

## **Procurement Procedures for Defence Capital Projects**

### **The DCP**

The Defence Capability Plan (DCP) is a practical document and one of the fundamental sources of inputs to the strategic planning processes of Sonartech ATLAS Pty Ltd (STA). The DCP provides a level of insight into defence procurement that is not always available in other markets our company competes in..

There has been commentary elsewhere regarding whether the Commonwealth should disclose actual funding provisions within the DCP and whether this might compromise the Commonwealth's commercial position. Rather than provide this funding data STA has the view that greater benefit could be obtained through the DCP providing more detail of the Commonwealth's expectations on delivery, better fidelity in project timelines and allocation of priorities for listed projects.

In their current form the DCP funding brackets are interpreted by STA as a less than perfect predictive tool to glean the intent of the Commonwealth in relation to a particular project. A greater level of detail regarding the Commonwealth's expectations on the outcomes or deliveries would help to minimise ambiguity with potential benefits for both defence and industry.

The lack of fidelity of the timelines within the DCP can make it difficult for a business to commit to a particular course of action including the planning and implementation of investment options whether it be plant and equipment, overall capacity and/or skills development. This lack of clarity can place additional financial risk or burden on potential suppliers, which often results in the company deferring related investment or worse not conducting such activities.

The basis for 'over planning and over programming'<sup>1</sup> is understood; however, STA notes that it could create another opportunity for potential suppliers to make planning decisions relying on inaccurate or inadequate data. As it stands, it is not possible for a business to determine the priority order of the projects within the DCP; i.e. the risk a project could be progressed or slipped dependent on other higher priority projects. This can be a significant issue if the project a potential supplier is pursuing and investing for is a lower priority project with less likelihood of advancement.

### **Competition**

The Defence Procurement Policy Manual (and the Commonwealth Procurement Guidelines on which it is based) establishes clear guidelines for the conduct of government procurement activities. Both documents are prescriptive about the importance of establishing and utilising fair and ethical procurement practices which aim to achieve value for money. This sound principle of value for money is shared with industry and a fundamental concept behind private enterprise expenditure as well.

Competition is a tool that assists the Commonwealth to ensure it meets the requirements for Commonwealth Procurement and has been stated as a primary mechanism to ensure potential suppliers do not unreasonably exploit the financial data the Government makes publicly available.

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<sup>1</sup> Defence Budget Audit pp 9

STA keenly supports the principle of competitive tendering for major equipment procurement, however in doing so, emphasise that realistic schedules should be defined and then maintained as required in normal project management based activities. In determining the cost of procurement and assessing the associated value for money, there could be benefit in including the cost of the procurement process as an element of the overall project cost and considered as a part of the whole activity.

STA recognises the Commonwealth's preference for competitive tendering, noting that this observation has also been recognised previously by the Department and finds comfort that it is reported in many of the external reviews that have been conducted.

## **Timelines and Schedules**

There have been many examples that demonstrate how difficulty in developing and maintaining a schedule for procurement places additional pressures on both the department and industry; and this issue has the potential to undermine the departments efforts to obtain value for money in procurement. In fact Dr Gumley, the CEO of the DMO, has often publically stated that his "*biggest problem is schedule*"<sup>2</sup>, though he is referring to the acquisition phase of the lifecycle there are many cases where this would also be true of the needs and requirements phases of the lifecycle. This difficult situation can be made worse if the planned capability is to replace an existing asset, with great and additional demand being placed on the sustainment budget.

Longer schedules for procurement can have a marked impact on the efficiency and effectiveness of the procurement activities, or more precisely the longer the exposure the greater the likelihood of an issue. Within the context of defence procurement exposure is the time it takes from identification of a capability need or deficiency to the time a decision is made on procurement and an issue is an event which has a negative impact on the activities thus far. As this time period is extended the more difficult it can be to define and manage the procurement activities, coupled with the increased likelihood for changes to occur, in turn this can undermine previous work by both industry and the department. This is briefly discussed in the context of the following aspects:

- Business Planning
- Capability Development Staff Tenure
- Rate of change in technology

## **Business Planning**

Much has been said about the need for local defence industry to up-skill and invest in order to be well placed to address the needs of the ADF. When considering such investments a company must prepare a business case which outlines the cost of the investment, the mechanism for investment and the risk attached to the investment. Any variability or instability in the defence procurement timelines or schedules makes the preparation of accurate and reliable business cases for investment difficult if not impossible; the seemingly endemic variability and instability of contemporary defence procurement timelines makes investment decisions extremely difficult for small and medium size enterprises (SME's). The SME's are an important element of the Australian industrial base employing approximately

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<sup>2</sup> Dr Stephen Gumley, CEO DMO, speech to the ADM Congress 17 Feb 2009

50% of the 29,000 persons working in Defence Industry<sup>3</sup> and are acknowledged as a “*vital source of innovation and niche capability in the local defence marketplace*”<sup>4</sup>.

There is of course a cost to training or up-skilling a workforce; there are the direct costs (sourcing the training, allowances, training materials, etc), the indirect costs (mentoring, supervising, continually growing staff, etc) and the opportunity costs (loss of staff whilst they undertake training). This issue has been recognised by the Government and a number of schemes and mechanisms, e.g. the Skilling Australia’s Defence Industry (SADI) Program, have been established to assist potential suppliers with the costs of improving their skill base. Nevertheless extended and delayed procurement timelines can still have a negative impact on suppliers beyond recovering or offsetting cost, e.g. staff leave to seek more dynamic market segments/industries: .

There are also some domains that are quite unique to defence and the required knowledge or skills is not readily available in the commercial market place. In these areas staff must be internally grown or developed and the absence of relevant work and opportunities makes this difficult at best. In terms of cost this is an area that programs such as SADI are aimed at addressing, however newly trained industry staff must be able to consolidate and practise their newly learned skills or what was learned is lost.

The situation is worse for smaller businesses that have less ability to absorb additional expenses, whether the costs relate to training or sustainment of non-income generating resources; and this ultimately could result in a forced reduction of their workforce.

In the worst case the result may be little if any lasting value obtained from the investment expenditure and ultimately neither defence nor industry benefits.

## **Capability Development Group Staff Tenure**

STA makes the following observations with the understanding that Defence works diligently to avoid unnecessary posting turbulence; even so the impact of changing staff within departmental and project offices is worthy of attention..

Extended project timeframes inevitably result in a large number of different uniformed and even public service personnel working on a Defence project; this can be disruptive both in terms of the projects progression and in some cases its direction.

Service or uniform personnel nominally have an 18-24 month posting cycle. The Defence Procurement and Sustainment Review Report stated that the average period of service within CDG for was 18 months<sup>5</sup>. STA notes that in 2009 Rear Admiral Thomas initiated a change to the posting cycle for Naval Officers with the rank of Commander or Captain posted to shore billets; this change, extended the relevant posting period to 36 months, which was a sensible attempt to provide consistency and continuity in senior officer shore postings. It is assumed that this 36 month posting cycle also applies to Naval personnel of the requisite rank within the Capability Development Group.

A comparison of this typical uniformed officer posting period (18 months as stated in the Defence Procurement and Sustainment Review Report) in relation to the timeframes for a procurement proposal is of interest e.g. process of progressing from 1<sup>st</sup> Pass consideration to 2<sup>nd</sup> Pass consideration, recognised as taking “around two years”<sup>6</sup> within an overall timeframe

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<sup>3</sup> Building Defence Capability: A Policy for a Smarter and More Agile Defence Industry Base pp 28.

<sup>4</sup> Building Defence Capability: A Policy for a Smarter and More Agile Defence Industry Base pp 29.

<sup>5</sup> Defence Procurement and Sustainment Review Report pp 24

<sup>6</sup> Defence Capability Development Manual 2006 pp 31

of 10 years from the time a Project is approved for inclusion in the Defence Capability Plan to approval of a specific solution at Second Pass<sup>7</sup> is not uncommon. It could be suggested that the time uniform personnel spend within the Capability Development Group, under such a posting cycle, may be insufficient for them to have any marked affect on the outcome of a Major Project. In fact the time they are in a position to influence the activities that occur whilst the project is under the direction of the Capability Development Group, could be less than a quarter of the lifecycle.

The ability of an officer to positively influence can be diminished further if that officer has limited experience with the processes and mechanisms by which the Department conducts its procurement or the activities required to support such procurement. The limitations of an officer's knowledge or experience in procurement may be reduced but cannot simply be offset by extending the 'handover' period i.e. the time available for the outgoing officers to brief their incoming relief on the status of projects they are responsible for and/or to educate them on the steps they must undertake to ensure the project is 'ready' for its next point of consideration. There may be justification for establishing a sub-specialisation in Capability Development or Capital Procurement for uniform personnel, such that they could build up experience in this crucial area before they're required to take a more primary role.

## **Complexity, Maturity and Risk**

The work and administrative overheads required to comply with procurement guidelines should be commensurate with the complexity, maturity or risk associated with the project, whilst satisfying the requirements of Commonwealth Procurement.

In many reviews of and forums covering defence procurement it has been recognised that projects have differing levels of complexity, maturity or risk and that in certain cases it may be more appropriate to establish or utilise a shortened or simplified procurement process. This would have many benefits but could also reduce the administrative burden and help ensure staff have time to properly address the business cases and problems of relevance to more complex procurement.

The Defence Capability Development Manual in principle, through reference to combined 1<sup>st</sup> and 2<sup>nd</sup> Pass considerations, supports the concept of a shorter lifecycle, as does the Defence response to Recommendation 2.2 of the Mortimer Review, which sought to expedite the capability development process. These indicate recognition of the potential problem and of the desire to improve the process. This aspiration to rationalise and expedite the capability development process is applauded and encouraged.

In closing it is also worth considering the rate of change in technology when trying to determine the complexity, maturity and risk as it can be an issue in itself. Moore's Law, often cited as a basis for the rate of change in technology, states that the processing power of computers doubles every two years<sup>8</sup>, this only part of the issue as technology is more than just processing power. An example that may help put this in context exists with MicroSoft, Windows Millennium was released in 2000 and Windows 7 in 2010 in between these Operating Systems was Windows XP and Windows Vista. Such technology jumps can have substantial impacts on procurement outputs and outcomes over longer term schedules. When considered against the 10 year procurement lifecycle, the underlying technology may have undergone four possibly five iterations, from the time the project was included in the

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<sup>7</sup> Defence Capability Development Manual 2006 pp 29

<sup>8</sup> 'Moore's Law' originally related to the number of transistors that could be inexpensively placed on an integrated circuit.

DCP up until the Government approves it at 2<sup>nd</sup> Pass, let alone introduction into service. The likelihood of changes in technology provide potential to undermine the work done by Defence staff and industry through the earlier stages of the Needs and Requirements phases, forcing reassessment, revalidation and/or update of this work in the latter periods.

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12<sup>th</sup> April 2011