

Joint Committee on Public Accounts and Audit

Inquiry into ANAO Report 16 (Major Projects Report) – 17 March 2016

ANSWER TO QUESTION ON NOTICE

Department of Defence

Topic: C-27J Spartan – Cost impact

Question reference number: 2

Senator: Conroy

Type of question: asked on Thursday, 17 March 2016, Hansard page 5

Date set by the committee for the return of answer: 21 April 2016

Question:

ACTING CHAIR: Turning to the C27J Spartan, this report highlights significant risk associated with the U.S. Air Force's divestiture. Can anyone talk to me about what has occurred there?

Rear Adm. Dalton: I can cover it at a little bit, if you like?

ACTING CHAIR: Yes, that would be great.

Rear Adm. Dalton: Do you have any specific questions?

ACTING CHAIR: Has the U.S. Air Force left the program?

Rear Adm. Dalton: They have.

ACTING CHAIR: What is the flow-on impact? I imagine they would have been, presumably, the largest customer for this platform.

Rear Adm. Dalton: There are some flow-on effects to Air Force with the US divestiture, but it is still being procured through the US system as a foreign military sale, so we still have access to the price that the U.S. Air Force had negotiated. As to the program maturing in its fully envisaged state in the US, that is not going to happen. So that has had some impact in Australia in terms of having to develop some additional airworthiness certificates and proof that the system will operate to its fullest extent in Australia.

ACTING CHAIR: Surely there must be a cost impact, given that the scale of production will fall?

Rear Adm. Dalton: Because the contract was signed through FMS it is being managed by the US still as a foreign military sale, and at the moment we are predicting that it will complete in budget.

ACTING CHAIR: 'In budget' is different from getting the platforms at the original contracted price. It might still be within the envelope of the acquisition, but do we know whether the actual platform cost will increase?

Rear Adm. Dalton: I will take that on notice, but my understanding is that there is no expectation that the individual aircraft price will increase above what was agreed in the original foreign military sales case.

Answer:

Pricing for C-27J aircraft acquired by Australia is secured in the Foreign Military Sales case and has not changed despite United States Air Force divestiture decisions.

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ANSWER TO QUESTION ON NOTICE

Department of Defence

Topic: Heavyweight Torpedo – Schedule Slippage

Question reference number: 3

Senator: Conroy

Type of question: asked on Thursday, 17 March 2016, Hansard page 6

Date set by the committee for the return of answer: 21 April 2016

Question:

ACTING CHAIR: Can I turn to the Heavyweight Torpedo project now? We have seen a five-month in-year slippage, which cumulatively means a 63-month slippage on the project, so that is five years of delay in this project—that is on table 4 the report. Why has the schedule slipped so much, Admiral Dalton?

Rear Adm. Dalton: I would have to take that one on notice. I do not have the subject matter expert with me. One of the issues will undoubtedly be the availability of Collins class submarines going through that update cycle, so it is quite possibly related to the upkeep cycle for the full-cycle docking for Collins.

Answer:

The Heavyweight Torpedo modifications can only be undertaken during a Full Cycle Docking. Changes to the submarine Usage and Upkeep Cycle, including adoption of the 10+2 year operating cycle recommended in the Coles Report, have delayed completion of the HMAS Collins Full Cycle Docking until mid 2018. This date has not changed since the 2014-15 Major Projects Report was tabled, and Note 3 to Table 3.3 explains the variation.

The in year delay of five months is due to a reassessment of the time required for administration and documentation activities leading to award of Final Operational Capability following completion of the HMAS Collins implementation. The delay in award of Final Operational Capability does not affect availability or employment of the submarines.

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ANSWER TO QUESTION ON NOTICE

Department of Defence

Topic: Heavyweight Torpedo – Weight of torpedo mounted dispenser

Question reference number: 4

Senator: Conroy

Type of question: asked on Thursday, 17 March 2016, Hansard page 6

Date set by the committee for the return of answer: 21 April 2016

Question:

ACTING CHAIR: You might need to take my next question on notice as well, which is on page 391 of the report. It identifies the weight of the torpedo mounted dispenser as creating a manual handling hazard for, presumably, Navy personnel. I would be interested in understanding what is happening there, and the implications of that, for personnel.

Rear Adm. Dalton: I will take that on notice.

Answer:

The hazard applies to personnel fitting the guidance wire dispenser to a torpedo onboard the submarine, due to a combination of the weight of the dispenser and the cramped access conditions. This activity is only required if the fitted dispenser becomes defective onboard the submarine, as the torpedo is embarked with a dispenser already fitted.

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ANSWER TO QUESTION ON NOTICE

Department of Defence

Topic: LAND 121 – Original FOC

Question reference number: 5

Senator: Conroy

Type of question: asked on Thursday, 17 March 2016, Hansard page 8

Date set by the committee for the return of answer: 21 April 2016

Question:

ACTING CHAIR: General Coghlan, can I turn to Land 121 phase 3 and page 119 of the report. In table 2.5, which lists pre- and post-Kinnaird schedule variance, it has Overlander with an FOC variance of only seven per cent. I am interested in how that ties up with the fact that we effectively had a six-year gap between the initial second pass approval and the updated second pass in 2013. Has that had no real impact on the FOC?

Major Gen. Coghlan: The FOC was reset as a part of that process. At this stage, our phase 3B IMR is 2018—fourth quarter. Phase 3B IOC is 2019—the fourth quarter—with a final 3B FOC of 2023—some years out yet.

ACTING CHAIR: What was the original FOC from the 2007 decision for phase 3?

Major Gen. Coghlan: I will have to take that on notice.

Answer:

The original Final Operational Capability from the 2007 decision for LAND 121 Phase 3 was 2019.

Joint Committee on Public Accounts and Audit

Inquiry into ANAO Report 16 (Major Project Report) – 17 March 2016

ANSWER TO QUESTION ON NOTICE

Department of Defence

Topic: Project re-baselining

Question reference number: 6

Senator: Conroy

Type of question: asked on Thursday, 17 March 2016, Hansard page 8

Date set by the committee for the return of answer: 21 April 2016

Question:

ACTING CHAIR: Okay. Are there any other projects on this list that have had a re-baselining of their schedule? Would you mind taking that on notice?

Major Gen. Coghlan: Without doubt, because of its length, the Bushmaster project would have been reset.

ACTING CHAIR: I see that pre-Kinnaird. Clearly there has been some schedule variance in that very important developmental project.

Major Gen. Coghlan: There has.

ACTING CHAIR: So if you could take that on notice.

Answer:

The Major Project Report (MPR) provides an accurate and transparent record of schedule performance for those projects included in the report. Schedule variance is calculated as a percentage increase (or decrease, if applicable) in the estimated project duration from Government approval to Final Operational Capability (FOC).

Project milestones are sometimes re-baselined at subsequent approval points. For the Major Project Report, the decision to measure variance - using the updated FOC date - is made in the context of Final Operational Capability requirements.

Three MPR projects have had their schedule variance calculated from later approved FOC baseline dates:

- Overlander Medium/Heavy,
- UHF SATCOM, and
- Bushmaster Vehicles.

For these projects, significant changes were made to the capability requirements defining FOC, making it impracticable to measure schedule performance from the original base line project milestone dates. The ANAO has assured this data in the Major Project Report.

The individual Product Data Summary Sheets - along with the delays to FOC discussed on page 117 of the MPR - provide a complete picture of the project approvals, schedule history and any delays. Further statistical analysis - such as Table 2.5 on page 119 of the MPR - is also provided in the tables and graphs of the Major Project Report.

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ANSWER TO QUESTION ON NOTICE

Department of Defence

Topic: Alliance Contract – Raytheon's share

Question reference number: 7

Senator: Conroy

Type of question: asked on Thursday, 17 March 2016, Hansard page 12

Date set by the committee for the return of answer: 21 April 2016

Question:

Mr CONROY: Given how many contracts the government has given Navantia, one would hope there would be a bit more integration and flexibility. I go back to the cost increase. If there was a \$290 million pain-gain risk, did the three alliance partners forfeit that \$290 million?

Mr Croser: They did.

Mr CONROY: What was Raytheon's share of that?

Mr Croser: Raytheon had a procurement fee which was part of the original contract because of their different role with respect to combat systems. I will take that on notice, but I believe it was around \$70 million over the program, and that was paid quarterly. The two companies—Raytheon and ASC—shared that gain on the basis of performance. In about 2012, the performance had dropped to the point where they were not technically on a pro rata basis in gain, and so payments of that in advance of delivery of the program share of the gain ceased. That was brought to account at the new contract in that they did not receive—and had to repay, in fact—their gain that they had received in advance based on performance. The new contract allows a gain share for Raytheon for future work from the time that the contract was signed in December last year, for Novantia for performance against the schedule and cost and for ASC a smaller element against performance.

Mr CONROY: They have had to pay back gain, but did they actually have any pain inflicted? Did they have to reduce their fee?

Mr Croser: The liquidated damages and pain—again, I would take it on notice because it is a question that is quite technical in nature. I would say that they were not asked to pay the pain but they lost all share of gain and their work is only paid for work that they have conducted, and there is no corporate overhead allowed to be paid against it.

Answer:

Raytheon stood to earn what is known as a Target Fee, made up of corporate overhead and profit. The portion of the Target Fee that had been paid to Raytheon to 5 December 2015 – when the Alliance Based Target Incentive Agreement (ABTIA) was amended – was paid back to the Air Warfare Destroyer Program in accordance with the revised ABTIA terms. Raytheon also received a Procurement Fee, paid over 10 years. Raytheon's fees are commercial-in-confidence.

Raytheon's prospect of fee earnings under the revised ABTIA terms is reduced.

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ANSWER TO QUESTION ON NOTICE

Department of Defence

Topic: Alliance contract – Raytheon procurement fee

Question reference number: 8

Senator: Conroy

Type of question: asked on Thursday, 17 March 2016, Hansard page 13

Date set by the committee for the return of answer: 21 April 2016

Question:

Mr CONROY: I have one more question for you on this before I ask the Auditor-General's opinion. The \$1.2 billion real cost increase—is there a procurement fee that Raytheon enjoy out of that contract change?

Mr Croser: I believe that the procurement fee has been fully paid up. I will check that on notice but I believe that they have been paid—or it may only be a couple of million that was outstanding at the time of the reset. I do not believe the procurement fee was increased; in fact I know was not increased or topped up in anyway.

Mr CONROY: Can you take on notice?

Mr Croser: Yes.

Mr CONROY: Out of the \$1.2 billion real cost increase, will Raytheon receive any money for anything other than actual work done?

Mr Croser: I will take it on notice. I can say that Raytheon, ASC and Navantia have a gain share element to their contract.

Mr CONROY: Could you take it on notice and outline what that gain share is?

Answer:

Raytheon is not entitled to any additional procurement fees under the revised Alliance Based Target Incentive Agreement (ABTIA) contract terms following the Real Cost Increase.

Under the revised ABTIA terms, Raytheon's direct project costs for Air Warfare Destroyer work performed will be reimbursed and, subject to meeting specific cost and schedule performance criteria, Raytheon will have an entitlement to gain share fees, a cost performance fee and a schedule performance fee. Raytheon's potential gain share is a maximum of 30 per cent of savings against the Target Cost Estimate.

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ANSWER TO QUESTION ON NOTICE

Department of Defence

Topic: Industry skilling initiatives

Question reference number: 10

Senator: Conroy

Type of question: asked on Thursday, 17 March 2016, Hansard page 14

Date set by the committee for the return of answer: 21 April 2016

Question:

Mr CONROY: Or other people. I have one more issue that is on page 78, which is a good summary of other industry policy issues that affect defence and, in particular CASG. The industry skilling initiatives highlight that some of the initiatives under the old ISPE and SADI programs were picked up and continued under the new white paper and others were not. You will probably want to take this on notice, but can you highlight which programs were continued and which ones were not?

Rear Adm. Dalton: I will take that on notice, Mr Conroy, but I would note that the defence industry policy statement has brought a lot of these programs together. It is not a matter of whether they have been discontinued or not, it is a matter of how they have been amalgamated under the new process.

Mr CONROY: If you could take on notice to marry these up—for example, SADI from around 2005 and ISPE in 2009, and now you have the new statement. Can we have clarification of which programs still exist, which ones are covered by other programs and which ones have been discontinued. Secondly, are you in a position to talk about the Priority Industry Capability Development Fund and how that will handle sustaining the PICs versus what was there before?

Rear Adm. Dalton: We would have to take that on notice.

Answer:

- (1) Please refer to Question on Notice 174 from 17 March 2016 Additional Budget Estimates hearing.
- (2) The 2016 Defence Industry Policy Statement states the existing Priority and Strategic Industry Capabilities will be replaced with a new Sovereign Industrial Capability Assessment Framework. Existing programs that use the Priority Industry Capability framework will continue to run until the introduction of the Sovereign Industrial Capability Assessment Framework in the second quarter of 2017.

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ANSWER TO QUESTION ON NOTICE

Department of Defence

Topic: AIR 5402

Question reference number: 11

Member: Brodtmann

Type of question: asked on Thursday, 17 March 2016, Hansard page 15

Date set by the committee for the return of answer: 21 April 2016

Question:

Ms BRODTMANN: I have a question about the Air to Air Refuelling Capability AIR 5402 project. Who do I direct the question to?

Rear Adm. Dalton: I will take it on notice, Ms Brodtmann, so fire away and I will see if I can answer it.

Ms BRODTMANN: I notice that it has come off the list of projects for concern.

Rear Adm. Dalton: That is correct; it is no longer a project of concern.

Ms BRODTMANN: As you know, there were many modifications on that—significant problems with the boom meeting up with the pods, and whatever. I am interested to know why it has been taken off the list of projects for concern.

Rear Adm. Dalton: The simple answer is that it has been taken off the list of projects for concern because the capability is now in service and Air Force is happy with it. That includes both the air refuelling pods and the air refuelling boom. I would note—and I raised it in my opening statement—that KC30 capability is in service now in the Middle East. It is what the US Air Force calls their go-to tanker. As far as I am aware, it is doing a really excellent job servicing the Air Combat Group in the Middle East, as well as other nations.

Ms BRODTMANN: From memory, how long was that delayed, given those challenges and experiences in terms of the connection?

Rear Adm. Dalton: I would have to take that on notice.

Answer:

Air 5402 was removed from the Project of Concern List on 6 March 2015 due to the air refuelling boom technical issues being remediated. As a result Final Operational Capability (FOC) is scheduled for approval in May 2016. This constitutes a 57 month slip from the initial FOC date as identified in the Material Acquisition Agreement.

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ANSWER TO QUESTION ON NOTICE

Department of Defence

Topic: MRH-90 – Cost Implications of delays

Question reference number: 12

Member: Brodtmann

Type of question: asked on Thursday, 17 March 2016, Hansard page 15

Date set by the committee for the return of answer: 21 April 2016

Question:

Ms BRODTMANN: All right. In terms of the delays that we have touched on today with MRH90, I have just been going through the report and I am trying to get a sense of how much these delays have cost. I will put on notice a detailed question on what that actually means in terms of cost over the scheduled delay—so what it means in terms of cost for the refit, the changes and having to make improvements to what some would think were stuff-ups—as well as the issue of what it meant for personnel and bases. Everyone was getting revved up for these things to come online at a particular point in time, and then they were obviously told to go slow. What did that mean in terms of cost implications?

Rear Adm. Dalton: We will take that on notice.

Answer:

An accurate aggregate figure for all cost implications as a result of the delayed delivery of the MRH90 aircraft is unable to be specified as many costs have been offset through commercial negotiations, improved support arrangements and improved intellectual property rights.

ANAO Performance Audit Report No.52 2013-14 estimated that a cost of \$311 million was incurred due to the need to extend the service life of S-70A-9 Black Hawk fleet. The increased costs to support Black Hawk have been partially offset by reduced flying hours on MRH90 and therefore savings to the Australian Government.

Costs recovered by Defence as a result of project delays were generally not direct financial payments, but rather enhanced acquisition and sustainment contract provisions. These enhancements included; additional access to intellectual property, new aircraft cabin seats, the 47th MRH90 aircraft, a Repair by the Hour Sustainment Scheme, final spares and support equipment, a warranty that sufficient major spares had been procured to support the mature rate of effort, resolution of technical deficiencies, obsolescence resolution and the strengthening of linkages between acquisition and sustainment contracts.

The MRH90 retrofit program undertaken on the first 13 aircraft, which remediated technical deficiencies and ensured all aircraft will be delivered to a consistent configuration, was undertaken at no additional cost to the Commonwealth.