



Auditor-General for Australia



23 January 2024

The Hon Shayne Neumann MP  
Chair  
Joint Standing Committee on Foreign Affairs, Defence and Trade  
By Email: [jscfadt@aph.gov.au](mailto:jscfadt@aph.gov.au)

Dear Mr Neumann

**ANAO submission for the Inquiry into the Department of Defence Annual Report 2022-23**

The Australian National Audit Office (ANAO) presented the following performance audits to the Parliament that you may find relevant to the above inquiry:

- Auditor-General Report No. 21 (2022-23) [\*Department of Defence's Procurement of Hunter Class Frigates\*](#);
- Auditor-General Report No. 24 (2022-23) [\*Defence's Management of the Delivery of Health Services to the Australian Defence Force\*](#);
- Auditor-General Report No. 33 (2022-23) [\*Department of Defence's Management of General Stores Inventory\*](#); and
- Auditor-General Report No. 45 (2022-23) [\*Australia's Provision of Military Assistance to Ukraine\*](#)

Information about what the audits assessed, concluded and recommended is attached. The audit reports are available online at [www.anao.gov.au](http://www.anao.gov.au).

Should the Committee require further information in relation to these matters, my office would be pleased to provide you with a briefing at a time convenient to you or appear as a witness at a hearing. To arrange a briefing, please contact our External Relations team at [external.relations@anao.gov.au](mailto:external.relations@anao.gov.au).

Yours sincerely

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Grant Hehir

## **Auditor-General Report No. 21 2022–23 *Department of Defence’s Procurement of Hunter Class Frigates***

### **Background**

1. The Royal Australian Navy (the Navy) currently has eight ANZAC class frigates. The 2016 Defence White Paper stated that:

The Government is bringing forward the future frigate program to replace the Anzac Class frigates. A continuous build of the Navy’s future frigates will commence in 2020. The future frigates will be built in South Australia following completion of a Competitive Evaluation Process.<sup>1</sup>

2. On 29 June 2018, the Australian Government announced the outcome of the competitive evaluation process, which had assessed designs by three shipbuilders:

The frigates, to be designed by BAE Systems and built by ASC Shipbuilding, are central to our plan to secure our nation, our naval shipbuilding sovereignty and create Australian jobs.

BAE’s Global Combat Ship – Australia will provide our nation with one of the most advanced anti-submarine warships in the world – a maritime combat capability that will underpin our security for decades to come.

The Future Frigates, named the Hunter class, will be built in Australia, by Australians, using Australian steel.

This \$35 billion program will create 4,000 Australian jobs right around the country and create unprecedented local and global opportunities for businesses large and small.

The Hunter class will begin entering service in the late 2020s replacing the eight Anzac Frigates, which have been in service since 1996.<sup>2</sup>

3. Construction of the Hunter class frigates is part of the Australian Government’s continuous naval shipbuilding program intended to develop sovereign Australian shipbuilding and sustainment. The Australian Government’s 2020 Force Structure Plan publicly reported that the cost of the Hunter class frigates was \$45.6 billion out-turned.<sup>3</sup>

### **Rationale for undertaking the audit**

4. The acquisition of nine Hunter class frigates is a key part of the Australian Government’s substantial planned expenditure on naval shipbuilding and maritime capability<sup>4</sup> and contributes to the ongoing

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<sup>1</sup> Department of Defence, 2016 Defence White Paper, p. 113, available from <https://www.defence.gov.au/about/strategic-planning/2016-defence-white-paper> [accessed 8 November 2022].

<sup>2</sup> Prime Minister, Minister for Defence, Minister for Defence Industry and Minister for Finance, ‘The Hunter class – defending Australia and securing our shipbuilding sovereignty’, joint media release, 29 June 2018, available from <https://www.minister.defence.gov.au/minister/marise-payne/media-releases/joint-mediarelease-prime-minister-minister-defence-minister-1> [accessed 26 October 2022].

BAE Systems is headquartered in the United Kingdom. The other participants in the competitive evaluation process, which was a limited tender approach, were Fincantieri S.p.A of Italy and Navantia S.A of Spain.

<sup>3</sup> Mid-Year Economic and Fiscal Outlook 2019–20 price and exchange.

<sup>4</sup> Defence reported to the Parliament in the most recent Major Projects Report (MPR) that the project is ‘a foundation project in the Government’s Continuous Naval Shipbuilding Program’ and ‘will provide the RAN [Royal Australian Navy] with the critical capability required to defend Australia well into the future.’ See Auditor-General Report No.12 2022–23 2021–22 Major Projects Report, p. 137, available at (internet) <https://www.anao.gov.au/work/major-projects-report/2021-22-major-projects-report>.

capability of the Australian Defence Force.<sup>5</sup> This audit examined the effectiveness of the Department of Defence's (Defence) procurement of Hunter class frigates to date and the achievement of value for money through Defence's procurement activities.

5. The audit builds on previous Auditor-General work on Defence's acquisition and sustainment of Navy ships and implementation of the Australian Government's 2017 Naval Shipbuilding Plan, to provide independent assurance to the Parliament on Defence's planning, procurement, decision-making and advising, contracting and delivery of the Hunter class frigates to date.

### **Audit objective and criteria**

6. The objective of the audit was to assess the effectiveness of the Department of Defence's procurement of Hunter class frigates and the achievement of value for money to date.

7. To form a conclusion against the objective, the following high-level criteria were adopted.

- Did Defence conduct an effective tender process?
- Did Defence effectively advise government?
- Did Defence establish fit-for-purpose contracting arrangements?
- Has Defence established effective contract monitoring and reporting arrangements?
- Has Defence's expenditure to date been effective in delivering on project milestones?

8. This audit reports on Defence procurement activity and developments in project SEA 5000 Phase 1 (Hunter class frigate design and construction) to March 2023. The government and Defence have indicated that the planned Hunter class capability has been considered as part of the Defence Strategic Review and related government processes.<sup>6</sup>

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<sup>5</sup> The 2020 Force Structure Plan included references to the acquisition or upgrade of up to 23 classes of Navy and Army vessels representing potential expenditure of \$168 billion to \$183 billion. The planned future investment at the time included the Attack class submarine, which was cancelled in 2021. As of March 2023, Defence had not released updated figures on planned total naval shipbuilding expenditure.

<sup>6</sup> The Defence Strategic Review was commissioned by the Australian Government and announced on 3 August 2022. Its final report was provided to the Prime Minister and Minister for Defence on 14 February 2023. The review's terms of reference included a requirement that: 'The Review must consider all elements of the Integrated Investment Program and provide recommendations for the Program's reprioritisation, particularly in light of recently announced large-scale projects, to provide Australia with the force structure required by 2032-33.' A public version of the final report of the review, which included the terms of reference, was released on 24 April 2023, available from: <https://www.defence.gov.au/about/reviews/inquiries/defencestrategic-review> [accessed 26 April 2023]. In the foreword to the public version, the reviewers noted at p. 11 that it was 'necessarily qualitatively different' from the version provided to the Prime Minister and Minister for Defence and 'less detailed, as many of the judgements and recommendations in the Review are sensitive and classified.' The review, its recommendations and the government's response to the recommendations are discussed in the following places in this audit report: footnotes 21, 52 and 169 and paragraphs 1.27, 3.120, 3.140–3.141 and 3.144–3.145.

In respect to the Hunter class frigates, the Chief of Navy advised, at the 15 February 2023 hearings of the Senate Foreign Affairs, Defence and Trade Legislation Committee, that: 'This is also one of those capabilities that have been and are being reviewed by the Australian government' in the context of the Defence Strategic Review. See Senate Foreign Affairs, Defence and Trade Legislation Committee, 2022–2023 Supplementary Budget Estimates, Proof Committee Hansard, 15 February 2023, p. 58. Available at: [https://www.aph.gov.au/Parliamentary\\_Business/Hansard/Estimates\\_Transcript\\_Schedule](https://www.aph.gov.au/Parliamentary_Business/Hansard/Estimates_Transcript_Schedule) [accessed 20 April 2023].

## Conclusion

9. The Department of Defence's management to date of its procurement of Hunter class frigates has been partly effective. Defence's procurement process and related advisory processes lacked a value for money focus, and key records, including the rationale for the procurement approach, were not retained. Contract expenditure to date has not been effective in delivering on project milestones, and the project is experiencing an 18-month delay and additional costs due in large part to design immaturity.

10. Defence did not conduct an effective limited tender process for the ship design. The value for money of the three competing designs was not assessed by officials, as the Tender Evaluation Plan (TEP) proposed that government would do so. The Commonwealth Procurement Rules (CPRs) and the Defence Procurement Policy Manual required officials responsible for procurement to be satisfied, after reasonable inquiries, that the procurement achieved a value for money outcome. Defence did not otherwise document the rationale for the TEP not requiring a value for money assessment or comparative evaluation of the tenders by officials.

11. Defence's advice to the Australian Government at first and second pass was partly effective. While the advice was timely and informative, Defence's advice at second pass was not complete. Defence did not advise that a value for money assessment had not been conducted by Defence officials and that under the TEP Defence expected government to consider the value for money of the tenders.

12. Defence has established largely fit-for-purpose contracting arrangements for the design and productionisation stage, and largely effective contract monitoring and reporting arrangements to ensure adequate visibility of performance and emerging risks and issues. However, the contract management plan was established 44 months (3.6 years) after contract execution.

13. Defence's expenditure to date has not been effective in delivering on project milestones, and the cost of the head contract has increased. Lack of design maturity has resulted in an 18-month delay to the project and extension of the design and productionisation phase, at an additional cost to Defence of \$422.8 million.<sup>7</sup> At January 2023 the project was forecast to exceed the whole of project budget approved by government by a significant amount.

## Supporting Findings

### Tender process

14. To select ship designs for the government-approved competitive evaluation process (CEP) — a limited tender approach — Defence conducted a shortlisting process informed by its own assessments and analysis by the RAND Corporation. Defence did not retain complete records of its assessments, and its rationale for shortlisting all selected designs for the CEP was not transparent. (See paragraphs 2.3 to 2.20)

15. Defence's Endorsement to Proceed documentation for the CEP approved the Request for Tender (RFT) going ahead and set out tender evaluation criteria and expectations for the assessment of value for money. However, the expectations regarding the assessment of value for money were not

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<sup>7</sup> Defence advised the ANAO in April 2023 that it expected the \$422.8 million would be offset from the price of the planned batch one build scope.

operationalised, as the Tender Evaluation Plan (TEP) specified that value for money would not be assessed by Defence. (See paragraphs 2.21 to 2.29)

16. The TEP, which was approved by the probity advisor, did not document how the evaluation process would address the core rule of the Commonwealth Procurement Rules (CPRs), which is achieving value for money. The CPRs require officials responsible for procurement to be satisfied, after reasonable inquiries, that the procurement achieves a value for money outcome. Defence did not document the rationale for the TEP not requiring a value for money assessment or comparative evaluation of the tenders by officials. (See paragraphs 2.30 to 2.35)

17. As the tender evaluation process was underpinned by a TEP that specifically excluded a value for money assessment of tenders by officials, the Source Evaluation Report (SER) did not include a value for money assessment. (See paragraphs 2.36 to 2.39)

18. Defence conducted the tender evaluation in accordance with the TEP but did not retain a record of delegate approval of the SER Supplement document, which recorded the outcomes of the evaluation process. (See paragraphs 2.40 to 2.45)

19. Not all probity matters were recorded and addressed as required by the November 2016 Legal Process and Probity Plan for the procurement. (See paragraphs 2.46 to 2.51)

### **Advice to government**

20. Defence's advice to government at first pass was timely and informative. However, its recommendation to include the BAE Type 26 design in the competitive evaluation process (CEP) as the third option, instead of the alternate, was not underpinned by a documented rationale. (See paragraphs 2.53 to 2.56)

21. At second pass, Defence's advice to government on the selection of the preferred ship design was not complete. Defence did not draw the following matters to government's attention.

- Contrary to the requirements of the Commonwealth Procurement Rules (CPRs), a value for money assessment had not been conducted by Defence officials. Defence's assessment was against the high-level capability requirements.
- Under the Tender Evaluation Plan (TEP) Defence expected government to consider the value for money of the tenders.
- A 10 per cent reduction to tendered build costs had been applied by Defence. The reduction had not been negotiated with tenderers.
- Sustainment cost estimates had not been prepared for government consideration as required by the Budget Process Operational Rules applying to Defence. (See paragraphs 2.57 to 2.85)

22. In its assessment, which was included in Defence's second pass advice to government, the Department of Finance (Finance) drew attention to the 10 per cent reduction to tendered build costs and other limitations in Defence's advice on costs. Finance did not comment on Defence's lack of a value for money assessment, compliance with the CPRs or quality of advice regarding value for money. (See paragraphs 2.79 to 2.80)

### **Contracting arrangements**

23. When it was executed in December 2018, the head contract reflected the contract negotiation outcomes reported to the delegate. However, the extent to which these outcomes were in line with

Defence's original negotiation positions is not transparent because not all outcomes were clearly defined or reported against, and some negotiation issues were not finalised when the head contract was signed. (See paragraphs 3.3 to 3.12)

24. Milestones under the head contract have clear entry and exit criteria and due dates, with the first milestone payable on contract execution. (See paragraph 3.15)

25. Performance expectations are clearly set out in the contracted statement of work and are linked to performance measures, with processes to manage poor performance included in the conditions of contract. Commercial levers to incentivise the prime contractor (BAE Systems Maritime Australia) and drive value for money outcomes in project delivery are limited. Key commercial levers such as profit moderation provisions were not active at the time the head contract was executed. On 29 June 2022 Defence signed a contract change proposal activating profit moderation for the Scope Fee from 1 July 2022, enlivening a key commercial lever in the head contract. (See paragraphs 3.18 to 3.28)

26. The head contract established processes for managing contract change proposals (CCPs). As of 31 March 2023, there were 93 contract changes and the number of key milestones had increased from 25 to 37. Thirty-six of the 93 CCPs approved by Defence were price impacting and the cost of the contract has increased by \$693.2 million. This represents a 36 per cent increase to the design and production cost of the Hunter class. (See paragraphs 3.13 to 3.17)

27. Amendments to the head contract mean that between December 2018 (contract execution) and March 2023, the contract has increased in price from \$1,904.1 million (GST exclusive) to \$2,597.4 million (GST exclusive). The contract price remained within the (PGPA Act) section 23 commitment approval amount as of 31 March 2023. (See paragraphs 3.13 to 3.17)

### **Monitoring and reporting arrangements**

28. The contract management plan was established 44 months (3.6 years) after execution of the head contract. Defence has managed the contract largely in the absence of an approved contract management plan, and BAE Systems Maritime Australia's (BAESMA's) contract master schedule remained unapproved as of March 2023. (See paragraphs 3.29 to 3.30)

29. Contracted requirements for BAESMA to report and meet with Defence have been established. Additional reporting requirements have been established in response to delays in the delivery of a contractable offer for the batch one build scope from BAESMA. (See paragraphs 3.38 to 3.43)

30. Governance and oversight arrangements — to manage and oversee project performance, risks and issues — have generally been established in a timely manner. Defence records indicate that governance bodies have met at the expected cadence and with the required Defence senior leadership attendance. (See paragraphs 3.32 to 3.37 and 3.44 to 3.45)

31. Defence has established appropriate project and program monitoring arrangements. These include performance monitoring mechanisms to inform Defence of relevant developments overseas, and Independent Assurance Review (IAR) processes. IARs have found insufficient resources, in particular skills and expertise in the project team, and that increased senior leadership attention was needed to manage realised risks and mitigate risks exceeding project risk appetite. (See paragraphs 3.46 to 3.50)

32. More generally, the Surface Ships Advisory Committee (SSAC) was asked to review cost, schedule and risk across the project and provide input to the Australian Government's Defence Strategic Review. Defence advised the Parliament in February 2023 that the SSAC's review had not resulted in any changes in scope to the project. (See paragraph 3.51)

## **Delivery on project milestones**

33. Actual project expenditure at 31 January 2022 was \$2,225.9 million, with \$1,308.4 million spent on the head contract with BAE Systems Maritime Australia (BAESMA). Defence has made milestone payments without all exit criteria being met and extended milestone due dates in response to project delays. (See paragraphs 3.53 to 3.84)

34. In June 2021 the Australian Government agreed to extend the design and productionisation period, and to an 18-month delay to the cut steel date for ship one, to enable Defence and BAESMA to improve design maturity and develop a contractable offer for the first batch of ships. The June 2022 contract change proposal to extend the design and productionisation phase increased the contract price by \$422.8 million (GST exclusive). (See paragraphs 3.106 to 3.116)

35. Design immaturity has affected Defence's planning for the construction phase, led to an extension of the design and productionisation phase at additional cost to Defence, and diverted approved government funding for long lead time items to pay for the extension and other remediation activities. Planning for the transition from the existing ANZAC class frigates to the Hunter class capability has also been affected. (See paragraphs 3.104 to 3.126)

36. In December 2021 Defence advised the Australian Government that it considered that BAESMA would recover the schedule delay over the life of the project and deliver the final ship as planned in 2044. (See paragraph 3.108)

37. The January 2023 Surface Ships Advisory Committee (SSAC) report noted that BAESMA had advised that a risk adjusted schedule would add 16 months to the delivery of the first Hunter class, moving delivery from early 2031 to mid-2032. (See paragraph 3.117)

38. As of January 2023, Defence's internal estimate of total acquisition costs, for the project as a whole, was that it was likely to be significantly higher than the \$44.3 billion advised to government at second pass in June 2018. The SSAC considered that current efforts by Defence and industry were unlikely to result in a cost model within the approved budget. As of March 2023, while Defence had advised portfolio Ministers that the program is under extreme cost pressure, it had not advised government of its revised acquisition cost estimate, on the basis that it is still refining and validating the estimate. (See paragraphs 3.86 to 3.97)

39. Defence has approved BAESMA's Continuous Naval Shipbuilding and Australian Industry Capability (AIC) strategies and plans, with an Australian contract expenditure target of 58 per cent of total contract value and 54 per cent of the design and productionisation phase. (See paragraphs 3.127 to 3.135)

40. The February 2022 Independent Assurance Review (IAR) was not assured that there was a clear path to realising the policy objective of a local surface combatant ship designing capability, due to delays in transferring relevant personnel and skills to Australia. (See paragraph 3.137)

41. In early 2023 the project remained in the design and productionisation phase, which is intended to inform Defence's planning and contracting for the ship build, including Defence's final estimate of construction costs. Defence advised the Parliament in February 2023 that the project is managing a range of complex risks and issues and is considering remediation options. Defence further advised that the Hunter class was one of the capabilities that were reviewed by government in the context of the Defence Strategic Review, which presented its final report to ministers on 14 February 2023. A public version of the final report was released on 24 April 2023. (See paragraphs 3.142 to 3.145)

## Recommendations

### Recommendation No. 1

The Department of Defence ensure compliance with the Defence Records Management Policy and statutory record keeping requirements over the life of the Hunter class frigates project, including capturing the rationale for key decisions, maintaining records, and ensuring that records remain accessible over time.

**Department of Defence response: Agreed.**

### Recommendation No. 2

The Department of Defence ensure that its procurement advice to the Australian Government on major capital acquisition projects documents the basis and rationale for proposed selection decisions, including information on the department's whole-of-life cost estimates and assessment of value for money.

**Department of Defence response: Agreed.**



## **Auditor-General Report No.24 2022–23 *Defence's Management of the Delivery of Health Services to the Australian Defence Force***

### **Background**

1. The Department of Defence (Defence) is required under its legislative and regulatory framework to provide comprehensive health care, including dental and other ancillary health care<sup>1</sup>, to members of the Australian Defence Force (ADF).<sup>2</sup>

2. Health services are provided to approximately 60,000 permanent ADF members and approximately 25,000 reservists. Health services are provided day-to-day across 51 health centres and clinics located on Defence bases throughout Australia.<sup>3</sup> Where an ADF member needs health care that cannot be provided on-base, ADF members are able to access a network of health care facilities and providers off-base. Access to off-base health care facilities and staffing of on-base facilities is acquired by Defence through the Australian Defence Force Health Services Contract (ADF health services contract or the contract).

3. On 14 January 2019, Defence awarded the ADF health services contract to Bupa Health Services Pty Ltd (Bupa or the contractor). The \$3.4 billion (GST inclusive) contract is for an initial period of six years, with options to extend to a maximum of 10 years and an estimated cost of \$6.0 billion (GST inclusive). The new arrangements replaced the previous contract with Medibank Health Solutions Pty Ltd.<sup>4</sup>

4. When seeking approval to enter into the new contract, Defence advised the Minister for Defence and the Minister for Finance that it would deliver the following benefits:

- enhanced health service delivery with a robust continuous improvement and innovation process;
- improved business intelligence through automation, data collection and analysis; and
- improved commercial arrangements through specific contract mechanisms that promote cost containment.

5. When entering into the new contract Defence advised ADF members and families that:

Whilst the range of health services procured under this Contract has not substantially changed, Joint Health Command has sought to continue to improve its delivery of health services to Defence personnel. Under the ADF Health Services Contract, Defence will see a greater use of data and analytics in health service delivery, the identification and minimisation of low value care, and an increased focus on continuous improvement and innovation.<sup>5</sup>

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<sup>1</sup> Ancillary health care includes services such as physiotherapy, optical, podiatry, audiology, and mental health services.

<sup>2</sup> Defence Determination 2016/19, Conditions of Service made under section 58B of the Defence Act 1903 identifies two classes of ADF members that meet the definition of 'rendering continuous full-time service'. These are a member of the Permanent Forces (Army, Navy, Air Force) or a member of the Reserves on continuous full-time service.

<sup>3</sup> The 51 health centres and clinics include RMAF Butterworth, Penang, Malaysia.

<sup>4</sup> Defence awarded the initial ADF health services contract to Medibank on 28 June 2012. Medibank provided health services until 30 June 2019, enabling the completion of a six-month transition-in period for Bupa.

<sup>5</sup> Department of Defence, ADF Health Services Contract [internet], Defence, available from <https://www.defence.gov.au/adf-members-families/health-well-being/services-support-fighting-fit/adf-health-services-contract> [accessed 6 February 2023].

6. Under the contract the full suite of health services necessary for ADF members to maintain an acceptable level of health, fitness and wellbeing is to be provided. This includes:

- a health professional workforce<sup>6</sup>;
- access to medical advice, triage and referrals (including providing mental health risk assessments) 24 hours a day, seven days a week;
- access to a broad range of specialised services;
- an appointment and booking system and/or service;
- imaging and radiology services;
- pathology services; and
- occupational rehabilitation services.

7. In July 2019, the workforce engaged under the contract to provide health care in the garrison environment (on-base) was comprised of approximately 997 contracted health professionals. In June 2022, approximately 1,283 health professional and support staff were providing services on-base. The composition of the workforce in July 2019 and June 2022 is illustrated at Figure S.1 (refer to Appendices).

8. The quantity and type of health services delivered under the contract through the off-base network, between July 2019 and June 2022, is illustrated at Figure S.2 (refer to Appendices).

### **Rationale for undertaking the audit**

9. Defence has a legal obligation to provide medical and dental services to ADF personnel who are providing continuous full-time service, and a capability imperative to maintain the health status of ADF personnel. Defence's ADF health services contract is a key element of its support arrangements for the ADF.

10. This performance audit is part of an ongoing program of work that has examined aspects of Defence's contract management and administration. The audit was undertaken approximately half-way through the initial six-year period of the ADF health services contract<sup>7</sup>, to provide independent assurance to Parliament on the effectiveness of Defence's contract management.

### **Audit objective and criteria**

11. The objective of the audit was to assess whether Defence is managing its ADF health services contract to achieve efficient and effective delivery of the contracted services.

12. To form a conclusion against the objective, the following high-level criteria were used.

- Has Defence established fit-for-purpose contract governance arrangements?

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<sup>6</sup> The health professional workforce provides health services in the garrison environment (on-base), such as primary and occupational healthcare, dental, physiotherapy, mental health and psychology services, pharmacy, occupational rehabilitation and health administration.

<sup>7</sup> The contract includes four options to extend for twelve months, allowing Defence to extend the total duration of the contract for a further four years, to a maximum of 10 years from the operative date of 1 July 2019.

- Has Defence established fit-for-purpose performance monitoring, evaluation and reporting arrangements?
- Have services been delivered effectively against contracted requirements?
- Have the expected cost and service delivery efficiencies under the contract been realised?

13. To assess Defence's contract management the ANAO reviewed both the design and implementation of the contracted arrangements.

14. The audit focused on Defence's arrangements to deliver its responsibilities under Defence Regulation 2016, subsection 49(1), through its management of the contract with Bupa Health Services Pty Ltd (Bupa) to deliver health services to the ADF.<sup>8</sup>

15. The audit also followed-up on the moderate financial audit finding raised by the ANAO in 2020–21, relating to the governance of ADF health services, including invoicing and assurance arrangements for the contract.<sup>9</sup>

16. The audit did not examine:

- the effectiveness of the procurement approach used to award the contract and the related value for money assessment;
- the effectiveness of the service delivery model selected by Defence to deliver health services to ADF personnel;
- other activities conducted by Joint Health Command that contribute to the delivery of Defence's legal obligation to provide medical and dental services to ADF personnel;
- related procurements, including planned facility upgrades, JP2060 Phase 3 – the provision of deployable health units, or JP2060 Phase 4 – the replacement of the Defence electronic Health System (DeHS) with a Health Knowledge Management System; or
- the delivery of clinical services to ADF members.

## Conclusion

17. Defence has been partly effective in managing its ADF health services contract to achieve efficient and effective delivery of the contracted services. In particular, Defence's contract management demonstrated shortcomings in ensuring the implementation of all contracted requirements.

18. While Defence has developed largely fit for purpose contract governance arrangements, the implementation of contracted requirements has been partly effective. Defence has not managed the contract to ensure that: all plans required under the contract have been put in place; contract change proposals are made in accordance with processes established in the contract; all reports prepared by the contractor meet the minimum contracted requirements; invoices are complete; and contract payments are only made on the basis of complete invoices. Weaknesses identified in Defence's control

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<sup>8</sup> Defence Regulation 2016 – Part 8, sections 49 and 50, and Defence Determination 2016/19, Conditions of Service made under section 58B of the Defence Act 1903, state that members providing continuous full-time service include members of the Permanent Forces and members of the Reserves who are required to perform a period of continuous full-time service with the Permanent Forces.

<sup>9</sup> Auditor-General Report No.40 2020–21 Financial Statements Audit Interim Report on Key Financial Controls of Major Entities, paragraph 1.112 and paragraphs 3.3.13–3.3.17.

framework for payments have not been fully resolved, reducing Defence's ability to provide assurance on the proper use of public resources for which it is responsible.

19. Defence has included a fit for purpose performance management framework in the contract. However, implementation has been partly effective. Defence has not managed the contract to ensure that the full suite of performance measures, and all review and assessment processes, have been fully implemented in line with contract requirements.

20. Performance measurement and assessment arrangements are not fully functioning and Defence is not well placed to provide assurance that services are being delivered effectively against the contracted requirements. Key arrangements and initiatives to drive and monitor benefits realisation have not been fully implemented and Defence is not able to demonstrate that the expected cost and service delivery efficiencies under the contract have been realised.

## Supporting Findings

### Contract governance arrangements

21. The contract includes a framework for contract management and governance intended to build the relationship between Defence and its contractor through the engagement of senior executives, regular monitoring of service provision, and clear arrangements to manage communication and escalate issues. However, senior executive engagement has been less regular than intended, a communications plan (which provides guidance on escalating issues) has not been in place since 1 July 2019, the terms of reference for five committees no longer align with contracted requirements, and Defence has drafted but not implemented a contract management plan. Further, an 'informal' approach to record keeping for key meetings between the parties has been adopted, which is not consistent with Defence records management policy. (See paragraphs 2.5 to 2.20)

22. While the contract establishes that it shall only be changed through contract change proposals (CCPs), contract adjustments have occurred outside the CCP process and without formal agreement. The contract management and governance framework does not address how contract changes are to be managed, and Defence has drafted but not implemented a contract management plan to provide guidance to those responsible for reviewing and processing CCPs. (See paragraphs 2.21 to 2.31)

23. The contractor is responsible for risk and issue management and has developed a risk management plan as required. However, the quarterly risk reports received by Defence and governance committees have not consistently met the minimum contracted requirements. Jointly chaired governance committees have responsibility for risk oversight but have not sought to assure themselves that controls to mitigate identified risks have been effectively implemented. (See paragraphs 2.34 to 2.41)

24. There is oversight of the contract's financial management through governance committees jointly chaired by Defence and the contractor. These committees receive and consider relevant financial reports. There are also financial levers included in the contract to help Defence manage contractor performance. These have been utilised, with Defence claiming liquidated damages totalling \$1 million from the contractor as at June 2022. Contracted gainshare arrangements have also been applied, with Defence sharing in gains totalling \$10.4 million. (See paragraphs 2.43 to 2.51)

### Management of claims for payment

25. Defence has established a commercial audit program to provide assurance that the contractor's monthly claims for payment have been calculated in accordance with the contract and are proper and

valid. Testing undertaken by Defence (through its commercial audit program) and by the ANAO (during the annual financial statements audit and this performance audit) has identified that Defence has made many payments on the basis of incomplete invoices. Information missing from invoices has included whether the ADF member was approved to obtain the service, who provided the service, what service was provided, and where the service was provided. (See paragraphs 2.53 to 2.62 and 2.73 to 2.81)

26. Weaknesses in financial governance and the billing system were identified through the commercial audit program in June 2020. In February 2021, a program of work commenced to improve the quality of invoice data submitted by the contractor to Defence, including through the development and implementation of business rules within the contractor's systems. As at December 2022, the weaknesses in Defence's control framework for payments had not been fully resolved, reducing Defence's ability to provide assurance on the proper use of public resources for which it is responsible. (See paragraphs 2.61 to 2.72)

### **Performance monitoring, reporting and evaluation**

27. The contract includes a performance management framework that sets out performance measures, payments, reporting, and review and assessment arrangements. (See paragraphs 3.3 to 3.8)

28. Four types of performance measures are used to assess contractor performance, against seven key result areas. One type has been fully implemented, one type has been largely implemented, and two types have been partly implemented. (See paragraphs 3.9 to 3.11)

29. The contract includes a range of payments to support Defence's management of contractor performance, including incentive payments and at-risk amounts. As at August 2022, Defence has shared in gains and retained amounts 'at risk'. Defence has also made incentive payments totalling \$7 million to the contractor in error. Defence has since commenced a program of work to identify any additional incentive payments made in error and recover the funds. (See paragraphs 3.14 to 3.17)

30. The contract requires the contractor to provide a monthly transactional report and a quarterly contract status report. The contract also provides that six types of performance reviews be undertaken. The performance reviews to be conducted by Defence have not been fully implemented, and joint performance appraisals have not been conducted. (See paragraphs 3.18 to 3.38)

31. The performance management framework has been evaluated. A review commissioned by Defence in November 2021 reported in August 2022. Defence started a process in late 2022 to update and revise the framework to address issues identified by the review. (See paragraphs 3.12 to 3.13)

### **Delivery of contracted requirements**

32. Without fully functioning performance measurement and assessment arrangements, Defence is not well placed to provide assurance that services are being delivered effectively against the contracted requirements. (See paragraphs 4.3 to 4.15)

33. The contract establishes a range of credentialing, training and security requirements intended to ensure that the services are fit-for-purpose for the Defence environment. Assurance arrangements for credentialing are fully established, and largely established for the training and security requirements. The security requirements were not established in a timely manner, with the contractor's ICT system operating under provisional accreditation for almost four years between June 2019 and April 2023. (See paragraphs 4.16 to 4.19)

## Expected cost and service delivery efficiencies

34. Defence is not able to demonstrate that the expected cost and service delivery efficiencies under the contract have been realised, as it has not fully implemented the arrangements intended to support benefits realisation. Defence identified the cost and service delivery efficiencies it expected to achieve from the contract in a benefits management plan developed during the procurement. Benefits management was handed over to the individual business units responsible for contract management and service delivery in October 2019. Benefits realisation has not been overseen by the responsible governance committees, and there is no evidence of reporting of progress to deliver the expected benefits identified. (See paragraphs 4.23 to 4.24)

35. Other key measures intended to support the realisation of cost and service delivery efficiencies have not been fully implemented. As at December 2022, three out of 17 initiatives had been implemented. The contractor's 'technical solution' — which includes the referral and booking system and services management tools — has not delivered the expected improvements in business intelligence. Further, ongoing data quality issues have meant that expectations regarding improved data collection and the use of analytics to achieve cost and service delivery efficiencies have not been realised. (See paragraphs 4.27 to 4.42)

36. The realisation of cost efficiencies has been eroded through unplanned growth in the contracted health workforce, the increasing use of flex-fill (short-term additional workforce requirements) and the introduction of a second price variation mechanism in 2021. (See paragraphs 4.43 to 4.47)

37. As at December 2022, the contract was overspent against its budget. The cost per eligible person is 11 per cent higher than the benchmark established in 2018 and the total expected value over the initial six-year period has increased by \$230.2 million, to \$3.6 billion dollars. The contract is demand driven and Defence has assessed that the realisation of cost savings was impacted by unanticipated events such as the 2019–20 black summer bushfires and the COVID-19 pandemic. (See paragraphs 4.48 to 4.50)

## Recommendations

### Recommendation No. 1

The Department of Defence ensure that all record keeping requirements are complied with in its management of the ADF health services contract.

**Department of Defence: Agreed.**

### Recommendation No. 2

The Department of Defence develop and implement an assessment and authorisation framework, supported by appropriate governance and assurance arrangements, to oversee the handling of contract change proposals under the ADF health services contract.

**Department of Defence: Agreed.**

### Recommendation No. 3

The Department of Defence ensure that accreditation processes for ICT systems that manage sensitive, including personally identifiable, information are completed in a timely manner, and that risks are identified and effectively monitored to ensure information is being managed appropriately.

**Department of Defence: Agreed.**

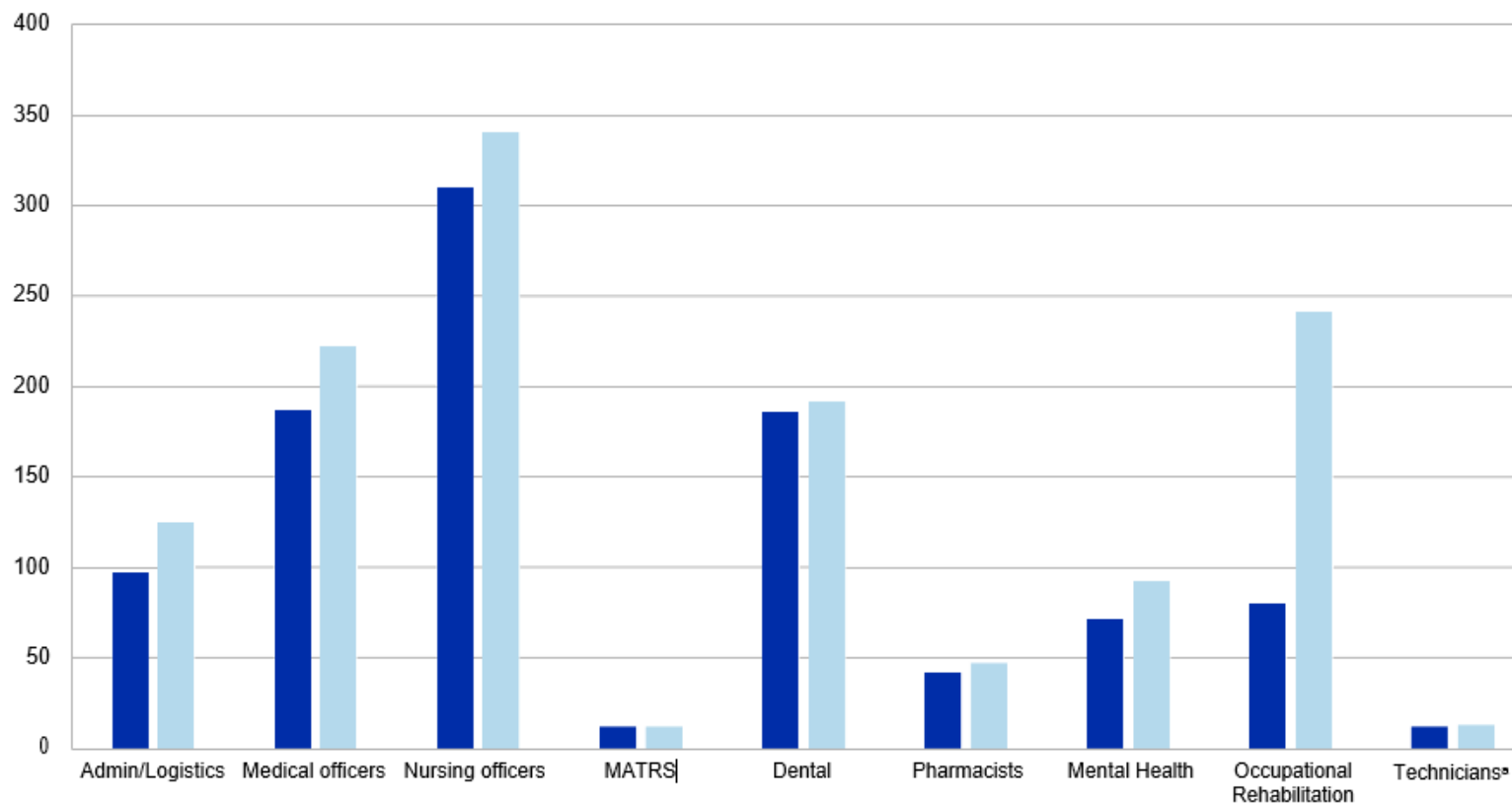
*Recommendation No. 4*

The Department of Defence implement the benefits management plan for the ADF health services contract and establish appropriate governance arrangements to monitor and report on benefits realisation.

**Department of Defence: Agreed.**

## Appendices

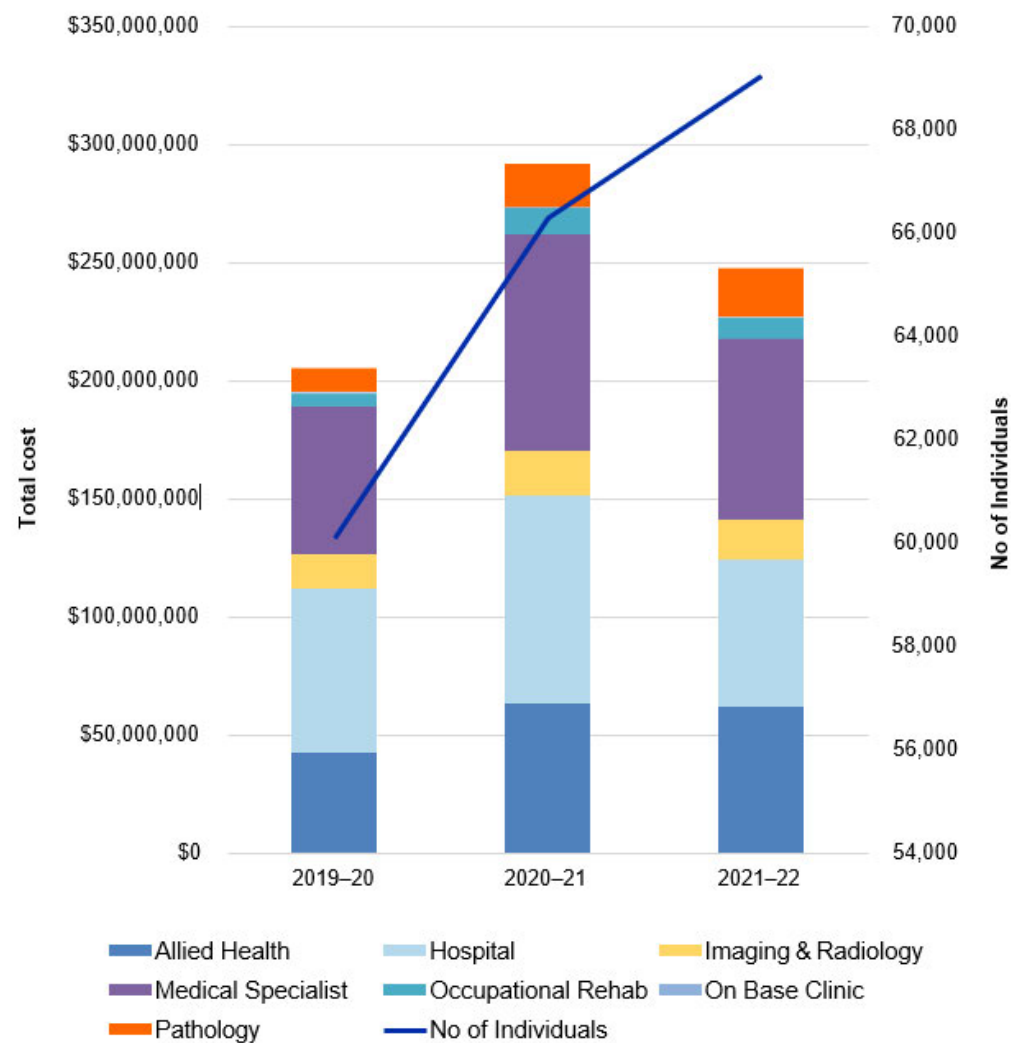
**Figure S.1: Health professional and support staff positions per category under the ADF health services contract — July 2019 and June 2022**



– Note a: The 'Technicians' category includes dispensary assistant/technicians and central sterile supply technicians. Source: ANAO analysis.



**Figure S.2: Health services delivered to ADF members through the off-base network — July 2019 to June 2022**



Source: ANAO analysis.

## Auditor-General Report No.33 2022–23 *Department of Defence's Management of General Stores Inventory*

### Background

1. Defence defines inventory management as the 'phase of military logistics which includes managing, cataloguing, requirements determinations, procurement, distribution, overhaul and disposal' of inventory.

2. As at 30 June 2022, Defence reported a balance of \$7.9 billion in inventories comprised of explosive ordnance (\$5.3 billion), general stores inventories (\$2.6 billion) and fuel (\$61.6 million).<sup>1</sup> Defence holds both 'operating stocks' to maintain capability, and 'reserve stocks' over and above operating levels.<sup>2</sup>

3. This audit is focused on Defence's management of general stores inventory (GSI).<sup>3</sup> Defence's Electronic Supply Chain Manual defines GSI as items:

Consumed in the course of Defence operations and used in the delivery and support of deployable military capability. GSI includes expendable and consumable items (Stock Type X) such as ration packs, clothing, sleeping bags, webbing, wet weather equipment, screws, washers, light globes, toiletries, as well as accountable inventory (Stock Type A) which incorporate those high value platform-specific and general replacement parts for Specialist Military Equipment (SME) assets which are not repairable.

4. Defence's GSI holdings comprise more than 70 million items of various stocks that are managed across 547 geographically dispersed locations. Defence records indicate that as at 17 November 2022, the majority of GSI (99.87 per cent) was being managed by Defence's Capability Acquisition and Sustainment Group (CASG).

5. Defence's Accountable Authority Instruction 8: Managing Defence Property (AAI 8) sets out a requirement to ensure that 'Defence property is used in an efficient, effective, economical and ethical manner'.<sup>4</sup> Defence property includes but is not limited to equipment, furniture, office supplies, clothing, uniforms, IT and telecommunications assets and military equipment. AAI 8 instructs

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<sup>1</sup> As reported in Defence's audited financial statements for 2021–22, which are included in Defence's 2021–22 Annual Report at Appendix A, available from <https://www.defence.gov.au/about/informationdisclosures/annual-reports> [accessed 9 January 2023]. See: Note 3.2B: Inventories (at pp. 215–16); and Key Audit Matter – Existence and completeness of inventories (at p. 177).

<sup>2</sup> The two stock types are defined in paragraph 1.1 of this audit report.

<sup>3</sup> The ANAO examined aspects of Defence's management of its fuel in Auditor-General Report No.28 2017–18 Defence's procurement of fuels, petroleum, oils, lubricants, and card services.

The ANAO examined Defence's management of explosive ordnance in:

- Auditor-General Report No.40 2010–11 Management of the Explosive Ordnance Services Contract;
- Auditor-General Report No.37 2010–11 Management of explosive ordnance held by the Air Force, Army and Navy; and
- Auditor-General Report No.24 2009–10 Procurement of Explosive Ordnance for the Australian Defence Force.

<sup>4</sup> The AAIs are made by the Secretary of the Department of Defence (the accountable authority) under the Public Governance, Performance and Accountability Act 2013 (PGPA Act). They apply to all persons engaged under the Public Service Act 1999 (PS Act) in Defence; all members of the Australian Defence Force (ADF); persons on exchange with, or on loan to Defence, who perform financial tasks; officials from other entities that use or manage public resources for which the Secretary is responsible; contractors, consultants and outsourced service providers (CCOSPs) undertaking work duties at the direction of Defence; and any other person who is defined as an official in accordance with section 13 of the PGPA Act and section 9 of the PGPA Rule.

‘everyone’ of their responsibility to ‘record, store, distribute, cost, disclose, dispose, track, transfer and stocktake property in accordance with policies endorsed by the Chief of the Defence Force (CDF) or the CFO [Chief Finance Officer]’. AAI 8 also instructs Defence Group Heads and military Service Chiefs that they ‘are responsible and accountable for all Defence property in your Group’s custody’.

6. By issuing AAI 8, the Secretary of Defence acts in accordance with the duty in section 15 of the *Public Governance, Performance and Accountability Act 2013* (PGPA Act) to govern the entity in a way that promotes the proper use and management of public resources.<sup>5</sup>

### **Rationale for undertaking the audit**

7. As at 30 June 2022, Defence was managing general stores inventories (GSI) comprising more than 70 million items of various stocks valued at \$2.6 billion across 547 geographically dispersed locations. The efficient and economical management of the level of inventories (both operating stocks and reserve stocks) contributes to: the achievement of Defence’s purpose; and compliance with the accountable authority’s responsibilities for the proper use and management of public resources for which the accountable authority is responsible.

8. This audit provides independent assurance to the Parliament of the efficiency and economy of Defence’s management of GSI.

9. The JCPAA identified the potential audit topic as a priority of the Parliament for 2020–21.

### **Audit objective and criteria**

10. The audit objective was to examine the efficiency and economy of Defence’s management of its general stores inventory. To form a conclusion against the objective, the following high level audit criteria were adopted.

- Has Defence established an authorising and administrative framework for the efficient and economical management of general stores inventory?
- Can Defence demonstrate implementation of its framework for the efficient and economical management of general stores inventory?

### **Conclusion**

11. Defence cannot demonstrate that it is achieving efficiency and economy in its management of general stores inventory.

12. Defence has established an authorising and administrative framework for the management of its general stores inventory which partly addresses efficient management and does not address economical management. Defence has been partly effective in maintaining its framework and has allowed it to degrade over time, pending implementation of new systems and supporting policies. The framework is not operating as intended to achieve the proper use and management of public resources.

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<sup>5</sup> ‘Proper’ is defined in section 8 of the PGPA Act, in relation to the use or management of public resources, as ‘efficient, effective, economical and ethical’ use. The term ‘use’ refers to the spending of relevant money, the commitment of appropriations, and the application of public resources generally to achieve a public purpose. The term ‘management’ is broad and encompasses the decisions, systems and controls around the custody and use of, and accountability for, public resources.

13. Defence is not able to demonstrate that it has fully implemented its framework requirements regarding cost-effective and efficient inventory management, and a ‘balanced inventory’ that avoids both understocking and overstocking. Defence was also unable to demonstrate, until late in this audit, an active focus or response by Defence senior leaders on known issues contributing to inefficiency and overstocking in the management of general stores inventory.

## Supporting Findings

### The framework for managing inventory

#### *Authorising and planning framework*

14. Defence has established but not fully documented a framework for the management of its inventory. The framework establishes both authorising and planning arrangements for the management of general stores inventory (GSI). The framework sets out roles and responsibilities within Defence and includes relevant policies and procedures to be followed. However, the authorising and planning frameworks for inventory stock holdings are not fully documented. (See paragraphs 2.3 to 2.65)

15. While the framework includes statements about the importance of cost-effective and efficient resource use, it does not directly address economical management of Defence inventory. (See paragraph 2.7)

16. Defence has allowed the framework to degrade over time, and non-compliant practices to arise, while awaiting the implementation of new systems and supporting policies. Defence could not provide the ANAO with evidence that the senior responsible officers — for entity-wide logistics policies and procedures and for Capability Acquisition and Sustainment Group (CASG) policies and procedures — have assessed the risks associated with the current approach or approved it. (See paragraphs 2.66 to 2.83)

17. The framework is not operating as intended to achieve the proper use and management of public resources and elements of the framework established in 2020 to provide visibility of, and authority for, justifiable overstocking have not been implemented. (See paragraphs 2.66 to 2.72)

#### *Systems*

18. Defence has established systems to support implementation of its authorising and planning framework for GSI. These include the Military Integrated Logistics Information System (MILIS). (See paragraphs 2.84 to 2.89)

19. A weakness of Defence’s systems is that they do not provide visibility of the holding and administrative costs associated with its GSI. Defence’s inventory management system includes ‘notional’ holding and administrative costs established in 1999, and the government’s 2008 Audit of the Defence Budget (the Pappas Review) found that Defence had materially underestimated those costs. In effect, not all relevant inventory management costs are well understood by Defence. This affects the ability of accountable logistics managers to make efficient and economical inventory procurement decisions and Defence is not well placed to demonstrate the efficiency and economy of its inventory management arrangements. (See paragraphs 2.90 to 2.101)

#### *Operational guidance and training arrangements*

20. Defence has established operational guidance and training arrangements to support the implementation of the authorising and administrative framework. Defence's guidance and training is largely focussed on the use of MILIS by its Designated Logistics Managers (DLMs), rather than the broader range of skills and experience required by the Defence Logistics Policy Manual, and does not focus explicitly on the efficient and economical management of GSI. (See paragraphs 2.102 to 2.115)

21. Defence has stated that its training arrangements are intended to support the professionalisation of logistics personnel. While training to access MILIS is mandated for DLMs and managed centrally, other relevant training is not. The completion of other training requirements is managed at a local level and Defence is not well placed to provide internal assurance that DLMs have the skills and experience required by the Defence Logistics Policy Manual. (See paragraphs 2.111 to 2.119)

## **Framework implementation**

### *Governance, monitoring, reporting and evaluation arrangements*

22. Defence has established governance, monitoring, reporting and evaluation arrangements for its GSI. These arrangements generate relevant management information for Defence's operational managers and senior leaders with oversight responsibilities, including in respect to overstocks of GSI. (See paragraphs 3.3 to 3.25)

23. The information available from these arrangements indicates that Defence is only partly effective in its implementation of the documented framework for cost-effective and efficient inventory management, which includes the goal of a 'balanced inventory' that avoids both understocking and overstocking. Since their introduction in 2015–16, annual Capability Acquisition and Sustainment Group (CASG) inventory health checks have repeatedly drawn attention to an inadequate focus on efficiency and resultant overstocking of Defence warehouses. They have further highlighted that overstocking is indicative of unnecessary overspending. (See paragraphs 3.26 to 3.53)

### *Demonstrating implementation of the framework*

24. Data from Defence systems indicates that on every measure examined by the ANAO, Defence's GSI is not 'balanced'. As of 7 February 2023, 79 per cent of general stores inventory warehouse stock on hand represented system-calculated overstock. Historically, this figure has been between 65 and 79 per cent. (See paragraphs 3.54 to 3.75)

25. The high levels of system-calculated GSI overstocks indicate that CASG's System Program Offices (SPOs) — which are responsible for day-to-day inventory management — continue to not calculate and/or model, or enter in Defence inventory management systems, operational and reserve stock quantities. (See paragraph 3.76)

26. Defence's performance against the examined measures, and non-compliance with the documented inventory framework, indicate that Defence is not able to demonstrate that it has fully implemented framework requirements regarding cost-effective and efficient inventory management, and a 'balanced inventory'. (See paragraph 3.76)

27. CASG's annual inventory health check findings on the reasons for overstocking and inefficiency in the management of GSI have been reported to operational management and senior leaders since the health checks were introduced in 2015–16. However, there was no indication until late in this audit of an active focus by Defence senior leaders on these known issues, nor an active management response (see paragraphs 3.77 to 3.82).

## Recommendations

### Recommendation No. 1

The Department of Defence clarify the status, and review the implementation, of the Capability Acquisition and Sustainment Group's Materiel Planning and Management Policy and associated procedures, to ensure that there is a documented rationale for holding general stores inventory identified as overstock.

**Department of Defence Response: Agreed.**

### Recommendation No. 2

The Department of Defence assess: (a) the risks associated with the current approach of allowing the existing framework of logistics policies and procedures to degrade over time while awaiting the implementation of the logistics management component of the Enterprise Resource Planning system; and (b) whether the current approach and related non-compliance can be authorised or needs to be re-aligned with documented requirements.

**Department of Defence Response: Agreed.**

### Recommendation No. 3

The Department of Defence review holding and carrying cost values established in its systems supporting inventory management, to ensure that they reflect a contemporary evidence-based estimate of these inventory management costs.

**Department of Defence Response: Agreed.**

### Recommendation No. 4

The Department of Defence develop a senior management response to the known issues contributing to inefficiency and overstocking in the management of general stores inventory, including a review of:

(a) inventory management training and compliance arrangements across all Domains and System Program Offices, to ensure that operational and reserve stock requirements are calculated and/or modelled and that these values are recorded in Defence's inventory management systems; and

(b) procurement against stock codes which are inactive, including those with no usage history, to determine whether these represent unauthorised overstocking.

**Department of Defence Response: Agreed.**

## **Auditor-General Report No.45 2022-23 *Australia's Provision of Military Assistance to Ukraine***

### **Background**

1. After the Russian Federation's invasion of Ukraine in February 2022, the Australian Government, like many other governments around the world, began to urgently provide financial, humanitarian and military assistance to the people and Government of Ukraine.<sup>1</sup> As of February 2023, the Australian Government had committed approximately \$688 million of support for the Government of Ukraine, including about \$510 million announced as lethal and non-lethal military assistance.<sup>2</sup>

2. The Australian Department of Defence (Defence) has been responsible for developing and providing advice to the Australian Government on what military assistance could be gifted to the Government of Ukraine without adversely affecting Australia's own military capability or preparedness. Once options were decided by the Australian Government, Defence was responsible for delivering the military assistance to a location in Europe for transport to Ukraine.

3. The majority of the military assistance provided by the Australian Government has been from Defence's own stock. Defence has also conducted procurements for items purchased from the Australian defence industry specifically for gifting to the Government of Ukraine. In addition contributions to a North Atlantic Treaty Organization (NATO) trust fund for Ukraine and a financial contribution to the United Kingdom's Ministry of Defence.

4. Australian Government announcements of military assistance to the Government of Ukraine are summarised in Table 1.1 (in Chapter 1) of this audit report.

### **Rationale for undertaking the audit**

5. Defence was required to advise on, organise and deliver military assistance, including heavy weapons and large military vehicles, to Europe quickly while ensuring that a range of domestic and international legislative and administrative requirements were complied with. This audit was

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<sup>1</sup> The Kiel Institute for the World Economy maintains a 'Ukraine support tracker'.

See: Kiel Institute, Ukraine Support Tracker Data, available from <https://www.ifw-kiel.de/publications/datasets/ukraine-support-tracker-data-17410/> [accessed 27 March 2023].

It has reported that in the period 24 January 2022 to 24 January 2023, 41 countries (including Australia) had provided approximately AUD\$224.4 billion in assistance to Ukraine. Of this, 46.4 per cent was in the form of financial assistance, 8.7 per cent was in the form of humanitarian assistance and 44.9 per cent was in the form of military assistance.

<sup>2</sup> The Australian Government has provided other forms of assistance or support to Ukraine. This has included: humanitarian assistance (through financial donations to non-government organisations), sanctions against Russian and Belarusian individuals and entities, tariffs and trade bans on certain Russian exports and imports, the provision of 70,000 tonnes of coal, and visa assistance to Ukrainian people. These forms of support are outside the scope of this audit.

For more detail, see: Department of Foreign Affairs and Trade, Invasion of Ukraine by Russia – overview, available from <https://www.dfat.gov.au/crisis-hub/invasion-ukraine-russia> [accessed 7 February 2023].

undertaken to provide independent assurance to the Parliament on Defence's development and implementation of the Australian Government's commitment to assisting the Government of Ukraine.

### **Audit objective and criteria**

6. The audit objective was to examine the effectiveness of Defence's development and implementation of Australia's approach to providing military assistance to the Government of Ukraine.

7. To form a conclusion against the audit objective, the following high-level criteria were adopted.

- Was Defence's response development effective?
- Was Defence's implementation planning and delivery effective?
- Was Defence's monitoring and reporting effective?

8. The focus of the audit was on the provision of military assistance as the largest part of Australia's contribution. The ANAO did not examine other forms of assistance such as the imposition of financial sanctions and travel bans or the issuing of visas to Ukrainian nationals. The audit scope did not include validating the financial values attributed by Defence to specific items of military equipment.

### **Conclusion**

9. Defence's development and implementation of Australia's approach to providing military assistance to the Government of Ukraine was largely effective. Defence delivered military assistance quickly and in line with Australian Government expectations, while assessing the risks and implications for Australian national interests and capability. However, not all legislative and administrative requirements were met in the context of this rapid implementation activity.

10. Defence was effective in supporting the development of an Australian Government response and moved quickly to identify options for providing military assistance to the Government of Ukraine. The department: engaged with relevant stakeholders to inform its thinking and advice; adopted established administrative and governance arrangements to identify and advise on options and implementation issues; and assessed risks to Australian national interests and preparedness. Defence provided timely, relevant and co-ordinated advice to its senior leaders and decision-makers. An exception was the completeness of its advice to decision-makers regarding financial assistance grants to NATO and the UK Ministry of Defence.

11. Defence's planning, implementation and delivery of the Australian Government's approved military assistance to the Government of Ukraine was largely effective. Defence delivered military assistance quickly to the Government of Ukraine, in accordance with Australian Government intentions. However, in the context of rapid implementation, some shortcomings were identified in respect to: demonstrating that policy approvals were secured for all items; resolving uncertainty around the legislative authority for grants of financial assistance; the completeness and quality of advice on aspects of Defence's grants administration; having Australian defence export permits for all items; securing authorisations for gifting certain items; lodging Australian Customs export declarations; and recording gifted assets.

12. Defence established effective arrangements for monitoring and reporting on the delivery of military assistance to the Government of Ukraine, and the physical control of materiel.

13. As at March 2023, Defence had not planned for or undertaken any post-implementation review activity.



## Supporting Findings

### Response development

14. Defence effectively engaged with a range of relevant stakeholders, within Australia and internationally, in its support of the Australian Government response.

- Defence consistently participated in, and provided updates to, whole of Australian government coordination committees. (See paragraphs 2.4 and 2.5)
- Defence contributed personnel to the International Donor Coordination Centre in Europe, which coordinates the physical delivery of support to Ukraine. (See paragraph 2.8)
- Defence participated in the Ukraine Defense Contact Group established by the United States, which involves 50 countries providing support to Ukraine. (See paragraph 2.9)

15. Defence adopted business as usual administrative and governance arrangements for the purpose of identifying, preparing and delivering military assistance. This was initially a fit for purpose approach. As the scale, duration and scope of the Australian Government's commitment became clearer over time, there would have been merit in Defence assessing the continuing fitness for purpose of its arrangements. (See paragraphs 2.10 to 2.16)

16. From the outset, Defence appropriately assessed risks in the context of potential impacts of gifts of military assistance on Defence's capacity to effectively defend Australia and its national interests. Recommendations to decision-makers were informed by consideration of risks to Defence preparedness and capability. (See paragraphs 2.17 to 2.23)

17. Defence provided timely, relevant and co-ordinated advice to its senior leaders, the Minister for Defence and government in relation to:

- the developing situation in Ukraine;
- options for the provision of military assistance;
- the Defence inventory value of the proposed gifts;
- the potential risks of gifting in terms of Defence's own capability, preparedness, readiness, force generation or sustainment; and
- summaries of military assistance provided to date. (See paragraphs 2.24 to 2.31)

18. Defence's advice to decision-makers, in the context of its administration of financial assistance grants to the North Atlantic Treaty Organization (NATO) and the United Kingdom Ministry of Defence, was not complete and did not satisfy all mandatory requirements of the Commonwealth Grants Rules and Guidelines. (See paragraphs 2.32 and 2.33)

### Implementation

19. Defence relied on its normal processes for tasking relevant business areas within Defence and for those areas to understand and fulfill any obligations within their usual areas of responsibility. In the context of urgent directions from the Australian Government to provide military assistance to the Government of Ukraine, Defence did not appoint a senior responsible officer or establish a taskforce to undertake planning, or develop a bespoke implementation plan to guide the provision of military

assistance to the Government of Ukraine. Defence has not revisited its general approach to planning. (See paragraphs 3.2 to 3.7)

20. Defence delivered military assistance quickly to the Government of Ukraine. However, Defence is not able to demonstrate that all Australian Government policy approvals were secured for 13.5 per cent of the military assistance despatched in 2022 (valued at \$36.4 million). Further, 58 items with a value of \$38.4 million were transferred to the Government of Ukraine without being included in an exchange of letters between the Governments of Australia and Ukraine. (See paragraphs 3.9 to 3.20)

21. Defence undertook procurement processes specifically for the purchase of items to be gifted to the Government of Ukraine. For these eight procurements, Defence relied on provisions for limited tender in the Commonwealth Procurement Rules (CPRs). Defence assessed value for money as required by the CPRs and documented that it was satisfied that the offerings represented value for money. (See paragraphs 3.21 to 3.33)

22. Defence acted quickly to facilitate grant funding approved by the Australian Government for the North Atlantic Treaty Organization (NATO) and the United Kingdom Ministry of Defence (UK MOD). Defence did not take steps to resolve uncertainty around the legislative authority for the payments, which had been identified while developing the first grant to NATO. Defence's advice to decision-makers, in the context of its administration of financial assistance grants to NATO and the UK MOD, was not complete and did not satisfy all mandatory requirements of the Commonwealth Grants Rules and Guidelines (CGRGs). (See paragraphs 3.34 to 3.70)

23. As at December 2022, Defence had partly complied with relevant legislative and other requirements for the export of military assistance to the Government of Ukraine. Certain items did not have, before their export to Ukraine: an Australian Defence export permit; gifting authorisations under the Public Governance, Performance and Accountability Act 2013 (PGPA Act); and lodged Australian Customs export declarations. (See paragraphs 3.72 to 3.108)

24. Defence has not effectively accounted for gifted assets by taking appropriate action to record the disposal of gifted equipment in its records. (See paragraphs 3.109 to 3.113)

### **Monitoring and reporting**

25. Defence established appropriate arrangements for monitoring and reporting on the delivery of military assistance to the Government of Ukraine. These arrangements included physical controls for the transportation and security of military assistance and acquittals for international grants, with NATO and the UK MOD confirming that funding had been received and used in line with the agreed purpose. (See paragraphs 4.3 to 4.25)

26. While there were some discussions in the latter part of 2022 about improving aspects of Defence's processes, as at March 2023 Defence had not planned for or undertaken any 'lessons learnt' or post-implementation review activity for its delivery of military assistance to the Government of Ukraine. More than one year into this activity, there is scope for Defence to review or evaluate its arrangements, to inform its approach to and implementation of any further assistance initiatives. (See paragraphs 4.27 to 4.32)

## Recommendation

27. The Auditor-General did not make any recommendations. Two opportunities for improvement were identified, relating to Defence:

- resolving, in consultation with the Department of Finance and the Department of Foreign Affairs and Trade, issues identified in its administration of financial assistance grants provided by the Australian Government to assist the Government of Ukraine; and
- reviewing or evaluating its arrangements for the delivery of military assistance to the Government of Ukraine, to inform its approach to and implementation of any further assistance initiatives.