

CHAPTER NINE

OPERATING COSTS

Logistics and Operating Costs

9.1 The increasing pressure on general operating costs was a persistent theme in evidence given by Defence. This includes increasing logistics support costs to maintain ageing or obsolescent platforms, and the personnel and other operating costs incurred in bringing new capabilities on line. This aspect affects the Navy and Air Force more than the Army, because of the reliance of the former two Services on high technology platforms and complex systems requiring technical maintenance.

9.2 The Committee was provided with the following indication of the magnitude of annual operating costs of some major platforms:¹

Table 9.1 Indicative Personnel and Operating Costs for Major Platforms

| Capability | Annual operating cost (in A\$ millions) |
|---------------------------------|---|
| F-111 aircraft | 244 |
| F/A-18 aircraft | 300 |
| <i>Adelaide</i> class frigates | 152 |
| <i>Perth</i> class destroyers | 106 |
| <i>Collins</i> class submarines | 36* |
| <i>Anzac</i> class frigates | 23* |

* indicates that these are preliminary figures as these systems were just entering service at time of advice

9.3 Where a completely new capability is acquired, such as the AEW&C aircraft, the funding required goes beyond the capital cost of purchasing the platform, and imposes additional personnel and operating costs. Maintenance facilities must be constructed, operators must be trained, spare parts must be acquired and stored and logistic support strategies must be developed. Where the new capability replaces an existing one, the additional costs are considerably smaller, because offsets exist against the cost of supporting the new platform - the cost of the personnel, fuel and maintenance is already included within the baseline of funding established for the previous capability. Unfortunately, over the next 10 years, new capabilities will be introduced into service more rapidly than old capabilities are retired.

9.4 Navy identified the need to fund the operation of the new *Anzac* class frigates, and the new coastal minehunters in the next financial year, offset only by the decommissioning of a single destroyer escort, HMAS *Torrens*. This situation will worsen

1 Friends of the Earth, Submission, p. S246.

over the next seven years, as approximately 20 vessels and a new helicopter capability are to be commissioned, while the only offsets available are the two submarines and a destroyer escort currently planned for decommissioning.² Navy gave further evidence that:

... the net increase in operating costs for the new capabilities presently approved is some \$40 million next financial year, rising to about \$80 million in 2001-02 and thereafter. This is after allowing for the offsets available from the decommissioning of capabilities, such as the DDGs which will be withdrawn in that period.³

9.5 Navy also identified existing and expected funding pressures in providing logistic support, particularly in the areas of naval aviation, some weapon systems, and ship repair.⁴ The size of the current year's logistic shortfall was estimated at around \$50 to \$60 million.⁵ These logistic support problems were not restricted to platforms approaching obsolescence. One example raised in evidence was that of the Navy's Seahawk helicopter, which required logistic support funding beyond what was originally planned, due to its failure to achieve the expected mean times between failures.⁶

9.6 In its submission, Defence identified the quanta of the personnel and operating costs associated with the AEW&C capability, and for the helicopters for the *Anzac* frigates, as potentially greater than \$360 million,⁷ and suggested that taking this out of existing future programming would be difficult to fit in without impacting on funds available for other new capabilities.⁸

9.7 Air Force highlighted the increasing logistic costs faced in maintaining ageing aircraft, and has assessed that there is about a seven to eight per cent per annum compound increase in funding required to support ageing aircraft over that necessary to provide logistic support for a young aircraft fleet. With the major proportion of the RAAF fleet either over or near the 25-year mark, continuing support of ageing aircraft is becoming a major issue for Air Force.⁹ Air Force claimed that the logistic shortfall at its present rate of effort was underfunded by about \$400 million across the four-year development program.¹⁰

9.8 Where an item of newly-acquired equipment to be supported does not replace an existing capability, or where estimates of the logistic support requirement for a new capability have been optimistic, the funding shortfall must be found from operating costs within the Defence budget, if it is not to reduce investment available for other items of equipment. The option of reducing activity rates is also unattractive, as this in turn reduces the preparedness of the ADF. The remaining option is that the additional funds must be found by eating into efficiency gains.¹¹ Logistics funding requirements have been the subject of extensive review in the development of the current FYDP (1998-02). Additional funds

2 Oxenbould, Dept. of Defence, Transcript, p. 171.

3 *ibid.*

4 *ibid.*, p. 170.

5 *ibid.*, p. 181.

6 *ibid.*, p. 180.

7 Dept. of Defence, Submission, p. S287.

8 Tonkin, Dept. of Defence, Transcript, p. 7

9 McCormack, Dept. of Defence, Transcript, p. 47.

10 *ibid.*

11 Tonkin, *ibid.*

have been allocated, principally from expected DRP savings, to meet urgent logistics requirements to ensure that the ADF remains at the minimum safe levels of capability.¹²

Preparedness and Operational Readiness

*At current levels and future budgeted levels of expenditure, we can't afford an effective and efficient military and provide the necessary equipment and give the people the hours on that equipment to keep them razor sharp.*¹³

9.9 Operating costs currently account for around 32 per cent of the Defence budget,¹⁴ and are primarily expended on aspects of Defence activities which contribute to preparedness. With the increasing pressures on both the personnel and capital equipment portions of the Defence budget, there exists an inclination to place preparedness aspects at lowest priority. While this enables diversion of funds to areas of greater need, it consequently allows a decline in preparedness.

9.10 The strategic review defines preparedness as the combination of the military readiness and the sustainability of ADF assets in operations,¹⁵ and warns:

holding our forces at high levels of preparedness is expensive, carrying high opportunity costs in resources for training and stockholdings which would have to be foregone in the development of future capabilities.¹⁶

9.11 Preparedness is a costly commodity. One example provided in evidence was that taking a battalion from 14 days readiness to seven days readiness costs approximately \$20 million.¹⁷ Costs of this magnitude emphasise the importance of prudent judgments on readiness levels. Where a force maintained at high readiness is not required, these costs are wasted where they may have been better spent on development of the ADF.

9.12 The ANAO conducted a preliminary audit into the management of ADF preparedness in 1995-96.¹⁸ The audit found deficiencies in defining the resource requirements for achievement of specific preparedness levels, but was not intended to scrutinise actual levels of preparedness, and reached no assessment of the ADF's then-current ability to meet its preparedness requirements. The Committee sought other evidence of the impacts of current funding levels in this area.

9.13 The problem of low readiness levels was widely acknowledged. Most Defence witnesses conceded that readiness levels were either unsatisfactorily low, or were at a level commensurate with meeting only essential Government-directed tasks and minimum

12 Dept. of Defence, Submission, p. S334.

13 Minister for Defence, Hon Ian McLachlan MP, on the release of the Report on the Defence Efficiency Review, Parliament House, Canberra, 11 April 1997.

14 Dept. of Defence, Submission, p. S318.

15 *Australia's Strategic Policy*, op. cit., p. 38.

16 *ibid.*

17 Barrie, Dept. of Defence, Transcript, p. 271.

18 ANAO Audit Report No 17, 1995-96, op. cit.

standards of safety and operational proficiency.¹⁹ These levels gave very little scope for further reductions before the capacity to conduct operations was degraded.²⁰ One Defence submission warned:

The further lowering of readiness would lead to an increase in the response time and a reduction of options available to Government as a result of the degradation or loss of essential skills.²¹

9.14 Almost uniformly, the poor levels of readiness were attributed to low levels of investment in operating costs, due to the need to allocate resources to investment and development.²²

9.15 Although there was a general concession of the current undesirable state of operational readiness levels as the result of funding shortages, specific evidence was not generally forthcoming, except from Army. The acutely low state of preparedness within Army was admitted in the rationale for the *Army 21* study, which conceded that substantial warning time and financial expenditure would be required to mobilise for a major conflict,²³ and that 'with some exceptions, reserve units are understaffed, poorly equipped and have a low readiness level'.²⁴ Hollowness in the Army was also the primary shortcoming used as justification for the subsequent Restructuring the Army program, and Army gave clear evidence that this deficiency had yet to be rectified. The Deputy Chief of Army acknowledged that the majority of Army units were not fully manned, and required further collective training, at unit and sub-unit level, to be ready for deployment on operations.²⁵ Further, a history of funding pressures has forced Army to accept reductions in personnel and to reduce readiness levels of units already at low readiness.²⁶

9.16 The Committee accepted that a number of recent media reports on Army ammunition shortages and restrictions also provided evidence of problems within the ADF in maintaining readiness standards.²⁷ In particular, one report identifies 'resourcing problems' and contends that:

Army is not currently maintaining capability and further reductions to ammunition will further reduce capability below recognised minimum safe standards.²⁸

9.17 In some cases ADF members are experiencing difficulty in obtaining basic weapons qualifications as a result of basic ammunition shortages. The Committee believed

19 Dept. of Defence, Submission, p. S314.

20 Barrie, Dept. of Defence, Transcript, p. 25.

21 Dept. of Defence Submission, loc. cit.

22 Barrie, Dept. of Defence, Transcript, p. 236.

23 From *Army 21*, quoted by Minister for Defence, Hon Ian McLachlan MP, *Hansard*, p. 8528, 25 September 1997.

24 *ibid.*

25 *Restructuring the Australian Army*, op. cit., p. 34.

26 Hartley, Dept. of Defence, Transcript, p. 30.

27 Warren, CPL F.D., 'Ammo shortfall affects training', letter to the Editor, *Australian Army Newspaper*, 18 September 1997. Also Greenlees, Don, 'Army limits ammunition for training' in *The Australian*, 8 October 1997.

28 Attributed to COL Michael O'Brien, Chief of Staff, Deployable Joint Force Headquarters, in Greenlees, Don, 'Army faces critical shortages', *The Australian*, 3 October 1997.

that this was also the inference of an Army remark that it had 'considerable hollowness in certain stock levels and pressures in maintaining existing stocks'.²⁹ Army also admitted that war stocks of some types of ammunition were currently being consumed to meet training requirements, due to current deficiencies in those ammunition categories.³⁰ As well as shortages of basic rounds, anecdotal evidence claims that several categories of missiles are in short supply throughout the ADF, with some units being limited to a single firing per year. Although adequate ammunition stockholdings is only a single aspect of preparedness, the Committee believed that evidence of ammunition shortages is an important and obvious indicator of overall deficiencies.

9.18 The current hollowness of some Army units was demonstrated in some overseas deployments over the last few years. Overseas deployment of the Australian land force is now identified as its most likely military task.³¹ Yet the ADF deployments to Somalia and Cambodia put great stress on the limited resources, in terms of the equipment and specialists available in each unit. In a similar vein, the deployment of three warships to operations in the Persian Gulf in 1991 required the transfer of essential self-defence weapons from other units in the fleet. Had they been requested, the ADF would have been unable to commit either F/A-18s or F-111s to the contingent deployed to the Persian Gulf in early 1998 due, in part, to the lack of self-protective electronic counter measures. The Committee viewed these as examples of unacceptably low levels of preparedness. The Committee was also critical of recent situations where only token military forces could be contributed to important crisis situations, because an insufficient proportion of the ADF was maintained at the level of readiness required for such deployment. Such occurrences serve to undermine Australia's military credibility within the region and give the Australian public cause to question the level of outcome which can be achieved from an annual investment of over \$10 billion.

9.19 From the evidence presented, there is little doubt that several aspects of preparedness have suffered as the result of inadequate funding for operating costs. This was particularly evident in Army, although current initiatives under the RTA program may alleviate some hollowness. It is noteworthy that the success of the RTA will depend on a considerable increase in funding for operating costs and equipment.³²

9.20 The Committee acknowledges that strategic circumstances over the past few years have to date permitted a degree of risk management to be tolerated in preparedness planning. However, a recurrent theme in evidence presented to this inquiry was that preparedness has now decreased to a level where further cuts in the proportion of funding allocated to operational activities would result in unacceptable levels of strategic risk.

9.21 The Committee concluded that the clear evidence of decline in the vital area of preparedness indicated that the area of operating costs was under considerable pressure, as were the areas of personnel funding and investment. While the Committee was unable to establish the quanta of any deficiency, it was able to make three observations:

- Even given Australia's current strategic circumstances, further cuts in operating costs would result in unacceptable strategic risk.

29 Hartley, Dept. of Defence, Transcript, p. 30.

30 Hartley, Dept. of Defence, Transcript from Senate Estimates Committee Hearings, 26 February 1998, from *Hansard*, p. 45.

31 See *Australia's Strategic Policy*, op. cit., p. 39, under 'Readiness'.

32 Dept. of Defence, Submission, p. S334.

- There is a current need to address a number of preparedness deficiencies, particularly regarding hollowness within the Army, and ammunition levels to meet realistic usage rates, and to sustain required contingency stockholdings.
- Any deterioration in Australia's strategic situation will require an immediate and substantial increase in the apportionment of funding to operating costs within the ADF, to permit a significant increase in preparedness.