
- A Strategic Sourcing Program to further inform rigorous priorities for AIC Plans in projects, and to enhance self-reliance through broadly based support for PICs and SICs.
- Energising of the implementation of defence industry policy and related programs through the establishment of KPIs for each key policy or program, the public identification of the appointment of the Senior Executive (or equivalent) with responsibility for the policy or program development and implementation, and with reporting against KPIs to be included in the DMO annual report.
- The DMO to provide efficient and effective scrutiny of AIC Plan implementation.
- Prime Contractors be held accountable for the achievement of AIC KPIs in their contracts, with a requirement for annual reporting of progress to Project Managers and with the overall progress of achievement against current AIC plans being included in the DMO annual report. Failure to fulfil the requirements of endorsed AIC participation plans to have real consequences for non-compliant prime contractors through the public reporting of such non-compliance and through impacts on the future tender assessment of such non-complying companies.
- AIC Plans to include contractually binding deeds of agreement between the prime contractors and supporting SMEs, with such deeds including designated performance requirements for both the prime contractor and SMEs. Changes to the deed would be subject to usual contract change procedures.

Key issues

Defence recognises that more than 3,000 SMEs work in the defence sector in Australia¹. These SMEs are estimated by AIDN to employ more than 50,000 people and, in conjunction with the primes in Australia, play a crucial role in providing Defence with new capability and the sustainment of that capability. Those employed in the defence industry SME sector are in general highly skilled, many with a high level of dedication to the support of the Australian Defence Force (ADF) and Australia's defence. Given the current outcomes of defence capability development and procurement processes, many of these companies and their key skilled staff see their commercial opportunities shrinking. As these companies and skills are lost to the defence industry, there is a very considerable impact on the provision and sustainment of ADF capability. Defence is in a continuing competition for skills and industrial capability with other sectors such as mining and transport. An effective and supportive defence industry strategy that ensures the engagement of the defence industry SME sector is essential if Australia's Defence interests are to be successful in this competition.

The proposed Defence and National Security SME Participation Plan has as its primary objective the establishment and maintenance of an Australian defence and national security industry base with the depth, capability and viability to cost-effectively contribute to the achievement of the necessary level of Australian defence self-reliance. Further, the key elements of the Plan articulated below are focussed on achieving not only benefits for Australian SMEs but also benefits for Defence through equal or better pricing, access to innovation, enhanced through-life support and consequently enhanced self-reliance.

SME participation plan for defence and national security - key elements

I. Reconsideration of the Definition of Value for Money

AIDN's assessment of current DMO procurement practices makes it clear that despite the policy emphasis on PICs and SICs, procurement decisions continue to be made on a narrow interpretation of value for money concept (i.e. lowest cost grounds) on a project-by-project basis, even if such decisions are to the detriment of the development and sustainment of PICs and SICs.

It is clear that a reconsideration of the definition of value of money is required in the assessment of both defence capability and sustainment source selection options and defence industry programs. This reconsideration needs to take into account a range of national interest considerations to ensure that short-term project expediency and a narrow cost focus does not override the longer-term objective of maintaining PICs to ensure national self-reliance and future project support.

Such a revised definition of value for money in the area of defence capability and sustainment procurement should, in addition to cost, include assessment of the demonstrated responsiveness and flexibility of tenderers, demonstrated reliability in terms of quality and timeliness of project or service delivery, ability to innovate in response to changing operational requirements and the economic multiplier benefits of a contract on both a national and regional basis. Further, where these benefits can be demonstrated without additional cost, a careful consideration of risk should be made so as to not disadvantage Australian solutions where capability already exists, or can be shown to be available through a low risk development path. This is not to say that Australian solutions should always be used where benefits are outweighed by cost and other factors in a value for money equation that includes the above considerations.

¹ Defence and Industry Policy Statement 2010 "Building Defence Capability: A Policy for a Smarter and More Agile Defence Industry Base", para 2.46, p29.

Key issues

2. Priority Industry Capabilities (PICs) and Strategic Industry Capabilities (SICs) Program Implementation

AIDN strongly supports the identification of PICs and SICs in line with current defence industry policy. AIDN notes that Defence has now moved some way towards addressing PIC and SIC maintenance through the establishment of the Defence Industry Innovation Board (DIIB)². The DIIB is charged with establishing the Guidelines for the new PIC Innovation Program. In conjunction, Defence has been asked to:

- Improve their definition of the essential elements of the PIC and SIC capabilities and the implications for Government;
- Make the distinction between PICs and SICs clearer;
- Determine appropriate intervention strategies to support PICs;
- Integrate them more effectively into the Australian Industry Capability Program, SADI and the Global Supply Chain Program; and
- Ensure that PICs and SICs are embedded in the DCP project descriptions.

AIDN recognises and welcomes the significant amount of work undertaken by the DMO in conducting a number of the PIC 'health checks' and recommends that the remainder of the PIC 'health checks' be completed as a matter of priority. The completion of the PIC 'health checks' will assist in the further definition of each PIC. A similar program needs to be undertaken to assist in the clearer definition of the SICs. Following the definition activity, AIDN recommends an Australian Government and Defence/DMO commitment to the establishment and implementation of a rigorous program for the implementation of PICs and SICs with clear objectives and milestones for progressing each capability and with appropriate public reporting of implementation status.

Based on AIDN's assessment of the approach that has been taken to date in the analysis and implementation of PICs and SICs, AIDN considers that higher level strategic planning for the development and sustainment of overall PIC and SIC capability needs to be enhanced. PICs and SICs cannot be considered in isolation from sustainment requirements. Consequently, strategic planning for PICs and SICs needs to take into account:

- The totality of each capability including sustainment;
- Where the capacity to provide capability is located in Australia; and
- The current and future projects that will rely on this PIC or SIC.

Without this, PICs and SICs will not reach their potential in support of Australian defence self-reliance. Further, the potential remains for a narrow interpretation to be placed on each capability to the detriment of the sustainment of the more broadly based industry capability needed to effectively support each PIC.

AIDN considers that the mandatory inclusion of PIC and SIC requirements in AIC Plans is the strongest tool available to ensure their maintenance. However, to ensure that this measure is not compromised, effective integration of PICs and SICs into AIC Plans must include consideration of:

- Their maintenance and enhancement not only in the procurement phase but also in sustainment.
- Where new capability is proposed, the effect on existing capability and the viability of the entire PIC/SIC area as a consequence.
- The inclusion of the strengthened AIC Plan proposals made above, with particular emphasis on reporting requirements and contractual provisions for binding deeds of agreement (see below).

2. Minister for Defence Materiel media release dated 16th February 2011 "Board to provide expert advice on Defence Industry Innovation"

Key issues

3. Strategic Sourcing Program

The DIPS makes the very valid point that Defence is well placed to “leverage its weight as a customer” as it was the world’s 8th largest arms importer 2001-2007³ and its rate of procurement is increasing substantially. However, when looking at barriers to global competition, it states in contrast that other nations take protectionist approaches to their national defence industries while Australia does not, and this reality must be accepted⁴. But it is also clear that the alternative – AIC Plan and Global Supply Chain policies - is failing Australian industry, particularly SMEs. The deficiencies in AIC Plans have been addressed above with clear recommendations for improvement. While Global Supply Chain initiatives are worthwhile, the overall successes achieved have been sporadic and the total value significantly less than achieved internationally by alternative policies.

AIDN is strongly of the view that significantly more can be achieved to enhance industry capability and to ensure that Australian companies win more defence work, while at the same time enhancing self-reliance and not reducing value for money in Government procurement. To do this, AIDN proposes the establishment of a Strategic Sourcing Program (SSP).

Rather than the piecemeal and largely project-specific approach currently being taken with AIC Plans, the SSP would rely on the strategic analysis of total capability proposed above under Implementation Strategies for PICs and SICs to produce a Defence Industry Capability Map (DICM). The DICM would consist of:

- PIC and SIC total capabilities.
- Capability gaps between PICs and SICs that would enhance the maintenance of the PICs and SICs.

- Capability areas surrounding the PICs, SICs and gaps which would also contribute to the maintenance of PICs and SICs.

Consequently, the DICM can be seen to be a strategically-focused, broadly-based map of the industry capability required in Australia to ensure on-going self-reliance. Project AIC Plans would then be formulated using the DICM to not only achieve project-specific industry capability outcomes but also to enhance innovation and longer-term capability objectives which contribute to self-reliance. The capability so produced could then be expected to continue beyond individual project timeframes as it would be required for future projects.

It is not expected that the DICM will be a static mapping of capability. As the DIPS rightly points out, PICs and SICs will change over time and so will the DICM change. However, initial determination of the DICM will be an essential step in determining the overall effect on the total capability required as the PICs and SICs change.

While the SSP would inform AIC Plan objectives for all projects, implementation in contracts would only occur where value for money for Defence is achieved through better and broader industry capability, equal or better pricing, improved delivery times, access to innovation, enhanced through-life support and consequently enhanced self-reliance. AIDN firmly believes that such benefits will accrue for the majority of projects and urges Defence to make realistic risk assessment for Australian solutions with the undoubted potential to achieve these benefits.

“Defence is well placed to leverage its weight as a customer as it was the world’s 8th largest arms importer”

3. Defence and Industry Policy Statement 2010 “Building Defence Capability: A Policy for a Smarter and More Agile Defence Industry Base”, para 2.54, p32

4. Ibid, para 2.19, p22

Key issues

“prompt and effective action is required if the poor state and declining prospects of the defence SME sector are to be rectified”

4. Defence Industry Policy and Program Implementation

While AIDN welcomes and supports the industry policy objectives and programs set out in the Australian Government's 2010 Defence and Industry Policy Statement, AIDN has significant concerns with the pace and comprehensiveness of their implementation. Prompt and effective action is required if the poor state and declining prospects of the defence SME sector are to be rectified.

To more effectively drive policy and program implementation AIDN recommends that KPIs be established for each key policy or program, together with the public identification of the Senior Executive (or equivalent) appointment with responsibility for the policy or program development and implementation, and with transparent reporting against policy and program KPIs to be included in the DMO annual report.

5. Application of Australian Industry Capability (AIC) Plans

Until 2012, AIC Plans were only required for DCP projects with a value of \$50m or more. AIDN argued for and welcomed the change to a \$20m threshold. Based on the information in the 2010 Defence Industry Policy Statement⁵, an AIC Plan requirement with a threshold of \$50m would capture less than 20 projects each year. Reducing the threshold to \$20m could be expected to include up to a further 30 projects at a value of around \$400m, principally in the areas of support, complex materiel and standing offers for services. It is in these areas, as well as in sub-contracting to primes, where greatest opportunities for defence SMEs exist.

AIDN is aware of the implications for DMO that resulted from the change to the AIC Plan thresholds. However, AIDN believes that scrutiny of AIC plans can be achieved with industry in an efficient manner with industry to ensure minimal need for additional DMO resources.

6. Contractor accountability for AIC Key Performance indicators and Consequences for Non-Compliance with Endorsed AIC Participation Plans

One of the perceived limitations of AIC plans at present is that there appears to be no mechanism through which prime contractors can be held accountable for non-performance against the requirements of a project's AIC plan. AIDN recognises that the issue of enforcement is difficult. Legal enforcement by DMO would be likely to be both prolonged and problematic, while SME suppliers are most reluctant to publicly complain or criticise because of the likely negative future business consequences. Sadly, some experience to date supports the need for such caution.

There are, however, a number of remedies that could significantly improve the current approach:

- Using a facilitated process such as through the St James Ethics Centre, agreement could be reached between the Defence prime contractors, Ai Group, AIDN and DMO on a framework for the ethical conduct of the relationship between primes and sub-contractors. That framework could address issues such as the protection of intellectual property and the treatment of bid team members in the transition from tender submission to contract implementation.

5. Defence and Industry Policy Statement 2010 "Building Defence Capability: A Policy for a Smarter and More Agile Defence Industry Base", Table 3 – DMO Contracts and Value FY2008-09, p52.

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- The appointment of an independent Defence Industry Advocate to address issues on non-compliance within such an ethical framework would provide greater confidence that issues of concern could be resolved without detrimental consequences for companies that raise concerns.
- As announced by then Defence Materiel Minister, Jason Clare and the Defence & Industry Conference 2011, in June 2011, that the DMO establish and maintain the AIC Implementation Team to monitor and report on AIC compliance. The team will audit AIC key performance indicators (KPIs) in Projects, with the overall progress of achievement against current AIC plans being included in the DMO annual report.
- Unrectified AIC participation plan non-compliance by prime contractors, as verified through the DMO auditing process, will be reported publicly by DMO following the completion of each AIC plan audit.
- Failure by companies to comply with the requirements of AIC plans be taken into account in the future assessment of tenders from such companies with the ultimate potential sanction being that companies that are deemed non-compliant with AIC plan requirements being deemed non-compliant for future tenders until such deficiencies are rectified. Such measures are used in other forms of contracting.

7. AIC Plan Deeds of Agreement

AIDN strongly endorses the recent policy change to reinforce the effectiveness of AIC Plans. AIDN also proposes that each plan include a contractually binding "deed of agreement" between the prime contractors and supporting SMEs with such deeds including designated performance requirements for both the prime contractor and SMEs covering issues such as agreed capability, capacity, facilities to be provided, security requirements, insurance, staffing, an intellectual property register, quality assurance and work systems, and teaming arrangements. Such deeds would:

- Be in addition to the existing contractual arrangements;
- Require contract change procedures to be used to amend them;
- Inform the AIC plan audits to be conducted by DMO; and
- Be consistent with the proposed ethical framework discussed above.

“AIDN strongly endorses the recent policy change to reinforce the effectiveness of AIC Plans”

Conclusion

AIDN considers that the proposed SME Participation Plan for Defence and National Security will both complement and assist with the achievement of the objectives of the 2010 Defence and Industry Policy Statement, as well as addressing the continuing decline in the opportunities and available capabilities of Australia's defence SMEs.

The Plan has as its primary objective the establishment and maintenance of an Australian defence and national security industry base with the depth, capability and viability to cost-effectively contribute to the achievement of the necessary level of Australian defence self-reliance. The main elements of the plan are:

- A reconsideration of the definition of value of money in the assessment of both defence capability and sustainment source selection options and defence industry programs to take into account long term maintenance of PICs and SICs and a range of national interest considerations.
- An Australian Government and Defence/DMO commitment to the establishment and implementation of a rigorous program for the implementation of the Priority Industry Capabilities (PICs) and Strategic Industry Capabilities (SICs) program with clear objectives and milestones, including comprehensive implementation in AIC Plans for individual projects and with appropriate public reporting of implementation status.
- Implementation of a Strategic Sourcing Program to inform rigorous priorities for AIC Plans in projects, and to enhance self-reliance through broadly based support for PICs and SICs.
- The implementation of defence industry policy and related programs be energised through the establishment of KPIs for each key policy or program, and the public identification of the appointment with responsibility for the policy or program development and implementation.
- The DMO be required to provide the minimal additional resources needed to ensure the efficient and effective achievement of AIC Plan implementation and scrutiny.
- That prime contractors are held accountable for the achievement of AIC KPIs in their contracts, and the overall progress against current AIC plans be included in the DMO annual report. Failure to fulfil the requirements of endorsed AIC participation plans to have real consequences through the public reporting and impacts on future tender assessment of non-complying companies.
- AIC Plans to include contractually binding deeds of agreement between the prime contractors and supporting SMEs.
- Continued support for the PIC IP to assist in fostering innovative solutions in PIC areas.



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AIDN

Industry Involvement for
Defence in Australia

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Industry Involvement for Defence in Australia



Since the 1990s, Australian governments have shunned offsets policies. This is despite the continued use of such policies by many countries to meet a range of defence industrial objectives. These include countries with which Australia trades in defence goods, and countries with which Australia has joint projects. Countries include America, Canada, Great Britain, Israel, Spain and Turkey.

The emphasis placed on such policies is evidenced by a recent announcement by the Canadian Defence and Industry ministers. Under the banner of a new Defence Procurement Strategy, they have just strengthened their offset requirements to achieve local industrial benefits and jobs. This is already leading to the major defence companies positioning themselves to meet the requirements, including Boeing reported as offering 100% offsets if Canada buys the Super Hornet and Lockheed highlighting local jobs that would result from an F-35 purchase.

Offset policies are used to derive a range of benefits. These include:

- technology transfer;
- establishment of licenced production, co-production, joint ventures and partnerships;
- involvement in global supply chains;
- economic development including job creation;
- skills development; and
- technological self-sufficiency.

Policies can be tailored to meet a range of such objectives.

One consequence of dealing with countries which have offsets policies is that any premium resulting from such policies is built into the price Australia pays. For joint projects, the premium will include those resulting from the policies of each of the partners.

In today's economic environment, with a shrinking industrial base and significant job losses, AIDN considers it time to revisit industry involvement policy for defence. Such a policy has potential to enhance outcomes arising from AIDN's SME Participation Plan for Defence and National Security by achieving more strategically important industry capability in Australia without incurring premiums. Consequently, it has produced this paper and invited the Australian Strategic Policy Institute to comment on how such a policy might be structured to best achieve the benefits in Australia currently enjoyed by our trading partners.

A handwritten signature in black ink that reads "Alan Rankins". The signature is written in a cursive, flowing style.

Alan Rankins
President, Australian Industry & Defence Network

Introduction

Australian Defence Industry is increasingly operating in a global environment. This is not only the case when they contend for exports, but also locally as international suppliers compete for our Defence dollar. As such, the need for fair competition and a level playing field is very significant if we are to keep a Defence industry capability. This is particularly the case as the concept of preference for local industry is practiced widely by our global competitors and customers under many titles including "Defence Offsets".

In March 2012, the Australian Industry & Defence Network (AIDN) released its "SME Participation Plan for Defence and National Security". Subsequently in November 2013 to meet current challenges for industry, AIDN has amended this Plan to include a more focussed approach to Value for Money and a Strategic Sourcing Program (SSP). The Plan calls for a more rigorous implementation of the policies that already exist, and the broadening of the Priority Industry Capabilities (PICs) and Strategic Industry Capabilities (SICs) domain to include associated and enabling capabilities creating a Defence Industry Capability Map (DICM) as part of the implementation of the SSP.

In addition to the SSP proposal above, this paper examines a range of overseas programs aimed at ensuring that local industry benefits accrue from overseas purchases of defence equipment and platforms. These benefits are then analysed with a view to determining their applicability as enhancements to the current Defence Australian Industry Capability (AIC) and the Global Supply Chains (GSC) programs. Priority in this analysis has been given to achieving long term, meaningful, strategic industry capability benefits that will enhance Defence self-reliance. However, it is anticipated that further research will be needed to quantify benefits and structure a program to maximise them for Australia.

Background

With North American and European Defence budgets declining since the end of the cold war, multinational Defence prime contractors are consolidating and reducing in numbers. They are also more active in the pursuit of export markets, and Australia is becoming high on the target list as a significant Defence equipment importer. The Stockholm International Peace Research Institute (SIPRI), considering 2011 and 2012 figures, ranks Australia as the fourth largest Defence importer in the world after India, China and South Korea.

Notwithstanding the scrapping of the Australian Defence Offsets Program in the early 1990s, the Australian Defence industry policy makers have always acknowledged the importance of maintaining a capable Australian Defence industry, and implemented some measures and programs for that purpose. On the other hand, a clear message has been maintained that Defence will not pay a premium to maintain local capabilities, and that "value for money" will be the main criteria for acquisition decisions, with very few exceptions. As such, the message to Australian industry has constantly been to work harder and smarter to be globally competitive.

However, while Australia is adopting an open market approach, with no hurdles for foreign suppliers to compete for its Defence projects, governments around the world are using many policies and programs to preference and guard their indigenous Defence industries. The measures implemented by the Australian Department of Defence to encourage its Defence industry, such as AIC and GSC, are dwarfed by those enforced by other

countries. Programs implemented by other governments favouring their indigenous industries are offered under many titles and definitions including Offsets, Industrial Cooperation, Industrial participation and others.

The 2010 Defence Industry Policy Statement (DIPS) used the theme: "A Policy For Smarter & More Agile Defence Industry Base". In reality, the result of that policy is a declining Defence Industry that, unless strategic change is implemented over the next couple of decades, will all but disappear or be reduced to only small offices representing the multinational prime contractors, and importing most, if not all Defence requirements. This is not a very smart or agile result for Australia or all the Australians who develop, maintain and sustain Australia's Defence Capability.

It is all too easy to forget in times of Peacekeeping and low intensity conflicts that Australia is an island at the end of a very long supply chain. A long term Australian Defence Industry is a national asset that is absolutely vital to ensure Australia's strategic self-reliance.

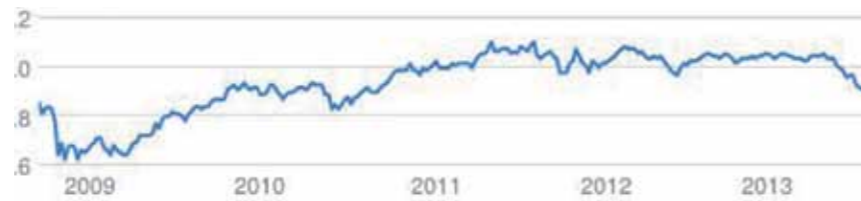
“a clear message has been maintained that Defence will not pay a premium to maintain local capabilities, and that “value for money” will be the main criteria for acquisition decisions”

Australian Defence Industry predicaments

“multi-national Defence suppliers, particularly for Defence support equipment, are increasingly using Chinese or Mexican factories”

Increasingly, Australian Industry is not able to compete globally when judged on price alone. The reasons are many including:

- Between 2009 and 2013, the strong Australian resource sector has caused the value of the Australian dollar to be inflated against its major trading partners. As such the price of Australian products rose when compared with similar international products.



Source: ozforex.com.au

- That high dollar value does not reflect the strength of the Australian economy in other sectors. However as the manufacturing sector competes with mining for skilled labour, labour rates rose significantly.
- In the same period, as the world suffered from the Global Financial Crises (GFC), international suppliers became more desperate, and dropped their prices to be able to survive. In many cases those competitors benefited from Government programs designed to make them more competitive.
- Australian manufacturers are also suffering from other high costs including energy, materials and taxes when compared with most competitors.
- With a relatively small armed force, Australian Defence industry does not have enough local economy-of-scale and as such, unless significant exports are achieved, Australian products are more costly.
- With no policy measures in place to favour local products, Australian industry is faced with a price disadvantage at home as well in its potential export markets.

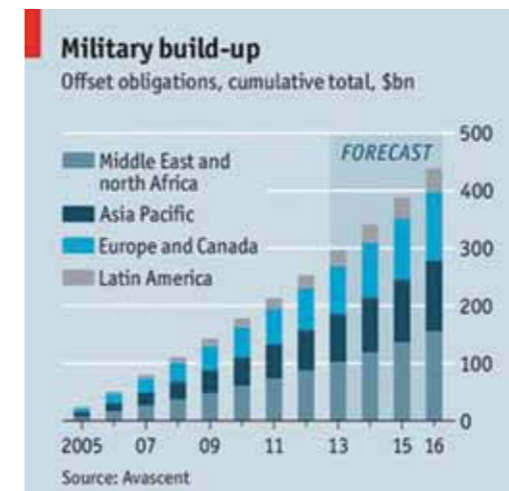
As a result, Australian Defence industry is in consistent decline, and regions that were traditionally considered as export markets such as India and South Korea are now targeting Australia as an export destination. Moreover, multi-national Defence suppliers, particularly for Defence support equipment, are increasingly using Chinese or Mexican factories to partly manufacture their equipment, making it almost impossible for Australian Defence manufacturers to compete.

Free trade compliance

One of the reasons behind the reluctance to implement Offsets or similar measures is the perception that this practice contradicts our commitment to the Free Market Principles. It is important to note however that offsets are permitted by the World Trade Organisation (WTO) in Defence procurement:

“World Trade Organization’s Agreement on Government Procurement prohibits the use of offsets in government procurement generally, but explicitly exempts a nation’s “action... 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 defense purposes”
 (Presidential Commission on Arms Trade Offsets, 2001: 13).”

As such the practice is well spread as seen by the Chart below by the Offset research company “Avascent”, presenting a forecast for Offset Obligations from 2005 to 2016.



Source: Avascent

“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 defense purposes”

Industry involvement by another name?

“Offset has become a dirty word; the industry now prefers the euphemistic industrial participation”

Notwithstanding the above, Offsets are often frowned upon, particularly by typical Defence exporters, and described as a protectionist anti free trade practice. The May 25th 2013 edition of the Economist magazine included an article by the title: “Guns and Sugar”. The article is critical of the use of Offset policies. It states:

“Offset” has become a dirty word; the industry now prefers the euphemistic “industrial participation”.

It is often argued that introducing obligatory limits and targets for local industry involvement, rather than “best endeavors”, the policy becomes an “Offsets” policy. However, the objectives and results matter more than the name or title of the policy. Indeed, in international forums, Defence researchers and multi-national prime contractors, active in the Australian Defence market, call our AIC and GSC programs the “Australian Offsets”.

Asia-Pacific Aerospace Report, 1 May 2013, included the following article:

“Offset Deal Emphasises Poor Australian Contract:

A 10-15 year offset deal worth US\$2.5 billion signed by progressive Israeli Aircraft Industries (IAI) and Lockheed Martin to build wings for the F-35 Joint Strike Fighter has given emphasis to the poor contracting for JSF component production carried out by the Australian defence department.

Lockheed Martin recently told the Australian industry that if the country's JSF order is reduced from the planned 100 the work allocated to local industry will be cut proportionally. Australian JSF businesses contracts are now worth A\$300m. Australia may soon order more Boeing F/A-18F Super Hornets which

will reduce its financial and operational capability to acquire the 100 JSFs originally proposed. It has been suggested the JSF order may be cut to 50 units.

Israel is a Security Cooperation Participant and signed a letter of agreement in 2006 paying US\$20m for its involvement. Australia paid A\$150m for its participation in the project as a Level three participant in 2002....”

Questioned later on that article at the Hunter Defence Conference 22 May 2013, Lockheed Martin asserted that this was not an “Offset” deal. For Industry however, it did not matter what the deal was called. What matters is that it was a contractually binding package of work, given to Israeli industry as a result of Israel's acquisition of the F-35 Joint strike Fighter.

As such, this paper looks into offsets practices and similar policies implemented globally. The purpose of this is to highlight:

- some aspects that might be considered and adopted as adjustments to existing relevant Australian programs; and
- possible additional measures to ensure fairness for Australian industry when competing for the Defence funds invested by its own tax payers.

Case studies

CANADA

Canada implements the Industrial and Regional Benefits (IRB) policy. The policy is explained in details on the “Industry Canada” website:

http://www.ic.gc.ca/eic/site/042.nsf/eng/h_00016.html :

“The IRB Policy ensures that Government of Canada defence and security procurements generate high value-added business activity for Canadian industry. The IRB Policy requires companies undertake business activities in Canada valued at 100 percent of the value of the defence or security contract they have been awarded by the Government of Canada. The IRB obligation is a contractual commitment and part of the overall government procurement contract.”

Following are some of the examples listed in that website: of them:

CF-18 Modernization Project

IRB Contractor: The Boeing Company
Total IRB obligation: \$372 million
Timeline: December 2000-December 2008

Examples of type of work:

- Direct: L-3 MAS (Quebec) — installation work of the radars and displays
- Indirect: ASCO and Avcorp (British Columbia) producing parts for Boeing Commercial Division

Jroberts Manufacturing Inc.

Daimler, and its Canadian division Mercedes-Benz Canada, delivered its G-Wagon to the Canadian Forces in 2004 and provides in-service support through contracts under the Light Utility Vehicle Wheeled (LUVW) project. As part of its IRB obligation, Daimler is working with Jroberts Manufacturing Inc., a precision machining and fabrication company located in Woodbridge, Ontario. Jroberts has performed design upgrades, manufacturing and overhaul services to the LUVW vehicle's turret assembly.

For Jroberts, the LUVW success reflects years of hard work, wherein Jroberts thoroughly researched Daimler and its LUVW vehicle, proactively engineered an improved turret and sold the idea to Daimler officials. Jroberts is now

reaping the benefits of increased employment and the opening of a new repair and overhaul facility operating a CARC (chemical agent resistant coating) system in Toronto. Jroberts is delivering technical solutions for military work in other areas.

Mil-Aero Electronics

Mil-Aero Electronics, located in Dartmouth, Nova Scotia specializes in the manufacture and integration of high performance electrical assemblies, build-to print electrical cables and harness assemblies, electrical control boxes and other value-added parts for the defence, aerospace, and industrial markets.

Raytheon Space and Airborne Systems has contracted Mil-Aero for the production of Radio Frequency cable assemblies. Mil-Aero's success with this work has positioned the company to participate in future opportunities, not only with Raytheon but with other leading international aerospace and defence manufacturers.

This relationship was developed because of Raytheon's Industrial and Regional Benefits (IRB) obligations to Canada as a result of the CF-18 Defensive Electronic Warfare Suites project. For Mil-Aero it has provided the opportunity to integrate into the supply chain of a world leader in the industry, and to demonstrate the quality of their products and services to other global contractors.

FINLAND

The Ministry of Defence of Finland introduces “Defence Materiel Industry and Industrial Participation” as follows:

http://www.defmin.fi/en/tasks_and_activities/resources_of_the_defence_administration/defence_materiel_industry_and_industrial_participation

“DEFENCE MATERIEL INDUSTRY AND INDUSTRIAL PARTICIPATION

The Finnish defence materiel industry plays an important part in the upholding and development of the Defence Forces.

When the Finnish Defence Forces make large purchases of defence material from foreign suppliers industrial participation (formerly offset deals) is required. Supply contracts are subject

to the condition of offset usually when the value of the procurement exceeds 10 million. Industrial participation is designed to safeguard domestic security of supply. The aim is to involve the industry in materiel and technology projects already at the planning stage.

The Finnish defence materiel industry must manage three areas of competence that are essential from the point of view of defence

- *The assemblage, maintenance and repairing of large, technologically demanding systems*
- *The management of information systems technology and systems integration*
- *Availability (and if necessary, manufacture) of critical components and spare parts*

In any case competence in gunpowder and ammunition production and in various production methods will continue to be needed in Finland in the future. This competence could be maintained in, for instance, centres of excellence jointly run by the industry, research institutions and defence administration.”

Case studies

UAE

In 2012, UAE Offset Programme Bureau renamed as Tawazun Economic Council. Tawazun establishes Joint Venture companies with multinational companies, creating local capabilities. The multinationals may only own 49% of the company, and are given offset credits relevant to the degree of success of the companies created.

Tawazun Economic Council's Abu Dhabi International Offset Conference 15 Feb 2013:

"The booming strategic manufacturing industry in the UAE is being driven by robust and long term partnerships between government and global and local private sector industrial leaders. A recent example is the creation of Tawazun Dynamics, which is a joint venture between Tawazun and the Dynamics division of Denel, owned by the Government of South Africa and South Africa's largest defense manufacturer. Tawazun Dynamics is focused on the production of eight different configurations of its flagship product, the Al Tariq System, which is a precision guided weapons system being designed, developed, manufactured and assembled in the UAE."

Tawazun website includes many other examples of companies established with most of the Defence global multinational companies.

USA

The May 25th 2013 edition of the Economist magazine included an article by the title: "Guns and Sugar", while critical of the use of Offsets policies by the buyers, adds:

"America has long been officially against offsets, though it practices something similar at home under the Buy American Act of 1933, which requires foreign armsmakers to source much of the work locally. (Some circumvent the rules by forming partnerships with American contractors in order to qualify as domestic suppliers.) And as embassy cables published by WikiLeaks make clear, America's diplomats are sometimes closely involved in its firms' discussions with foreign governments, including even squeaky-clean Norway's, over proposed offsets."

In fact, the USA is using a number of legislations and practices to offer advantages to its own Defence industry against any potential off-shore suppliers, making it extremely difficult to compete against a US company in the USA. Those measures include:

- **Buy American Act, including the Berry Amendment.** Congressional Research Service, Domestic Content Legislation: The Buy American Act and Complimentary Little Buy American Provisions (April 25 2012): "Essentially, the Buy American Act attempts to protect domestic labor by providing a required preference for American goods in direct government purchases. In determining what are American goods, the place of mining, production, or manufacture is controlling. The nationality of the contractor is not considered when determining if a product is of domestic origin. Manufactured articles are considered domestic if they

have been manufactured in the United States from components, "substantially all" of which have been mined, produced, or manufactured in the United States. The term "substantially all" is defined in the regulations to mean that the cost of foreign components does not exceed 50% of the cost of all components."

"The Berry Amendment is a "super percentage" statute which requires that certain purchases of the Department of Defense be 100% American in origin. The Berry Amendment is an example of a provision where Congress has decided that a greater percentage of American content should be required in acquisitions that are subject to the "big" Buy American Act."

- **Little Buy American Provisions.** Congressional Research Service, Domestic Content Legislation: The Buy American Act and Complimentary Little Buy American Provisions (April 25 2012): "Congress has enacted "Little Buy American Acts" to restrict procurements that do not fall under the application of the Buy American Act or to adjust the percentage content standard. The Buy America Act, which attaches a domestic content requirement to purchases made with federal transportation funds, is illustrative of provisions that govern purchases not made directly by a federal entity, but which use federal funds. The majority of the Little Buy American Acts are this type of legislation. Unless the provisions specifically reference the definitions of the Buy American Act, they generally require the purchase of 100% American made products."

Case studies

- **Buy America Provisions** US Department of Transportation Website, <http://www.dot.gov/highlights/buyamerica> : "The Department of Transportation is committed to maximizing the economic benefits of the Obama Administration's historic infrastructure investments through Buy America provisions that keep American companies healthy and families working. Buy America provisions ensure that transportation infrastructure projects are built with American-made products. That means that Department of Transportation investments are able to support an entire supply chain of American companies and their employees."

Furthermore, the US offers loans, grants, surety bonds, venture capital and other financial assistance to its own SMEs through the US Small Business Administration (SBA). The assistance also extends to contracting advantages offered through a wide range of programs including:

- Small Business Set-Aside (SBSP)
- Service-Disabled Veteran-Owned Small Business Set-Aside,
- Women Owned Small Business WOSB Set Aside
- Economically Disadvantaged Women Owned Small Business EDWOSB Set-Aside
- Historically Underutilized Business Zone (HUB Zone) Set Aside.

The U.S. Department of Commerce, Bureau of Industry and Security produces an annual report "Offsets in Defense Trade" to Congress. The Executive Summary of the February 2013 report states:

This report notes that exports of defense articles and services can: lower overhead costs for the Department of Defense; help sustain production facilities, workforce expertise, and the supplier base to support current and future U.S. defense requirements; promote interoperability of defense systems, subsystems and components between the United States and friends and allies; and contribute positively to U.S. international account balances.

However, offset agreements and associated offset transactions can negate some of the potential economic and industrial base benefits accrued through defense exports if the offset activity displaces work that would otherwise have been conducted in the United States.

It is fair to conclude that this perceived loss to the seller, at least partly, is a gain for the buyer.

The December 2007 version of that report contains the information in the table over the page. It includes Australia as one of the offsets countries based on our former All program. The minimum value of contract (threshold) attributed to the Australian program seems to be mistakenly based on the discontinued Australian Offsets Program, which was AUD\$5 million, around US\$3.75 million in 2007 figures. It is interesting to note the minimum offset required by Australia (nil), compared to the rest of the world.

“the US offers loans, grants, surety bonds, venture capital and other financial assistance to its own SMEs through the US Small Business Administration”

Case studies

S.No..	Country	Title of Policy	Minimum Value of Defence Contract	Minimum Offset Required	Offset Sector	Multiplier
1	Australia	Australia Industry Involvement Programme	US \$3.75 million	No Specific Min. of Max	Defence	None in policy
2	Canada	Industrial & Regional Benefits Policy		100%	Defence & Civilian	None in policy
3	Finland	Industrial Cooperation Program		100%	Defence	0.3-3 for exports of finish products; for others multipliers are negotiated
4	Greece	Policy of Offsets Benefits	10 € million	120%	Defence	Up to 10
5	Israel	Industry Cooperation Program	US \$0.5 million	35%	Defence & Civilian	1-1.5
6	Italy	Not Codified	US \$6.6 million	Not less than 70%	Defence	Maximum of 3
7	Netherlands	Industrial Benefits and Offsets Policy	5 € million	100%	Defence & Civilian	Negotiable; ranges of 1-5, 5-10, and 10-30
8	Norway	Guidelines for the Establishment and Implementation of Offsets in Connection with Defense Procurements	US \$6.7 million	100%	Defence & Civilian	0-5
9	Poland	Korean Defense Offset Program	5 € million	100% (defence 50% min)	Defence & Civilian	Negotiable up to 2-5%
10	South Korea	Policy of Armament and Material Agency	US \$10 million	30%	Defence	Determined by authorities
11	Spain	Spanish Offset Policy	NA	100%, but may vary	Defence & Civilian	Between 2 and 5, when used
12	Switzerland	Industrial Cooperation Program	US \$17 million (may vary)	100%	Defence & Civilian	Maximum of 2-3
13	Taiwan	Industrial Participation/Offset Directive	US \$10 million	Will be increasing to 70%	Defence	1-10
14	Turkey	Industrial Participation Policy	US \$10 million	50%	Defence & Civilian	1-5
15	UK		US \$17.2 million; £50 million for French & German Companies	100% target	Defence	No multiplier for IP credit

Source: U.S. Department of Commerce, Bureau of Industry and Security, "Offsets in Defense Trade: Twelfth Report to Congress", December 2007.

Case studies

SOUTH AFRICA

South Africa runs a Defence Industrial Participation program linked to its Strategic Defence Packages (SDPs) of 1999. It has been reported on recently by the South African Aerospace Maritime & Defence Industries Association in their paper of July 2014 "The Impact of Defence Industrial Participation (DIP)". It states that DIP injected some R15 billion into South African defence companies in the decade following 1999.

DIP requirements include both direct and indirect DIP. Indirect DIP focused on export facilitation and technology transfer to achieve longer-term benefits for industry. Direct DIP resulted in work placed in South African industry across a range of aerospace projects, munitions, combat systems, optronics, telemetry and other systems and components. Indirect DIP achieved exports and establishment of facilities across a similar range of capabilities. Spin-offs have included substantial investment in new design and manufacturing capabilities across a range of technologies.

Despite the clear benefits achieved for South African industry, it was noted that a lack of a nationally focused industry policy resulted in some of the investment occurring in areas that were not sustainable in the longer term. It was also considered that better outcomes would have occurred if more South African SMEs had been involved in the programs, rather than just primes and major sub-contractors. The report concluded that a carefully planned and focused mandatory program of industrial participation has the potential to be a "business multiplier" for local defence industry, and for general manufacturing and service areas.

OTHER COUNTRIES

The paper "A Survey of Successful Offset Experiences Worldwide" by Anuhadra Mitra in Journal of Defence Studies Vol.3 No. 1, explores how Offset Policy may be tailored to suit national industry objectives. It examines Offset success in Saudi Arabia, Israel, Japan, Spain, and Brazil, and how the structure of the programs varied to suit national objectives:

- Saudi Arabia – their objectives were to achieve technology transfer; private sector business, partnerships and joint ventures to strengthen the economy. The country did not have a skilled workforce to undertake direct offsets. Instead they concentrated on establishment of industry and R&D for commercial and dual use products with a wider market. They were able to achieve many of these objectives through a number of large defence purchases;
- Israel – here the objective was to foster close cooperative work between Israeli and foreign firms in strategic partnerships that would lead to integration of local firms into global supply chains. Their program formed a significant part of their transformation from an agrarian to a fully industrialised economy in some 50 years;
- Japan – following WWII, Japan pursued an overall policy of technology transfer to establish industry then further develop it to a position of world leadership. A significant part of their success in this came through defence offsets, particularly with the USA;

- Spain – the Spanish used their offsets program for re-industrialisation to meet European standards in their defence industry. They used: designated offsets in aircraft projects; co-production in aerospace projects locally and in global supply chains; and indirect offsets in both defence and commercial technologies;

- Brazil – the Brazilian aim was self-sufficiency in national security. Their offsets objectives include technology transfer; licensed production, co-production and joint ventures for its defence industry. They have been successful in this.

Finally, the prevalence of offset programs worldwide can be seen in a report produced by the Australian Defence Materiel Organisation (DMO) in March 2010. It documents details of offsets programs in 53 countries. An edited version can be found at Attachment 1.

General conclusions from other country offset programs

From the case studies above and in the attached paper, it is clear that:

- Long-term industry benefits can be obtained from offsets programs. Benefits may include:
 - direct technology transfer and licencing
 - establishment of licenced production, co-production, joint ventures and partnerships through which technology is transferred, capability created and ongoing investment in R&D and know-how made to ensure the long term viability of the capability
- fostering greater involvement in global supply chains
- economic development including industrialisation and job creation
- creation of dual-use and commercial capability and strategic civil industries
- long term strategic partnering between national and foreign companies
- establishment of technological self-sufficiency
- There are generally costs associated with achieving offset benefits. These may take the form of direct funding by specific government programs to aid in establishment of capability, tax breaks and holidays, and premiums in prices for local goods and services
- Broader economic benefits, multiplier effects on local work and taxes collected on profits, wages and goods and services may offset some or all of the costs
- Offset programs can be tailored to meet the particular needs of nations and should be strategically focussed to do so.

Australian experience

Defence had an offset program, with the threshold of \$5m. This program was discontinued as a result of the Defence Strategic Review of 1993 and a review in 1994 by the Industry Commission into Defence Procurement Industry Programs. Based on that report, the Defence Industry Policy Statement 2010 argues against Offsets, presenting Case Study 6:

Why Offsets Don't Work, with the 1981 F/A-18 Hornet program as an example.

But a number of questions should be examined:

- **Was it a complete Failure?**
While the industry participation program did not deliver as many benefits as it should have, it is not entirely to conclude that it was a total failure. Much of the current Australian Aviation industry capability can trace its roots to that program. While Hawker de Havilland (HDH), Government Aircraft Factory (GAF), and Commonwealth Aircraft Corporation (CAC) no longer exist, the capabilities and the know-how acquired by those companies through the F/A-18 and other defence and civil offset programs are now the back-bone of Australian Aerospace and Aviation industry capabilities. Much of the expertise gained is now at work in a number of Aerospace/Defence companies in Aero-structure, Radar, upgrade, support, MRO and other related capabilities.
- **Were the failures in the policy or the implementation?**
Instead of dismissing the concept of offsets altogether, with the benefit of hindsight we can identify the shortcomings of our earlier Offset Program, and make sure that any future industrial involvement measures do not fall into the same traps. As an example,

Australian experience

we should include contractual obligations to make sure that the benefits gained are enduring, the capabilities established are applicable beyond the particular project, and that technology transfer obligations are adhered to.

- **Did the Department of Defence use its buying power effectively?**

The total premium paid by Defence in the case of 1981 F/A-18 was quoted as 17% of the acquisition and support costs. However, according to "The Arms Trade as Illiberal Trade by Ann Markusen (2001)", premiums are typically between 7 and 10% of the contract value. This is another case of the Australian Defence Department lack of ability to leverage its buying power in dealing with multi-nationals. The 17% additional cost to Defence does not take into consideration the additional Tax clawbacks from Personal Income Tax and Company Income Tax when considered on a whole of Government basis.

The Current Environment for Australia

It is acknowledged that an offset program under any title would have some cost associated with its implementation. However any associated costs must be weighed against the benefits returned. In a whole of government approach, economic benefits such as job creation, export opportunities, technology transfer and the associated multiplier effects should not be ignored. They should be measured along with the enhancement to self-reliance that the additional industry capability would bring.

As we can see from the experiences of other cases above, offsets or other industrial involvement measures should not have to amount to a net premium paid by the Australian tax payer. Long term, it can actually pay both capability and economic dividends.

In a Boeing presentation to the Abu Dhabi International Offset Conference, 19 Feb 2009, Mr Dennis Swanson, Regional Director, Industrial Participation and Alliances described the arrangement as "Focused on Win-Win-Win Collaborative Relationships" noting that:

- "Multiple opportunities to create value across the region through offset initiatives.
- Developing opportunities takes time to mature.
- Well-structured offset initiatives can become strategic long-term partnerships."

It should also be acknowledged that, with most of Australia's potential partners in very large joint military projects already requiring offsets programs in their share of the projects, Australia may in fact pay a premium for not having a similar program. This will arise as contractors will prefer to place work where it meets their offset obligations, and consequently are likely to pay a premium to do so. Australia will both pay that premium in its price, and fail to support an Australian capability that otherwise may have provided the best value for money.

“It should also be acknowledged that, with most of Australia’s potential partners in very large joint military projects already requiring offsets programs in their share of the projects, Australia may in fact pay a premium for not having a similar program”

An Australian industry involvement program

It is considered from the case studies and analysis presented above, there is a strong case for Australian implementation of its own Industry Involvement Program (IIP). The question becomes what form of Program would suit Australia best. Given the mature and broadly based industrial capabilities already existing in Australia, there is not a strong case for a Program aimed at broader economic benefit, or any particular commercial technologies. Clearly the focus should be Defence self-reliance. And self-reliance objectives would themselves be focussed on platform enhancement and adaption, and through-life support.

As the existing industry policy already contains two specific policies aimed at self-reliance – the Australian Industry Capability (AIC) and Global Supply Chain (GSC) policies – the most beneficial approach would likely be to expand their requirements by incorporation of an IIP within them. The primary features of the IIP

in each of these programs might be:

- **Australian Industry Capability Enhancement**
The current AIC Program would first be expanded by incorporation of the Strategic Sourcing Program as proposed by AIDN. Then, mandatory targets expressed as a percentage of project cost could be enforced where the enhanced AIC Plan falls short of the target
- **Global Supply Chain Enhancement**
The current “best endeavours” GSC deeds with prime contractors could be replaced by similar deeds but with mandatory targets expressed as a percentage of the value of Australian contracts held by the primes and could be enforced where GSC outcomes are falling short of the target. Successes achieved could count towards meeting their enhanced GSC and their enhanced AIC obligations as applicable.

The clear attraction and benefits of implementing such an IIP must still be balanced against any premiums associated with its implementation. Further, short term project benefits and costs should not override achievement of longer term self-reliance objectives.

As there is currently insufficient data to support the implementation of such an IIP to meet Australian requirements, more research is needed to structure a program that could leverage from the benefits achieved by overseas programs and maximise enhancement to self-reliance.

Recommendation

Investigation is recommended into the implementation of an Australian Industry Involvement Program including possible enhancement of the current Australian Industry Capability (AIC), and the Global Supply Chain (GSC) Programs by introducing minimum obligatory limits to be achieved as contractually binding

deliverables. Investigation should include research into:

- How overseas programs are able to maximise benefits while avoiding premiums and costs, and

- The best structure for an Australian IIP to achieve long-term self-reliance objectives

Attachment I Comparative defence offset policies - DMO March 2010 (edited)

Country	Minimum Threshold	Level of Offset Obligation	Offset Preference	Discharge of Offset Requirements	Penalties for Non-Performance
Argentina		100%			
Austria	EUR 700,000	100%	Direct and indirect	5-15 years	5-10 % of undischarged obligation
Belgium	EUR 2.7 million or EUR 11 million	Bidders free to to offer a level	Direct and indirect	Contract period plus 1-2 years	10 percent
Brazil	USD 1 million	Often 100-120%	Direct, with aeronautics industry focus		
Bulgaria	EUR 5 million or EUR 2.5 million.	Minimum 110% with ratio of the direct to indirect of 30% to 70%.	Direct and indirect	10 years maximum	
Canada	No official offset policy	Encourages to 100% via Industrial and Regional Benefits Policy	Direct and indirect		
Chile					
China	No formal offset policy		Technology transfers, licensed production, licensed assembly, R&D programs		
Cyprus	No offsets policy				
Czech Republic	CZK 500 million prime contracts, CZK 250 million sub-contracts	100%	Direct and indirect	10 years maximum	
Denmark	DKK 25 million (~ USD 4.96m)	100%	Direct and indirect	30 percent to be discharged in 4 years	Remaining payable on non-performance.
Estonia	EUR 9.59 million	100%	Direct and indirect	Within contract period	120% of undischarged obligation
Finland	EUR 10million	targets of 100%.	Direct	Contract plus 1-2 years	Penalties applied
France	No offsets policy				

Attachment I

Comparative defence offset policies - DMO March 2010 (edited)

Country	Minimum Threshold	Level of Offset Obligation	Offset Preference	Discharge of Offset Requirements	Penalties for Non-Performance
Germany	No offsets policy		Direct offsets as cost/work share in cooperative programs.		
Greece	EUR 10 million (prime and subcontracts)	100%	Direct and indirect. Defence-related.	Within contract period	10 percent of the unfulfilled portion
Hungary	HUF 1 billion (~EUR 3.5m)	100%	Direct and indirect	Contract period plus one year	
India	INR 3 billion (USD 64.9m)	30%. higher if strategically important	Direct and indirect	Within contract period	
Indonesia	No offsets policy				
Ireland	No offsets policy				
Israel	USD 5 million	50%	Direct and indirect	Within contract period	Prevented from competing for future contracts if unfulfilled
Italy	EUR 5 million	70 to 100%	Direct and indirect. Defence-related.	Contract period plus additional case by case	Up to 10% of the unfulfilled obligation
Japan	No offset policy	Industrial participation case by case			
Jordan	No official offset policy				
Kuwait	KD 3 million	35%	Direct and indirect	8 years	6 percent of the total contract value
Latvia	No offset policy				
Lithuania	5 million Litass (~EUR 1.5m)	100%	Direct and indirect	10 years maximum. 50% in first 5 years	
Luxembourg	No formal offset policy, but may form part of the supply contract.		Direct	10 years	
Malaysia	EUR 10 million	50%	Direct and indirect. Direct preferred		

Attachment I

Comparative defence offset policies - DMO March 2010 (edited)

Country	Minimum Threshold	Level of Offset Obligation	Offset Preference	Discharge of Offset Requirements	Penalties for Non-Performance
Malta	No offset policy				
Netherlands	EUR 5 million	100%	Direct and indirect.	Generally within the contract period, but not exceeding 10 years.	Failure to meet milestones may result in 15-30% of the unfulfilled portion.
New Zealand	No offsets policy	Tenderers may voluntarily make offset proposals			
Norway	NOK 50 million (EUR 5.618m)	100 % with 50% strategic	Direct and indirect	10 years.	10%
Pakistan	Major programs	30%			
Poland	EUR 5 million	100%	Direct and indirect. Direct > 50%	10 years maximum	
Portugal	EUR 10million	100%	Direct and indirect. Priority sectors	6-8 years.	Up to 15 % of contract value. May be barred from future contracts.
Romania	EUR 3 million	80%	Direct and indirect	Contract period plus 2 years	
Saudi Arabia	Not specified	Minimum of 35% to > 40%.	Direct and indirect	10 years	
Singapore	USD 10 million	25-30%.	Direct, with indirect in isolated cases	Up to 10 years.	typically 3-5% to 10% of unfulfilled obligation
Slovakia	EUR 6 million prime contracts, EUR 3 million sub-contracts	100 percent	Direct, semi-direct and indirect,	5 years.	7% of the undischarged portion
Slovenia	EUR 400,000	100%	Direct and indirect	5 years.	Value undisclosed
South Africa	USD 2 Million	Defence Industrial Participation. USD 2-10 million: 80-100%	Direct and indirect.		
South Korea	USD 10million	50%	Direct and indirect. Also technology transfer and R&D collaboration	Offset banking allowed up to 5 years.	

Attachment I

Comparitive defence offset policies - DMO March 2010 (edited)

Country	Minimum Threshold	Level of Offset Obligation	Offset Preference	Discharge of Offset Requirements	Penalties for Non-Performance
Spain	EUR 1 million	100%	Primarily direct	Within contract period	
Sweden	SEK 100 million (EUR 9-10 million)	100%	Direct and indirect	Within contract period	
Switzerland	USD 18million	100%	Direct and indirect	Contract period plus 3 years	
Taiwan	USD 5 million	40%	Direct and indirect		
Thailand	No official offset policy				
Turkey	USD 5 million	50%	Direct and indirect	2 years maximum	
UAE	USD 10 million	60%	Indirect.	7 years.	8.5% of the undischarged portion.
United Kingdom	No formal offset policy. EUR 1.2 million	100% on a case by case basis	Direct	Within contract period	
United States	No formal offset policy				
Vietnam	No formal offset policy	Technology transfers			



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