



COMMONWEALTH OF AUSTRALIA

Official Committee Hansard

SENATE

FOREIGN AFFAIRS, DEFENCE AND TRADE LEGISLATION
COMMITTEE

ESTIMATES

(Budget Estimates)

WEDNESDAY, 31 MAY 2006

CANBERRA

BY AUTHORITY OF THE SENATE

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SENATE

FOREIGN AFFAIRS, DEFENCE AND TRADE LEGISLATION COMMITTEE

Wednesday, 31 May 2006

Members: Senator Johnston (*Chair*), Senator Hutchins (*Deputy Chair*), Senators Bishop, Ferguson, Payne and Stott Despoja

Senators in attendance: Senators Mark Bishop, Faulkner, Fierravanti-Wells, Ferguson, Hogg, Johnston, Hurley, Lightfoot, Nettle, O'Brien, Payne, Ronaldson and Trood

Committee met at 9.03 am

DEFENCE PORTFOLIO

In Attendance

Senator Sandy Macdonald, Parliamentary Secretary for Defence

Department of Defence

Portfolio overview

Mr Ric Smith AO, PSM, Secretary of Defence

Air Chief Marshal Angus Houston AO, AFC, Chief of Defence Force

Air Commodore John Harvey, Director General, New Air Combat Capability

Air Commodore Rodney Luke, Director General, Airlift and Training Systems

Air Commodore Brian (Jack) Plenty, Director General, Headquarters Joint Operations Command Project

Air Commodore Colin Thorne, Director General, Aerospace Maritime and Surveillance

Commodore Peter Law, Director General, Guided Weapons and Explosive Ordnance

Commodore Mark Campbell

Rear Admiral Trevor Ruting, Head, Maritime Systems Division

Brigadier Anthony Fraser

Brigadier Mark Patch, Director General, Army Aviation Systems

Ms Shireane McKinnie, Head, Electronic and Weapon Systems Division

Budget summary (financial statements, capital investment budget and improvement initiatives)

Mr Phillip Prior, Chief Finance Officer

Mr George Veitch, First Assistant Secretary Budgets and Financial Planning

Capability development

Lieutenant General David J Hurley AO, DSC, Chief Capability Development Group

Dr Ralph Neumann, First Assistant Secretary Capability Investment and Resources

Defence Materiel Organisation

Outcome 1: Defence capabilities are supported through efficient and effective acquisition and through-life support of materiel

Output 1.1: Management of capability acquisition (including major capital equipment projects)

Output 1.2: Capability sustainment

Output 1.3: Policy advice and management services

Dr Stephen Gumley, Chief Executive Officer Defence Materiel Organisation
Mr Kim Gillis, Acting Deputy Chief Executive Officer Defence Materiel Organisation
Dr Ian Williams, Chief Finance Officer Defence Materiel Organisation
Mr Frank Lewincamp, Chief Operating Officer, Defence Materiel Organisation

Major capital facilities projects

Mr Alan Henderson PSM, Deputy Secretary Corporate Services
Mr Geoffrey Beck, Head Infrastructure Division

Defence outcomes**Outcome 1: Command of operations in defence of Australia and its interests****Output 1.1: Command of operations****Output 1.2: Defence Force military operations and exercises****Output 1.3: Contribution to national support tasks**

Lieutenant General Ken Gillespie, Vice Chief of Defence Force, AO, DSC, CSM
Rear Admiral James Goldrick, Commander Joint Offshore Protection Command, AM,
CSC, RAN

Outcome 2: Navy capability for the defence of Australia and its interests**Output 2.1: Capability for major surface combatant operations****Output 2.2: Capability for naval aviation operations****Output 2.3: Capability for patrol boat operations****Output 2.4: Capability for submarine operations****Output 2.5: Capability for afloat support****Output 2.6: Capability for mine warfare****Output 2.7: Capability for amphibious lift****Output 2.8: Capability for hydrographic, meteorological and oceanographic operations**

Vice Admiral Russ Shalders, Chief of Navy, AO, CSC
Mr David Spouse, Director General, Navy Business Management

Outcome 3: Army capability for the defence of Australia and its interests**Output 3.1: Capability for special operations****Output 3.2: Capability for medium combined arms operations****Output 3.3: Capability for light combined arms operations****Output 3.4: Capability for army aviation operations****Output 3.5: Capability for ground based air defence****Output 3.6: Capability for combat support operations****Output 3.7: Capability for regional surveillance****Output 3.8: Capability for operational logistic support to land forces****Output 3.9: Capability for motorised combined arms operations****Output 3.10: Capability for protective operations**

Lieutenant General Peter Leahy, Chief of Army, AO
Mr Lance Williamson, Director General Corporate Management and Planning—Army

Outcome 4: Air Force capability for the defence of Australia and its interests**Output 4.1: Capability for air combat operations****Output 4.2: Capability for combat support of air operations****Output 4.3: Capability for surveillance and response operations**

Output 4.4: Capability for airlift operations

Air Marshal Geoff Shepherd, Chief of Air Force, AM

Ms Grace Carlisle, Assistant Secretary Resource and Planning—Air Force

Outcome 5: Strategic policy for the defence of Australia and its interests**Output 5.1: International policy, activities and engagement****Output 5.2: Strategic policy and military strategy**

Mr Michael Pezzullo, Deputy Secretary Strategy

Outcome 6: Intelligence for the defence of Australia and its interests**Output 6.1: Intelligence**

Mr Shane Carmody, Deputy Secretary Intelligence and Security

Outcome 7: Superannuation and housing support services for current and retired defence personnel

Output 7.1: Superannuation support services for current and retired defence personnel**Output 7.2: Housing assistance for current defence personnel****Output 7.3: Other administered expenses and revenue****Business processes****Inspector General**

Claude Neumann, Inspector General

Chief Information Officer

Air Vice-Marshal John Monaghan AM, Chief Information Officer
Corporate Services

Mr Alan Henderson PSM, Deputy Secretary Corporate Services

Mr Mark Cunliffe, Head Defence Legal

Coordination and Public Affairs

Mr Peter Jennings, Chief of Staff Australian Defence Headquarters and Head of Coordination and Public Affairs

People**Defence Personnel**

Major General Mark Evans, Head Defence Personnel Executive, DSC, AM

Mr Peter Sharp, First Assistant Secretary, Defence Personnel Executive

Defence Housing Authority**Department of Veterans' Affairs****Portfolio overview****Corporate and general matters**

Outcome 1: Eligible persons (including veterans, serving and former defence force members, war widows and widowers, certain Australian Federal Police personnel with overseas service) and their dependents have access to appropriate income support and compensation in recognition of the effects of their service

1.1: Means tested income support, pension and allowances

1.2: Compensation pensions, allowances etc

1.3: Veterans' Review Board

1.4: Defence Home Loans Scheme

1.5: Incapacity payments, non-economic lump sums through SRCA

1.6: Administer individual merit reviews of SRCA decisions

1.7: Incapacity payments, non-economic lump sums through MRCA**1.8: Administer individual merit reviews of MRCA decisions**

Mr Mark Sullivan, Secretary

Mr Ed Killesteyn, Deputy President

Mr Ken Douglas, General Manager, Service Delivery

Mr Barry Telford, General Manager, Policy and Development

Mr Paul Pirani, Principal Legal Adviser, Legal Services

Outcome 2: Eligible persons (including veterans, serving and former defence force members, war widows and widowers, certain Australian Federal Police personnel with overseas service) and their dependents have access to health and other care services that promote and maintain self-sufficiency, wellbeing and quality of life

2.1: Arrangement for delivery of services**2.2: Counselling and referral services****2.3: Deliver medical, rehabilitation under SRCA and related legislation****2.4: Deliver medical, rehabilitation under MRCA**

Mr Mark Sullivan, Secretary

Mr Ed Killesteyn, Deputy President

Mr Ken Douglas, General Manager, Service Delivery

Mr Barry Telford, General Manager, Policy and Development

Dr Graeme Killer, Principal Medical Adviser

Outcome 3: The service and sacrifice of the men and women who served Australia and its allies in wars, conflicts and peace operations are acknowledged and commemorated.

3.1: Develop and implement commemorative initiatives**3.2: Maintain, construct and refurbish war graves and post war commemorations****3.3: Coordinate and manage the delivery of commemorative and related activities at Gallipoli**

Mr Mark Sullivan, Secretary

Mr Ed Killesteyn, Deputy President

Ms Kerry Blackburn, General Manager, Commemorations and War Graves

Major General Paul Stevens AO, Director, Office of Australian War Graves

Outcome 4: The veteran and defence and certain Australian Federal Police communities have access to advice and information about benefits, entitlements and services

4.1: Communication, community support to the veteran community and providers, including veterans' local support groups**4.2: Advice and information to members of the defence force community under the SRCA****4.3: Advice and information to members of the defence force community under the MRCA**

Mr Mark Sullivan, Secretary

Mr Ed Killesteyn, Deputy President

Ms Jo Schumann, General Manager, Corporate

Mr Chris Harding, General Manager, Business Integrity

Mr Ken Douglas, General Manager, Service Delivery

Mr Barry Telford, General Manager, Policy and Development

Mr Pablo Carpay, National Manager, Parliamentary and Corporate Affairs

Mr Neil Bayles, Chief Finance Officer, Resources

Mr Bob Hay, Chief Information Officer, Information Management

Outcome 5: Serving and former defence force members and dependents have access to support services provides through joint arrangements between DVA and Defence

5.1: Joint Defence/DVA projects

Mr Mark Sullivan, Secretary

Mr Ed Killesteyn, Deputy President

Ms Jo Schumann, General Manager, Corporate

Mr Chris Harding, General Manager, Business Integrity

Mr Ken Douglas, General Manager, Service Delivery

Mr Barry Telford, General Manager, Policy and Development

Mr Pablo Carpay, National Manager, Parliamentary and Corporate Affairs

Mr Neil Bayles, Chief Finance Officer, Resources

Mr Bob Hay, Chief Information Officer, Information Management

Output group 6: Provision of services to the Parliament, Ministerial services and the development of policy and internal operating regulations—attributed to outcomes 1 to 5

Mr Mark Sullivan, Secretary

Mr Ed Killesteyn, Deputy President

Ms Jo Schumann, General Manager, Corporate

Mr Chris Harding, General Manager, Business Integrity

Mr Ken Douglas, General Manager, Service Delivery

Mr Barry Telford, General Manager, Policy and Development

Mr Paul Pirani, Principal Legal Adviser, Legal Services

Mr Pablo Carpay, National Manager, Parliamentary and Corporate Affairs

Mr Neil Bayles, Chief Finance Officer, Resources

Mr Bob Hay, Chief Information Officer, Information Management

CHAIR (Senator Johnston)—I declare open this meeting of the Senate Foreign Affairs, Defence and Trade Legislation Committee. I welcome Senator Macdonald, representing the Minister for Defence; Air Chief Marshal Angus Houston, Chief of Defence Force; Mr Ric Smith, Secretary of the Department of Defence; and officers of the defence organisation. The committee has before it the particulars of proposed budget expenditure for the year ending 30 June 2007—documents A and B—and the portfolio budget statements for the Defence portfolio. The committee may also examine the annual reports of the departments and agencies appearing before it. The committee will now consider the estimates of the Department of Defence, beginning with the portfolio overview and major corporate issues. We will then move on to outputs, business processes and people.

When written questions on notice are received, the chair will state for the record the name of the senator who submitted the questions. The questions will be forwarded to the department for answer. The committee is due to report to the Senate on 20 June 2006 and has resolved that Thursday, 27 July 2006 is the return date for answers to questions taken on notice at these hearings. Under standing order 26, the committee must take all evidence in public session. This includes answers to questions on notice. Witnesses are reminded that the evidence given to the committee is protected by parliamentary privilege. It is unlawful for anyone to threaten

or disadvantage a witness on account of evidence given to a committee, and such action may be treated by the Senate as a contempt. Giving false or misleading evidence to the committee may constitute a contempt of the Senate. The Senate, by resolution, in 1999 endorsed the following test of relevance of questions at estimates hearings:

Any questions going to the operations or financial positions of the departments and agencies which are seeking funds in the estimates are relevant questions for the purpose of estimates hearings.

The Senate has resolved that there are no areas in connection with the expenditure of public funds where any person has a discretion to withhold details or explanations from the parliament or its committees unless the parliament has expressly provided otherwise. An officer of a department of the Commonwealth or a state shall not be asked to give opinions on matters of policy. He or she shall be given reasonable opportunity to refer questions asked of the officer to superior officers or to a minister. This resolution prohibits only questions asking for opinions on matters of policy, and does not preclude questions asking for explanations of policies or factual questions about when and how policies were adopted.

If a witness objects to answering a question, the witness should state the ground upon which the objection is taken, and the committee will determine whether it will insist on an answer, having regard to the ground which is claimed. Any claim that it would be contrary to the public interest to answer a question must be made by the minister and should be accompanied by a statement setting out the basis for the claim.

[9.06 am]

Department of Defence

CHAIR—Minister, do you have an opening statement?

Senator Sandy Macdonald—As I am sure the committee would be aware, the ADF have a number of pressing operational commitments both at home and abroad, particularly the operation in East Timor. Thus, the Chief of Defence Force, Air Chief Marshal Angus Houston, will make himself available for around two hours at the start of the proceedings on both days. However, he will be called away on both days to deal with the situation in East Timor. The Vice Chief of Defence Force and chief of operations, General Ken Gillespie, and the Deputy Secretary of Strategy, Mr Michael Pezzullo, will be here during the course of the two days, but both are likely to be called away on tasks associated with the East Timor operations. A number of military and civilian staff, particularly from the organisational and international division, will be similarly affected. Chair, I hope that you and your committee will bear with us as the department manages East Timor over the next few days. As always, my officials will seek to answer questions as fully as they can or to take the questions on notice.

CHAIR—Air Chief Marshal, do you wish to make an opening statement?

Air Chief Marshal Houston—I am delighted to be back here, but we are very busy. As the minister said, the Vice Chief of Defence Force could be called away at any time. I regret that he will be unable to be with us this morning, because there are a series of matters that he has to take care of with regard to East Timor. I would like to make an opening statement concerning some of the defence issues that have been prominent in the public arena lately. I will start with the ADF operational tempo, and I will talk initially about Operation Astute, which is our operation in East Timor—or Timor Leste.

I am immensely proud of how the Australian Defence Force has reacted and performed since we were directed by the Prime Minister to begin contingency planning for a possible Timor Leste assistance mission. Once we were invited by the government of Timor Leste to intervene, the deployment of our troops under Operation Astute occurred very quickly thanks to the high state of readiness we maintain, our decision to predeploy some key defence assets and our preparation of force elements that would be required for evacuation and stabilisation operations. I can assure you that it is no easy task to deploy this number of people and this amount of equipment, let alone as quickly as we were able to achieve it, but I am very pleased to say it was a first-class deployment. Indeed, the stabilisation battalion group was deployed in just over two days following a government decision last Thursday night. All combat elements were on the ground in Timor Leste by close of business on Saturday.

The ADF continues to provide a significant presence on the streets of Dili, characterised by an intensive patrolling program and the protection of vital assets. We have separated the army and the police, and they are no longer using lethal force against each other. The killing that we saw only one week ago has stopped. This disengagement has seen the chain of violence subside substantially. Brigadier Slater has established critical liaison and communication teams, and they are currently communicating with these groups. There has also been a noticeable reduction in communal and gang activity, although it continued yesterday at a higher level than it did the day before. I think Brigadier Slater mentioned that yesterday was a bad day; the day before had been a good day. We anticipate that this sort of organised gang violence will continue for some time to come.

Additionally, we are working very closely with the government of Timor Leste and non-government aid agencies to help the innocent victims of this crisis. However, I must stress that the most effective way the ADF can help is to quickly stabilise the situation, and this remains our first priority. We must maintain the disengagement between the parties that effectively were at war only a week ago. I am very pleased with the performance of the ADF on the ground in and around Dili. They are working very hard for the people of Timor Leste and there has been a dramatic turnaround in the situation since we arrived.

Moving on to concurrency: since this deployment began, there have been many questions about whether the ADF is overstretched. Over the last six weeks we have responded to crises in the Solomon Islands and Timor, and we have also changed over our task groups in Afghanistan and Iraq. This amounts to over 4,000 individual deployments or redeployments. I think it has all been done in a very smooth and effective way. I think you should take note of that as a great demonstration of how we do business.

I would like to reiterate here this morning that the ADF is at high operational tempo but is not overstretched. We can sustain our current deployed force, and we do have the capacity for further deployments. We have an additional battalion at very short notice which is undergoing predeployment training. We also have two company groups with about 140 troops each on high readiness should they be required. I cannot provide much more detail about our state of readiness on the public record, because obviously it is highly classified information and could be useful to those who work against our interests—but I am able to provide you with a private briefing, if required, and, of course, with the concurrence of Minister Nelson.

More generally, let me just say that the ADF takes considerable steps to ensure that each deployment is within the capability of our forces, is sustainable for the expected duration of the deployment and leaves the ADF appropriately postured to meet our domestic and regional defence and security responsibilities. We maintain a robust preparedness management system that is scrutinised closely by the Chiefs of Service Committee and the Defence Committee. The output from this preparedness management system allows me to provide government with robust advice on matters to do with military capability options, concurrency implications, sustainability and the ADF posture to meet short notice or longer term contingencies. Yes, we are very busy at the moment. We have almost 4,000 personnel deployed overseas and in our maritime protection zone, but I am comfortable with both the capacity and the availability of our force.

I will now briefly highlight a number of other important developments in regard to our operations in the Solomon Islands, Afghanistan and Iraq. We have now scaled back our commitment to the Solomon Islands. Since deploying 400 personnel on Operation Anode in April, excellent progress was made in restoring law and order. After reviewing the security situation and consulting with the Solomon Islands government and our regional military partners, our commitment has been scaled back to about 140 personnel.

In regard to Operation Slipper, our contribution to the international fight against terrorism in Afghanistan, 240 personnel will deploy in July as part of a reconstruction task force. They will work on reconstruction and community based projects. Our two Chinook helicopters and supporting personnel will remain in Afghanistan, conducting airlift support and aeromedical evacuations until at least April next year to support the reconstruction task force and the Netherlands led provincial reconstruction team. We will also maintain our special forces task group until at least September this year.

In terms of Operation Catalyst, our contribution to the rehabilitation and reconstruction of Iraq, Brigadier Michael Moon has taken over as Commander of the Australian Forces in the Middle East area of operations. He takes over from Brigadier Paul Simon, who held the appointment since November 2005 and who did a wonderful job in what has been a very difficult and demanding rotation. Our third Al Muthanna Task Group has deployed to Iraq on Operation Catalyst for six months and will continue the fine work of the first two rotations in providing a secure environment for the Japanese engineers and training the Iraqi army. Our remaining contribution to this operation—a SECDET, a Royal Australian Navy frigate and Royal Australian Air Force PC3 Orions and C130s—remain unchanged.

On operation last month we tragically lost Private Jake Kovko whilst he was serving in Iraq as a member of our security detachment. We are all saddened by the loss of this fine young soldier and our deepest sympathy goes to the Kovko family. The circumstances of Jake's death are the subject of a board of inquiry which I have convened. The board of inquiry will be an open and transparent process. The proceedings will be open to the public unless privacy or security matters dictate otherwise. The board members are very experienced and they have full scope under the terms of reference to determine the facts of this tragic matter.

I am not going to go into the specific details of how we managed Private Kovko's death. Firstly, it is a matter for the board of inquiry to investigate and determine the facts of what occurred. I do not want to say anything that will jeopardise this important process. Secondly,

further speculation on the cause of his death or how it was handled only adds to the pain and distress that Private Kovko's family have already endured. The mistake in bringing Jake's body home and the loss of a draft report into this repatriation error has been a very distressing situation for everyone involved, but most especially for Jake's family. I have personally apologised on behalf of the ADF to Jake's wife, Shelley, and the rest of the Kovko family for the distress these errors have caused them. As Chief of the Defence Force I am ultimately responsible for these errors. My focus now is on supporting the Kovko family and correcting our shortcomings.

Brigadier Cosson's report into the repatriation of Private Kovko is being finalised and will be provided to the board of inquiry. In the meantime, I have directed immediate changes to our repatriation process. Defence will endeavour to make sure that the bodies of ADF personnel will be repatriated on an Australian aircraft. A minimum of two Australian personnel will also travel with the body at all times. We will also avoid where possible the use of non-military mortuaries in the Middle East. Of course, much depends on the precise circumstances of each situation, including the location and the number of casualties involved. The key principle, as always, is that Defence people will handle repatriation matters with the utmost respect for their fallen mates and with concern for their families.

I would now like to update you on the progress we have made on the implementation of the military justice inquiry recommendations. Last year I stated I would personally drive the implementation of enhancements to our military justice system. I am pleased to report that, in the first six months of the two-year implementation period, significant achievements have been made in reforming this system to deliver impartial, rigorous and fair outcomes through enhanced oversight, greater transparency and improved timeliness.

I will now take you briefly through some of these enhancements. Firstly, I am pleased to report the backlog of redress of grievance cases has been cleared. There is no longer pressure on our complaints resolution system. Further, we have established the Defence Fairness and Resolution Branch as the central management body outside of normal line management for managing all complaints and grievances. The initial phases of the triservice police investigative capability audit, which will establish the best means for developing our investigative capability, have been completed. To assist with this audit a senior retired AFP officer was seconded, and the audit will inform a decision on the requirement for the ongoing secondment of a permanent AFP officer. Additionally, to head the new triservice investigative unit, which will be formed following this audit, I have appointed Colonel Tim Grutzner as the initial Provost Marshal ADF. That took place just very recently, at the beginning of May.

Effective immediately, because we now have the provost marshal in place, dedicated service police investigators will be deployed to Iraq, Afghanistan, the Solomon Islands and Timor Leste. These investigators will be responsible to me through the Provost Marshal ADF. This further assures that the ADF military justice system delivers impartial, rigorous and fair outcomes both at home and, importantly, on deployed operations. I might add they are all in place at this stage.

We have also enhanced the impartiality of our service tribunal system by establishing a number of new positions, including Chief Judge Advocate and Registrar of Military Justice, both as statutory appointments; the Director of Military Prosecutions, at the one-star rank and

also as a statutory appointment; and the Director of Defence Counsel Services, which has already been filled. We have completed a review into the Defence Whistleblowers Scheme, and the operation of this scheme will be reported in the Defence annual report. Additionally, reporting of wrongdoing was included in the 2004-05 Defence annual report and will continue to appear each year.

The defence inquiry regulations have been amended to incorporate new provisions with respect to the representation of affected persons at board of inquiry. This ensures that all persons who appear before an inquiry are treated fairly. Additionally, interim arrangements are now in place by which the CDF, the secretary and CDF operating jointly, the service chiefs or other authorised officers can commission a board of inquiry which, in order to ensure independence, impartiality and transparency, will be presided over by a civilian. These inquiries, to be known as a CDF commission of inquiry, will be mandatory for all suicides and deaths in service. The Inspector-General ADF has been established as a statutory position to provide independent oversight of the military justice system.

The administration of ADF cadets has been enhanced through the engagement of a child human rights expert and the provision of additional resources. We have conducted the initial phase of the audit of ADF schools and training establishments. I expect this inquiry will establish a baseline from which to drive change in the ADF's training culture.

Finally, we have submitted drafting instructions to the Office of Parliamentary Counsel in order to create the Australian Military Court. We are aiming to have this legislation included in Defence's submission for the 2006 sittings of parliament. Though work remains to be done, considerable progress has been made in enhancing our military justice system. I am monitoring our progress on a monthly basis, and of course the initial six-monthly progress report was provided to you in April. I remain strongly committed to a fair and just military work environment, and I will continue to personally drive the required enhancements. Thank you for allowing me the time to make this statement; I am now ready to take questions.

CHAIR—Mr Smith, do you have an opening statement?

Mr Smith—No, not on this occasion.

Senator MARK BISHOP—I also welcome the Chief of the Australian Defence Force and the secretary of the department. I want to make a couple of preliminary comments. Firstly, I want to wish the Australian defence forces all the best in their most recent deployment up to East Timor. From reading the press and hearing your comments this morning, Chief, all appears to be going well. So on behalf of the opposition I will just confirm the comments made by the Leader of the Opposition in consultation last week after the Prime Minister made his announcement. It is a very difficult task that you have been asked to engage in, and we wish you, your officers and your men all success and an early return home.

In that context, it does raise serious considerations for government and opposition as to time, cost, sovereignty, our apparently increasing responsibility in this part of the world and the increasing prominence of the use of our military forces in adjacent areas. They are matters that I am sure the government is considering, and you should assume that the opposition is giving a lot of thought to those issues into the future. I repeat, as I said at the outset, Chief, that we wish you well and we wish your men and women well. I would also like to thank you

for those introductory remarks. We understand that you are very busy. I have given the secretary of the committee an outline of the areas that we wish to pursue over the next two days. That has been somewhat complicated by the clear demand for your presence elsewhere, so there will be a little bit of latitude in the program.

The first thing I want to turn to is the issue of force preparedness, force readiness and the ability to deploy at short notice. You made some very strong comments in your introductory remarks. As I heard you, you said essentially that we have got significant amounts of troops involved in deployment overseas, that you are in the process of preparing an additional battalion and two companies to have their state of readiness improved or increased, and that if additional demands of a like nature were made upon our forces at relatively short notice you are confident that your people would be capable of meeting the demand of government. Is that a fair summary of your comments?

Air Chief Marshal Houston—Yes. first of all can I say thank you very much for the support of the opposition. I think we have been very fortunate to have the total support of the Australian people, and bipartisan support from the Parliament of Australia is deeply appreciated by me, the chiefs and indeed everybody who is in the ADF and the defence organisation at the moment. So, a very sincere thank you for that.

In terms of our posture at the moment, yes, we are busy. Our people like to be busy. We train for operations and when I go out, when the chiefs go out, and engage our people, they are always delighted by the fact that they are going on a deployment. That is certainly the feedback that I have been getting through the chain of command at the moment. In terms of our posture, the service that is most affected by everything we are doing at the moment is the Army. As I mentioned to you, we have two more companies on very high readiness. Another company is going into Timor today—a New Zealand company group are being deployed into Dili today. That is not a reinforcement; that is part of the deployment. They had a later decision in terms of moving into the area of operations.

We have two companies on short notice. We have a battalion that is also now on high readiness. As soon as we deploy, we reconstitute and raise another battalion to replace the ready battalion group. I think you would be aware that we always maintain one battalion ready to go for credible contingencies around the region. So at the moment we have a posture where we are doing all these operations, but we also have the ready battalion group raised on the appropriate notice to be able to respond to whatever else might pop up in our neighbourhood at short notice. Our posture is exactly what is required by longstanding strategic guidance.

Senator MARK BISHOP—Could you tell me a bit of detail. Was 1RAR the unit that was tasked with being on a high state of readiness for deployment at the time of the recent unrest in the Solomon Islands? Was that 1RAR?

Air Chief Marshal Houston—In terms of what?

Senator MARK BISHOP—In terms of being on a high state of readiness for deployment. When we had to put troops into the Solomon Islands, was it 1RAR?

Air Chief Marshal Houston—In responding to the Solomon Islands, we had companies from different battalions. I would prefer not to get into a discussion of individual numbers and numbered battalions because we do not normally talk about those details.

Senator MARK BISHOP—I was not going to ask you about the numbers involved. What I want to explore is this: it is my understanding that 1RAR was tasked with being on a high state of readiness for deployment at that time, back in April, to the Solomons, but we found it necessary to deploy a company from 3RAR and not a second company from 1RAR. If the 1st Battalion was tasked with being on a high state of readiness, why did we feel it necessary to draw down from 3RAR, not just another company from 1RAR?

Air Chief Marshal Houston—We deployed a ready company. All the companies that were deployed were part of the 3rd Brigade, the operational deployment force. We mix and match as required.

Senator MARK BISHOP—But why not from 1RAR?

Air Chief Marshal Houston—Essentially, the task in the Solomon Islands was to send two companies. We now have one company there, and we have draw down the other company.

Senator MARK BISHOP—I understand that. You put two companies in a relatively short period of time into the Solomons—one company from 1RAR and one company from 3RAR. It was my understanding that in relation to 1RAR all companies were going to be tasked with a high state of readiness. Was there a sufficient state of readiness in 1RAR?

Air Chief Marshal Houston—Absolutely.

Senator MARK BISHOP—Why was it necessary then to—

Air Chief Marshal Houston—We made a judgment to deploy because of what was going on. We have a number of options available from a brigade. We put the force in in a particular way depending on the circumstances that prevail at the time. I do not think we have to go into detail as to why we did this and why we did that. Let me just tell you that at the time we could meet all of our preparedness requirements—and indeed we can still meet all of our preparedness requirements. We have a ready company group—and we have only one ready company group on very short notice to move. What we required for the Solomon Islands was two company groups. Okay?

Senator MARK BISHOP—Yes.

Air Chief Marshal Houston—So we deployed the ready company group, and then we took the next most ready company group from the formation. That is just the way we do business.

Senator MARK BISHOP—But there were not two ready company groups in the first that could be deployed within two days—you had to take them from the third.

Air Chief Marshal Houston—What we did was to take two high-readiness company groups. We have a requirement to have only one on very high readiness but we deployed two, and we deployed the best two to meet that requirement.

Senator MARK BISHOP—So the ready company in 3RAR was at the same level of readiness as the company in 1RAR?

Air Chief Marshal Houston—Our infantry is at different states of readiness, depending on what they have been up to. For example, if we have a company that has just returned from a deployment, they clearly would not have been the company that we would use in the circumstances that arose in the Solomon Islands. We pick a suitable company to go and do the business. Indeed, that is what we did. There is nothing sinister about this. We made a military decision to send the two best companies to do the job, and, as you know, they did it very well. They were both in there in very short order. I think it demonstrates yet again our ability to deploy at short notice to meet the government's requirements.

Senator MARK BISHOP—Okay. So you took two companies in a high state of readiness from two separate battalions and deployed them within a couple of days of each other. You say that that was an operational call and that nothing sinister can be read into it. I accept that. If the second company from 3RAR had not been at a sufficient state of readiness, would there have been a second company available from 1RAR to have been deployed within two days?

Air Chief Marshal Houston—We had multiple options. We made a decision to deploy the company that was on the short leash—we always have one company on a short leash—and then we picked another company that was suitably prepared, and it worked well.

Senator MARK BISHOP—All right. So how many companies do we now have in the Solomon Islands? Just the one?

Air Chief Marshal Houston—What we have got in the Solomon Islands is one Australian company, but we also have a platoon from New Zealand and a platoon from Fiji, so we have a force over there for RAMSI of about 200 or so troops.

Senator MARK BISHOP—With only one company from RAR still in the Solomons, do you have the ability now to deploy an additional company or additional companies from 1RAR if another hotspot should emerge?

Air Chief Marshal Houston—I have got multiple options.

Senator MARK BISHOP—In terms of company deployment?

Air Chief Marshal Houston—Absolutely.

Senator MARK BISHOP—How many companies would you be able to deploy?

Air Chief Marshal Houston—I prefer not to get into the precise detail of that. I am very happy to organise a private briefing for you, but let me tell you that it is not one and it is not two; it is a lot more than that. Okay?

Senator MARK BISHOP—I understand the point. We might—

Air Chief Marshal Houston—We have it covered. We can meet what is required by longstanding strategic guidance that has been in place for 20 years.

Senator MARK BISHOP—All right. We might take you up on that private briefing in due course.

Air Chief Marshal Houston—Yes, I would like to do that. I think there is a lot out in the media which is ill-informed. We are not in the situation that is portrayed by some commentators in the media.

Senator MARK BISHOP—All right. What is meant by the term ‘agreed vacancies’, in military jargon, in levels of personnel in companies or platoons?

Air Chief Marshal Houston—I am not sure what you are referring to.

Senator MARK BISHOP—Are there currently significant vacancies—it has been described to me as ‘agreed vacancies’—within 1RAR rifle companies and technical support troops which the unit has been prepared to sustain until the current time?

Air Chief Marshal Houston—I am still not sure what you mean.

Senator MARK BISHOP—Are they at full strength?

Air Chief Marshal Houston—Let me say this: all of the companies that we have deployed recently are at a strength that enables them to perform their task in a very robust way.

Senator MARK BISHOP—Is that level of strength a 95 per cent, an 80 per cent or a 75 per cent staffing level?

Air Chief Marshal Houston—In terms of effect, what we are talking about is a company that can deliver 100 per cent of its capability effect. Essentially, you are asking whether we have every last slot filled. Essentially, we have deployed in sufficient strength to deliver the effect. Do we have the exactly the establishment? Some companies have probably gone with perhaps a few more than the establishment and another couple of companies might have gone with a few less. A lot depends. During the process of preparation, people sometimes get injured. Some people will get sick. In the main, what we are talking about is a company that is effectively full strength. I put that qualification on it because sometimes people are not able to go for entirely sensible reasons. They may get the flu, a cold or an injury.

Senator MARK BISHOP—But you are assuring the committee that the companies that were deployed to the Solomon Islands and the recent deployment in the last fortnight up to East Timor are if not at strength then at sufficient strength to carry out their required duties in the most robust fashion?

Air Chief Marshal Houston—They are completely capable of performing the task that I have given them.

Senator MARK BISHOP—On 24 May Minister Nelson announced a draw-down of troop numbers in the Solomon Islands, as you are aware. I presume that was consequent upon a recommendation from you.

Air Chief Marshal Houston—As is always the case in these circumstances, I will provide advice and government will consider the advice and do their own review. It is a whole-of-government process. The government then makes a decision which, in this particular case, was announced by the Minister for Defence.

Senator MARK BISHOP—Was it your advice to draw down troop numbers in the Solomon Islands as Minister Nelson advised on 24 May?

Air Chief Marshal Houston—Absolutely. My advice was that the circumstances in the Solomon Islands were such that we could draw down to the size we have at the moment. But I might add that that advice was supported right across the whole of government. It was not just me who was providing that advice. Similar assessments were coming from other parts of government.

Senator MARK BISHOP—Do you mean intelligence agencies?

Air Chief Marshal Houston—I am talking more about the Department of Foreign Affairs and Trade. They obviously have a major role to play in these circumstances. Indeed, input from intelligence agencies supports certainly the assessment that I will make and the assessments that government will make.

Senator MARK BISHOP—But the risk analysis that you did on behalf of the ADF, in terms of the number of personnel and the number of companies that should be maintained at that time in the Solomon Islands, led you to recommend to the government that it was appropriate to draw down to one company?

Air Chief Marshal Houston—Absolutely. I am completely comfortable with the level of force that we have in the Solomon Islands at the moment. What we effectively have is a company group, plus two platoons. It is a reasonable presence for the circumstances we have in the Solomon Islands at the moment.

Senator MARK BISHOP—You would not have had occasion, I take it, since that time to revisit your thinking in terms of company deployment numbers in the Solomons?

Air Chief Marshal Houston—No. I absolutely believe that we have the right level of support there for the RAMSI arrangements, which of course is an assistance mission that is primarily based around a very robust policing capability. I consider the issues in the Solomon Islands to be primarily of a law and order nature and we are there to provide the back-up when things go slightly wrong. I think that 200 soldiers is about right.

Senator MARK BISHOP—I accept that. Are you now giving consideration to a further draw-down of the company and/or platoons that remain in the Solomons? Has the situation stabilised to such a level that the policing side of things is now dominant and can be conducted better by them as opposed to having 200 fully-armed soldiers there?

Air Chief Marshal Houston—I would expect the level of Army presence to stay about the same, certainly from an Australian point of view, for some time to come. My expectation is that we in the ADF will have to provide a company group for the foreseeable future.

Senator MARK BISHOP—You think that it will be an ongoing task to maintain at least company level there for a significant amount of time into the future?

Air Chief Marshal Houston—I think we should see how it goes. They have a new government. The government is still bedding itself down. My expectation is that we will be providing that capability for several weeks yet—probably a few months.

Senator MARK BISHOP—Is the period of deployment there for four months or six months?

Air Chief Marshal Houston—For each company?

Senator MARK BISHOP—Yes.

Air Chief Marshal Houston—It is usually around six months.

Senator MARK BISHOP—You made some concerning comments about the ongoing level of communal and gang violence activity in East Timor. It went down a few days ago and re-emerged at unacceptably high levels yesterday—that is my phrase not yours, but it is of serious concern. What time frame are we committed to to remain in East Timor? Is it for as long as the job takes or is it for four months, six months or 12 months?

Air Chief Marshal Houston—There has been a fair bit of discussion on that, I note, in the media. Our planning is on the basis of a six-months deployment. However, I would hope that the level of force we have got there at the moment can gradually reduce from where we are at the moment to something less as the situation stabilises. Right now we have an Australian battalion group. The New Zealanders are going in with a company today. The Malaysians are in there currently with 230-odd troops. Their supply ship comes in on Friday; that will mean more troops and more mobility. We have the Portuguese coming in with a company a little bit later on. So, in effect, what we are going to have on the ground is something just under two battalions worth in and around Dili. My hope is that, as things stabilise, we can adjust the force downwards at some time in the future. But I am not focused on that at the moment.

Senator MARK BISHOP—Are the major areas that require troop attention, by us and the other countries you have mentioned, in Dili or in Dili plus out towards the Indonesian border and up in the hills as well?

Air Chief Marshal Houston—In my view the vital ground is Dili. If we go back just one week, the objectives that we had were to break the cycle of violence. The characteristics of the violence at that time, last Wednesday, were that we had people in the streets, armed police elements, armed army elements, having a go at each other. Indeed, I think last Wednesday we had 10 people killed on the streets of Dili. Our job was to go in and break that cycle of violence. We achieved that almost instantaneously. What we have seen since then is some sort of organised rioting, organised chaos, on the streets.

Senator MARK BISHOP—Is it criminal or political?

Air Chief Marshal Houston—All I will say is it is organised, and there are certainly opportunistic elements within it.

Senator MARK BISHOP—But is it generally youths or louts taking advantage to enrich themselves or—because you deliberately used the word ‘organised’—is it more politically inspired or politically motivated violence?

Air Chief Marshal Houston—I think there are some gangs out there and I think those gangs are being organised. I think there are also criminals who are exploiting the circumstances to pursue petty crime. But you will note, in terms of the people that are on the streets, that we have seen one or two firearms but in the main these people are armed with sticks, stones, sometimes machetes and some sort of home-made sword. Certainly we saw fewer machetes yesterday than we did at the beginning of the week because our people have been taking the machetes off the people. As you know, we have disarmed a lot of people. We have got over 400 weapons that we have taken off the people that have been on the streets. If

we find somebody with a weapon, we will detain them straightaway, take the arms off them and put them into detection.

Senator MARK BISHOP—Thank you for that. I understand that looting and theft and some criminal activity occurs in situations where there is a loss of law and order. I accept that. It is reprehensible, and you or other authorities will attend to that as a matter of urgency. But that is not my question. You used the word ‘organised’ and that means something to me. My question is: on the advice you have received, is that organisation politically motivated for a particular purpose? And is that political motivation from inside the country or directed or controlled from outside the country?

Air Chief Marshal Angus Houston—The only comment I will make is that I do not believe that there is any external influence on what is going on in the streets of Dili. I would like to leave the discussion at that, if I may.

Senator HOGG—Can I just ask a question on that. Are these the residual elements that were associated with TNI when they were there and caused disruption around the time of independence or post independence?

Air Chief Marshal Angus Houston—The situation—

Senator HOGG—That is not a direct link, in that sense?

Air Chief Marshal Angus Houston—Let me put it this way: the situation on the streets of Dili is a very complex set of circumstances. We have east versus west, we have lots of different factions, we have lots of different gangs and we have criminals. In the current environment some elements are using gangs of youths to pursue particular objectives. There are lots of different elements of this. All I will say is that it is very complex and it is something that we are countering.

Senator MARK BISHOP—Is the deployment into East Timor classified as warlike service?

Air Chief Marshal Angus Houston—The minister has not made a determination at this time. That is clearly something that has to be done, but he has not made a decision yet.

Senator MARK BISHOP—Is that a job for the Minister for Defence?

Air Chief Marshal Angus Houston—What normally happens in these circumstances is that we give the minister advice on the nature of service. The minister considers the advice and makes a decision on the nature of service. That decision then comes back to the department and we provide the minister assisting the minister with the precise advice on the package that makes up the conditions of service.

Senator MARK BISHOP—I remember having similar types of discussions in another portfolio over the last three, four or five years. The point was always made to me by the responsible minister, his agent at that time or, indeed, your predecessor Dr Costigan—sorry, General Cosgrove—

Air Chief Marshal Angus Houston—I must say that I see why you get confused. He does look like a judge sometimes!

Senator MARK BISHOP—I would not have said that! They repeatedly made the point to me that the military people desired to have the classification of service determined prior to troops being deployed overseas so that they, their families and those who might have to make claims in due course knew at the outset what the circumstances were. Has the practice changed? That point was repeatedly made to me.

Air Chief Marshal Angus Houston—No, the practice has not changed but can I remind you that the government made the decision to deploy the main body—in other words, the ready battalion group—on Thursday evening of last week. We have had Friday, Monday and Tuesday and it is now Wednesday, so we are in the fourth working day after a government decision to deploy a very large force. Normally we have much more time before a deployment to do this sort of work. I think the decision on this will be made shortly.

Senator MARK BISHOP—Whilst the minister has the power to make the call, it is generally done on your recommendation. I take it, from the scenes we have seen on the TV, that in your mind you would regard this as warlike service and that it could appropriately be so classified?

Air Chief Marshal Houston—I do not want to go into that in a discussion with this committee. This is clearly a matter for my minister—for government. I have provided advice on the basis of the sort of methodology we use to determine what the nature of service is. It might be that the advice I have provided does not satisfy my minister so it would be inappropriate of me to say what that advice was.

Senator HOGG—When did you provide the advice? That is not asking what the advice is.

Air Chief Marshal Houston—As I said, this is only the fourth working day—mind you, we worked through the weekend. I cannot remember when I signed off on it.

Senator HOGG—Yesterday? A couple of days ago?

Air Chief Marshal Houston—In the last day or two.

Senator HOGG—From what you have said, I understand that there are other nations involved. Is there anyone in command of the various nations operating there or is each nation in charge of its own force? Is some sort of UN operation going to emerge?

Air Chief Marshal Houston—It is not a UN operation. The basis for the stabilisation force was established at the request of the government of Timor Leste, which invited us to come in. They also invited three other countries: Portugal, New Zealand and Malaysia. All countries have responded. We felt that there was a need to come up with more robust arrangements to cover what we might have to do, so General Gillespie led a delegation up there. It departed Thursday last week and came back on Friday. He was able to negotiate what I will call an arrangement with the government of Timor Leste. Simply put, the arrangement the Prime Minister spoke about, I think, late last week in the parliament—maybe it was Monday; I have lost track of the days—was signed off by President Gusmao, Prime Minister Alkatiri and the President of the parliament. We believe that provides a suitable basis for what we have to do. It also gives Brigadier Slater sufficient power to complete his stabilisation mission.

Senator HOGG—I understand that, and that is in respect of the Australian forces. But my question goes to the other forces that are there as well. Is there someone who has assumed control, responsibility or leadership over the other three nations that are there as well? Is there a joint task force commander, in effect?

Air Chief Marshal Houston—At the moment we have a combined task force. The New Zealanders are under our operational control. They placed their forces under Brigadier Slater, as is the normal practice when we do business with New Zealand. It always works wonderfully well.

Senator HOGG—They are subject to our rules of engagement?

Air Chief Marshal Houston—The New Zealanders will have their own national caveats. We are in coalition in a number of different coalitions around the world at the moment. We have our own rules of engagement but we have rules of engagement that are consistent and workable with the rules of engagement of those that we are working with.

Senator HOGG—What about the Portuguese and the Malaysians?

Air Chief Marshal Houston—The Portuguese have not arrived yet. We need to firm up those arrangements. Bear in mind that they are bringing in paramilitary elements—military police, if you like; the European gendarme.

Senator MARK BISHOP—So they are not regular army?

Air Chief Marshal Houston—They are not regular army or regular police; they are about halfway between.

Senator MARK BISHOP—And the Malaysians?

Air Chief Marshal Houston—The Malaysians are there with regular army forces. I have spoken with my counterpart and, essentially, they are under our operational control but they are under Malaysian national command. The same thing applies to the New Zealanders—they are under New Zealand national command but our operational control. They are the arrangements for the countries that are deployed there at the moment. All tasking is closely coordinated by Brigadier Slater and, indeed, we have a New Zealand element that has been there for a while. They are doing tasks basically given to them by Brigadier Slater, and the Malaysians are doing exactly the same thing. That is essentially what operational control means—controlling the tasking so that everything is coordinated.

Senator MARK BISHOP—What is the current balance of the force? How many infantry troops to how many aviation and related personnel to how many logistics people? Do you have those numbers?

Air Chief Marshal Houston—Yes. It is essentially a battalion group which is built around a commando company and infantry companies. We have five Australian companies on the ground. We will also have a New Zealand company and, at the moment, two Malaysian companies. So we are talking about eight companies as we see it at close of business the day after the New Zealand company has gone in. In terms of helicopters, we have eight Black Hawks. We have a large number of armoured personnel carriers and a large number of vehicles. We have something that is pretty close to the sort of battalion group that we have

responding to these sorts of circumstances in our region. It is pretty typical in size and structure for this sort of mission.

Senator MARK BISHOP—How many companies do we have overall? We have five in East Timor and one in the Solomons. How many do we have in Iraq and Afghanistan?

Air Chief Marshal Houston—We have the Al Muthanna task force in Iraq, we have a company providing security in Baghdad and we have a task force in Afghanistan.

Senator MARK BISHOP—So we have seven companies and two task forces?

Air Chief Marshal Houston—What we have in Al Muthanna is essentially a battle group. I would not want to characterise it as a battalion or anything like that, but it is a large battle group. We have a company in Baghdad and we have a special forces task group in Afghanistan—and, again, that is a specific structure to meet the task. This is why I am a little sensitive about getting into a discussion about companies and battalions. It depends on the mission. We have great flexibility now, and if I basically ask the Chief of Army to prepare a force for a particular job, he will look at the task, he will look at what he has got and he will basically put together the force elements to give us the capability to give us the desired effect.

Without giving too much away, in particular circumstances we might want to up the firepower for a particular element, or for another element we might want more protected mobility because there is a particular threat that we have to deal with. All I am saying is that it is not useful to get into a discussion about how many companies you have got where, because companies are ideal for the problem we have got in Dili but they are not ideal for what we might have to do in the Al Muthanna region of southern Iraq.

Senator MARK BISHOP—Do we have a hospital ship in the harbour up there?

Air Chief Marshal Houston—We have got a great ship up there at the moment and it has got a hospital aboard, yes. That is the *Kanimbla*.

Senator MARK BISHOP—Do you anticipate that you will require additional services, in terms of a location onshore as opposed to the level of services that could be provided by the *Kanimbla*?

Air Chief Marshal Houston—We have got a very adequate capability in Dili, provided primarily at this time by the ship. We are an hour and a half's flying time by aeromedical evacuation C130, or indeed a civilian aeromedical capability, from Darwin.

Senator HOGG—On the first occasion that we had reasonable numbers of forces in East Timor we used the services of a hired Incat to move a lot of supplies and troops. You said it is looking like a six-month engagement at this stage—

Air Chief Marshal Houston—No, I did not say that. What I said was that we always worst case the circumstances. We have planned for six months, but it is up to government to determine how long we go for.

Senator HOGG—All right. Will you be using anything such as that to replenish the supplies that are needed by the forces there, or is it too early for that at this stage?

Air Chief Marshal Houston—We have had a look at that sort of capability and we have talked to the people who can provide it. For a number of reasons we have decided that we will

not persist with that capability. These circumstances are different from 1999, and we can sustain the force with the plans that we have put in place. Of course, one of the things we will do is transition to civilian contractors as soon as we can.

Senator MARK BISHOP—Is the rotation policy for aviation personnel and other support elements the same as for the infantry—around the six-months mark?

Air Chief Marshal Houston—Again, we tend to try to be as flexible as we can in these circumstances. One of the things with air crew is that you need to have particular tasks that they do and sometimes, because of the nature of the work and the sorts of skills they have to maintain, we will adjust the deployment period to a more practical set of arrangements. Often that means that the air crew will only go for, say, four months before they rotate out. It all depends on the circumstances. If you look around where we have got aviators deployed at the moment, we do not have a particular standard for air crew. Some of them rotate at four months; others rotate at six months. It just depends on the capability and the circumstances.

Senator MARK BISHOP—Just to finish this discussion on East Timor, if a problem of a similar scale to the current problem we have in East Timor arose and we were required to deploy the best part of 1,500 or 2,000 troops in a relatively short period of time, are we capable of doing that in the same time frame in which the Prime Minister desired action in the current case?

Air Chief Marshal Houston—We will be able to provide a battalion group, which is what we are talking about in Dili, at a readiness level that meets strategic guidance. That is all I would like to say about that. In other words, yes.

Senator HOGG—That is a long way of saying yes!

Air Chief Marshal Houston—I want to just define it because you sort of started expanding it out a bit. What we have deployed there at the moment is a battalion group. We could deploy a battalion group in the future on the basis of maintaining a level of readiness that meets strategic guidance. The reason I say that is because you will never see a battalion group deployed as fast as this one was. This was deployed in essentially just over two days. That is way inside strategic guidance. So I am not going to sign up for that again. We were able to achieve that because the government made a decision two weeks ago to authorise me to do the necessary preparations against a contingency that things might go wrong in Dili and we might get a request to go in and help. So I need to qualify it. We will be able to meet government's strategic requirements, which is reflected in our readiness notice, with a battalion group.

Senator MARK BISHOP—I want to turn now to Iraq and the Al Muthanna task force. I have some questions about that. At the last round of estimates I asked for some advice on the mission of the Al Muthanna Task Group and the army training team in Iraq. You took that on notice and provided a response in due course. With the new deployment or rotation in Al Muthanna, has the mission statement changed at all or is it still as you provided in advice to me in writing?

Air Chief Marshal Houston—No, the Al Muthanna Task Group has just recently or has almost completed its relief in place. We have a completely new team—AMTG3, Al Muthanna Task Group 3. Their mission is the same mission as their predecessors. They need to go in and

provide security for our Japanese friends in Al Muthanna. They also have a training capability and that training capability is slightly smaller than the training capability we deployed last time. That is being used to do training in another part of Iraq—in southern Iraq. They will be doing basic training for the Iraqi army in southern Iraq.

Senator MARK BISHOP—Is Al Muthanna in southern Iraq?

Air Chief Marshal Houston—Yes, it is.

Senator MARK BISHOP—Is that different basic training in the south of a different nature to the training that was done in the first two groups?

Air Chief Marshal Houston—It is very similar to training we did right at the outset. We will be providing around 30 people to do training at a place called Tallil in southern Iraq.

Senator MARK BISHOP—Has the focus of the total group changed significantly or is this additional or different training in the new place only on the margins?

Air Chief Marshal Houston—Perhaps I should go back: the training team with Al Muthanna Task Groups 1 and 2 was primarily aimed at getting the security forces, the army, up to speed in Al Muthanna. They were doing a lot of battalion type training. They were raising the skill level of the soldiers that were in the two battalions that comprised the brigade at Al Muthanna. So it was very much unit type training. Soldiers had completed their basic training and they were then bringing them up to a standard whereby they could do operational security tasks at Al Muthanna. What we will be doing at Tallil is basic training tasks. It is individual training as opposed to unit type training.

Senator MARK BISHOP—Do we have a similar level of focus on the security protection for the Japanese people as we had before?

Air Chief Marshal Houston—Yes. The provision of security for the Japanese will not change at all.

Senator MARK BISHOP—Can you bring us up to date with the level of discussions that either you or the government have had with the Japanese government in terms of ascertaining their deployment plans in southern Iraq once the next rotation completes?

Air Chief Marshal Houston—The Japanese have not made any decision at this stage as to when they will withdraw from Al Muthanna.

Senator MARK BISHOP—What is their current thinking?

Air Chief Marshal Houston—They are still considering their decision.

Senator MARK BISHOP—Until when are they committed?

Air Chief Marshal Houston—They have recently committed to a six-month extension that takes them through towards the end of the year.

Senator MARK BISHOP—Yes—about November.

Air Chief Marshal Houston—We have been involved in discussions with all our coalition partners about transitional arrangements in Al Muthanna, but we have no visibility of the Japanese decision. We await to hear that, hopefully in the next few days.

Senator MARK BISHOP—So they are committed to staying there until towards the end of the year and you are awaiting further advice, which is expected in the next few days, as to their intent past the end of this year?

Air Chief Marshal Houston—Perhaps I could clarify that. They made a decision to do another deployment and that deployment should see them through to the end of the year. I believe they have a mandate to go through towards the end of the year. Our expectation is that at some stage they will make a decision to perhaps withdraw at some stage before that occurs, but we do not have any visibility of when that might be.

Senator MARK BISHOP—There has been some press reporting that, possibly following the eventual withdrawal of the Japanese, Australian soldiers will work alongside Iraqi forces in Project Overwatch. Can you firstly put on the record what Project Overwatch is and any contingency planning that you are able to share with us as to our role if that should come to pass?

Air Chief Marshal Houston—Government has not formally decided to go for circumstances of operational oversight. The conditions under which we continue our presence in Iraq have yet to be formally agreed by government. But my expectation would be that we will do some form of security task that will involve working closely with the people that we have trained in Al Muthanna. There will clearly be a need for mentoring, further training to lift the level of capability amongst those that we have trained and to provide them with support in certain circumstances. It is that sort of general security support and support that would be aimed at lifting their capability to a higher level.

Senator MARK BISHOP—There has been a series of press reports in the last four or five weeks that Iraq's Shia led Interior Ministry is complicit in or has sanctioned sectarian violence and a range of extrajudicial killings of Sunni Arabs. In the light of those press reports—I do not put it any higher than that—to what extent are any future commitments of Australian troops contingent on the ability of the Iraqi government to look after its own security? And is Project Overwatch related to that type of activity?

Senator FERGUSON—I think that is more a question of government policy. I think you are straying outside what you can ask the CDF. It would be a government decision rather than—

Senator MARK BISHOP—Let me rephrase the question. There have been press reports of a range of organised, extrajudicial killings of key people on a sectarian basis in a number of different parts of Iraq. We just had discussion about the improved training of security people in Al Muthanna. My question is: is that improved training of security people in any way attached to this wave of sectarian violence that is reported in the press?

Air Chief Marshal Houston—We have just got a brand new and permanent Iraqi government. A minister for defence and a minister for the interior have not been appointed yet. We are hopeful that we will get a strong Iraqi government, a government for national unity and so forth. In terms of the situation in Al Muthanna, no, that has got nothing to do with that. But, suffice to say, any time we go and work with the Iraqis in a training environment what we are trying to do is not only give them a high level of skill in whatever we are training them in but also imbue them with the right culture and values. We have found

that the Iraqis that we have trained are very comfortable learning about our culture and, in many cases, reflecting our culture. Whether that goes into the long term is really a challenge for the commanders in the new Iraqi army.

Senator MARK BISHOP—The Prime Minister in various ways, on behalf of the government, has made it clear that our presence in Iraq will remain—I think the phrase he used is ‘until the job is done’, or words to that effect. That has a common understanding. In that context, has the commitment that Australian troops will remain in Iraq until the Iraqi government can look after its own security been formalised in any way with the Iraqi government? If so, have any reciprocal undertakings been made by the Iraqi government in that respect?

Air Chief Marshal Houston—The new, permanent, sovereign Iraqi government has just been formed. It has only been active for a matter of days, a couple of weeks, so we have not actually interacted with it on any of this stuff. But, clearly, into the future we need to have suitable arrangements in place with the new Iraqi government because, unlike the last one, it is an elected government, it is a sovereign government and it is a government that we need to have the normal sorts of arrangements with for whatever we do in Iraq.

Senator MARK BISHOP—When the government is bedded down and responsible ministers are appointed to the key posts, it would be the intention of our government to progress those types of negotiations that we are talking about?

Air Chief Marshal Houston—We have armed forces in the country of Iraq. We can only be there if the government of Iraq wants us to be there. So, yes, obviously we have to have a very clear understanding of the conditions under which our forces would remain in Iraq.

Senator MARK BISHOP—I do not know whether this is a question for you, Chief, or the secretary. What is the total cost of Australia’s contribution to Al Muthanna province to date?

Mr Smith—To the task force, do you mean?

Senator MARK BISHOP—I mean the total cost of location of the Al Muthanna Task Group.

Mr Smith—We have some gross figures; I will see if we can disaggregate them.

Mr Veitch—I do not have the figures on the Al Muthanna component itself but I can get those for you this morning some time. The figures I have before me are the total figures for the full deployment.

Senator MARK BISHOP—How do you define full deployment?

Mr Veitch—That is for both components: the Al Muthanna and the wider deployment in Iraq.

Senator MARK BISHOP—Can you give us the figures you have and at a later time make available the disaggregated figures for Al Muthanna?

Mr Veitch—For the total commitment of around 1,400 personnel, there has been an additional \$392.7 million provided in this budget. All up, taken with money provided in prior budgets extending back to 2002-03, the government has provided \$1.635 billion.

Senator MARK BISHOP—That is for the total operation.

Mr Veitch—All operations in Iraq since 2002-03.

Mr Smith—Some of that projects ahead to cover restitution and recovery costs in out years.

Senator MARK BISHOP—The aggregate figure for the last three years is around \$1.6 billion.

Mr Veitch—That covers the period 2002-03 right through to 2008-09.

Mr Smith—For that restitution and recovery work that is foreshadowed.

Senator MARK BISHOP—The restitution and recovery work is minimal, isn't it?

Mr Veitch—It is. Out of that \$1.635 billion, \$71 million is provided in 2007-08 and \$15.6 million in 2008-09. That is to cover the return of forces home, the reconstitution of stores and equipment used on the operation, and repair and maintenance of equipment.

Senator MARK BISHOP—Thank you. Back to you, Chief: there has been some press speculation of late and some comments by the Prime Minister of Great Britain that they will be drawing down their troop levels in Iraq in the immediate future. Have we had any discussions with the British government to ascertain their deployment plans in southern Iraq?

Air Chief Marshal Houston—As you know, our people in Al Muthanna are under the operational control of the British coalition commander in southern Iraq. He is commander of the military district south-east, Commander MND South-East, which includes four provinces; one of those four provinces is obviously Al Muthanna.

We also have people who are embedded in the coalition headquarters, which is a primarily British headquarters. So, yes, we are aware of some of their plans. Of course, we also engage with them in London and, indeed, in Baghdad at the policy level through our policy people and also through our defence attache and our high commissioner. So we have a reasonable understanding of their plans and what they are going to do in south-east Iraq.

Senator MARK BISHOP—Have the British indicated the detail of the planned withdrawal of troop numbers in the south?

Air Chief Marshal Houston—It is true to say we have a good idea of their thinking. I am not sure where they are at in terms of making government announcements about some of the planning that we are privy to. Of course, we are in a very privileged position; we understand what they are planning to do and they consult with us extensively. But we keep all of that confidential until their government announce it officially.

Senator MARK BISHOP—So we are in the loop as to their intent, but you are saying it is not a matter for you to be advising us in a public forum of their intent.

Air Chief Marshal Houston—I would be quite happy, in fact I would be delighted, to give you anything that is on the public record, but I cannot obviously share information that has been given to us in a privileged way.

Senator MARK BISHOP—I understand that. Does it have any impact on our ongoing deployment of people in the task force in southern Iraq—the British withdrawal?

Air Chief Marshal Houston—Well, British plans.

Senator MARK BISHOP—British plans, yes.

Air Chief Marshal Houston—British plans clearly have a direct consequence for us because we are essentially part of the team in southern Iraq, so the answer to that is yes.

Senator MARK BISHOP—Are we doing any planning for increasing our deployment once the British—

Air Chief Marshal Houston—No, not at all. We are working on the basis that the Al Muthanna Task Group, after the Japanese task is complete, would be used to do some other security task in Iraq. In fact, we would not have any need for an increase in numbers, the way we see it. We have talked to the Brits about the support they provide to us. We would expect that support to continue into the future and we would continue to work closely with them, such that we did not need to increase our numbers.

Senator FAULKNER—I have a question arising out of your opening statement, CDF. It is in relation to some instructions you have made on the repatriation of bodies. You said you have instructed that Australian aircraft would be involved.

Air Chief Marshal Houston—Where practicable, yes.

Senator FAULKNER—Do you mean, in that instance, military aircraft or commercial aircraft? Could you make that clear, please.

Air Chief Marshal Houston—Essentially: wherever possible an Australian military aircraft. But in the circumstances we have in the Middle East at the moment we have an aircraft that we have chartered which will eventually be flown by Australian crews. To all intents and purposes it is a state aircraft—we apply for diplomatic clearances for that aircraft and so on—although it is not a permanent aircraft of the Royal Australian Air Force. Because of the speed of that aircraft and the fact it can fly to Australia very quickly with minimal stops, it is a very efficient and effective way of repatriating a body from the Middle East. So that would be one option for body repatriation which I would regard as Australian because it is under charter to us and it is an Australian state aircraft even though it is provided by an international contractor.

Senator FAULKNER—Has a Defence instruction been issued to this effect?

Air Chief Marshal Houston—I put out a directive that this is to be the case, yes. I would quickly add, though, that in certain circumstances where you may have mass casualties—for example, the tsunami or the Bali bombing, where the level of casualties is such that they are way beyond our capability—the most effective way of repatriating bodies is by using a contractor and civil means. But the directive that I put out essentially puts the onus on our people to wherever possible get an Australian aircraft, an Australian chartered aircraft or an Australian commercial aircraft. The problem we have in the Middle East is that Qantas does not fly into that part of the world.

Senator FAULKNER—And this directive was issued as a result of the Private Kovko matter?

Air Chief Marshal Houston—Absolutely, yes.

Senator FAULKNER—Chair, there are other issues, but I specifically wanted to address that one to CDF before he left so I appreciate the committee's indulgence.

Air Chief Marshal Houston—I would be delighted to provide a copy of that if you wish.

Senator FAULKNER—You could perhaps table a copy of the directive. I am sure the committee would appreciate it.

CHAIR—What sort of aircraft is it that we have chartered?

Air Chief Marshal Houston—It is an A330 airbus. In fact, it is very similar to what we are purchasing for the tank or transport capability.

Senator HOGG—How long has this aircraft been on charter?

Air Chief Marshal Houston—For quite a long time; certainly in my time in this office. It has certainly been with us for all of the last year and for some period before that. There may be somebody here who knows precisely when we chartered it.

Senator HOGG—It just seems to me—

Air Chief Marshal Houston—It is longstanding.

Senator HOGG—I thought I had seen it on the ground in a number of places, as a matter of fact.

Air Chief Marshal Houston—You have, yes.

Senator HOGG—I was just wondering if it was crewed by an Australian air crew.

Air Chief Marshal Houston—Currently it is not crewed by Australians. But steps are being taken to provide it with an Australian crew.

Senator HOGG—Will that Australian crew consist of ADF personnel?

Air Chief Marshal Houston—No, it will not.

Senator HOGG—Is there an option to buy this aircraft?

Air Chief Marshal Houston—No, because we have a project, as you know, to buy five of these aircraft which will also have a tanking capability—

Senator HOGG—Yes, I understand that.

Air Chief Marshal Houston—that is, tanker transport. They will be able to do tanking or air-to-air refuelling matters or this sort of task.

Senator HOGG—So this is a limited engagement?

Air Chief Marshal Houston—It has turned out to be a long-term charter.

Senator MARK BISHOP—I want to net out that discussion we were having about troop deployments in various parts of the world. We have the company in the Solomon Islands, a battalion group up in East Timor, a task force in Iraq and I think a task force of people in Afghanistan. But you say that, notwithstanding that heavy deployment of troops in operations overseas, within the strategic guidance given to you by the government, if we had to put up to a battalion into another hotspot in this region you would be able to satisfy the request of the Prime Minister?

Air Chief Marshal Houston—Absolutely. When we deploy the ready forces, we reconstitute and reorganise to have another unit ready to go, and that is exactly what we have done.

Senator MARK BISHOP—I have a final matter on East Timor. Is it true that you have taken 28 personnel from staff training courses in order to man the operational headquarters in East Timor? Would you care to comment on that?

Air Chief Marshal Houston—We have taken people out of the staff college to augment our operational staff areas here in Australia.

Senator MARK BISHOP—Is the headquarters for the operation in East Timor located in Australia or East Timor?

Air Chief Marshal Houston—We essentially have a headquarters in Timor—that is Brigadier Slater's brigade headquarters. That is a normal formation headquarters. The next headquarters that is in the chain of command is Headquarters Joint Operations Command. That straddles Sydney and Canberra. We have elements of it here in Canberra and elements of it in Sydney. That will all come together in the future in the Bungendore arrangements. We have put more resources into Headquarters Joint Operations Command and some additional resources into the operations staff area within Australian Defence Force headquarters. Those resources have come from the staff college.

Senator MARK BISHOP—Is it normal practice to take people out of their staff training role to augment operational planning requirements when we have people deployed overseas?

Air Chief Marshal Houston—It is what we did in 1999 in very similar circumstances.

Senator MARK BISHOP—Is that demand driven by the immediacy of the deployment in East Timor or is it driven by other matters? You do not have a similar arrangement for the task force in the Middle East, do you?

Air Chief Marshal Houston—No, we do not, because, if you look at Iraq and the circumstances for Afghanistan, we have been able to plan those in slow time and use the staff resources that we have for our current circumstances. But because of the speed at which the situation arose in Timor Leste we decided that we would pull some people out of the staff college. I might add that we did the same thing for a brief period during our involvement in the war in Iraq as well.

Senator MARK BISHOP—How many people have you pulled out of the various staff colleges?

Air Chief Marshal Houston—It is just under 50.

Senator MARK BISHOP—They are operational planning people—is that a fair call or not?

Air Chief Marshal Houston—They are people mainly of the rank of major equivalent. They all have a very rich operational background from the three services and in these circumstances they are worth their weight in gold.

Senator MARK BISHOP—Those 50 people that you have pulled out of the staff colleges: are they essentially the Australia based operations/planning group for the job in East Timor?

Air Chief Marshal Houston—I have just received a note that says that we are now up to just over 60 people. The information I gave you was from three or four days ago. When our people find a rich resource, they exploit it! Could you ask the question again?

Senator MARK BISHOP—Those, now 60, people that you have pulled out of the staff college: are they not merely augmenting the planning or operations group but are really the nucleus of the planning operations group for East Timor?

Air Chief Marshal Houston—No. They are augmenting our existing staff here in Australia. They are giving us a much more robust 24-hour-a-day capability. They are giving us a much more robust planning capability and a much more robust ability to monitor operations, not only in Timor but in all the other things that we are doing.

Senator MARK BISHOP—If we have added 60 from the staff training college, how many people in Canberra and Sydney at the JHQ are involved in that planning and operations work for the East Timor operation?

Air Chief Marshal Houston—Just about all of them are involved in Joint Operations Command, but I would like to take that on notice and come back to you on where they have all gone because I am aware that some of them have gone into the enabling areas as well. One of the things about this particular deployment is the fact that there is always a tendency to focus on the sharp end but the whole organisation comes under challenge. Not only the headquarters here but the services, the logistics part of our organisation, the corporate support, our intelligence agencies, every part of the organisation, gears up. So, whilst we talk in terms of a battalion group, the effect of the deployment is much more widespread. It affects the whole of the organisation, both military and civilian, because we are a fully integrated organisation.

Senator MARK BISHOP—Yes, I understand.

Air Chief Marshal Houston—All parts of the organisation do a great job in responding to the operational requirement.

Senator MARK BISHOP—I accept that response. You might take it on notice and ask one of your people to advise us how many people in total are in that JHQ in Canberra and Sydney for the East Timor operation, how many were there at the outset, how many have been supplemented from the staff college and if there are further plans for additional supplementation. If you could provide us with that general detail over the next few hours it would be much appreciated.

Air Chief Marshal Houston—Certainly.

Senator MARK BISHOP—While you are here, I have one more issue. I am advised that we have committed six sub-units to Afghanistan. Is that correct? What are we deploying in Afghanistan at the moment?

Air Chief Marshal Houston—At the moment or the planned deployment?

Senator MARK BISHOP—The planned deployment.

Air Chief Marshal Houston—The planned deployment, as I mentioned in my introductory remarks, is a reconstruction task force. It is built around two engineering

capabilities—in other words, two discrete engineering capabilities, one we can put out in one area of Afghanistan, the other we can put out in another area, so that, if you like, we have two separate capabilities. It is a capability that will obviously need to be supported. We have all the normal support people and the command elements and we also put a very heavy emphasis on providing the right level of force protection. We will be embedded within the Dutch Provincial Reconstruction Team, and I think this will be a very credible and effective contribution which is focused primarily on engineering tasks. Initially, the tasks that we will conduct will be in the vicinity of the capital of the province of Uruzgan. I believe that is a place called Tarin Kowt. As the security situation dictates, we will start to move out from there, probably on road improvement tasks. We will also work with the Afghans and do a bit of contract management as well.

Senator MARK BISHOP—Who is the senior officer on the ground in charge of those two separate detachments in Afghanistan?

Air Chief Marshal Houston—The tactical commander in both cases is a lieutenant colonel.

Senator MARK BISHOP—Your comments apply to the deployment of the special operations people in Afghanistan as well, don't they?

Air Chief Marshal Houston—Yes.

Senator MARK BISHOP—Why was the decision made to have the senior Australian officer in command on the ground at lieutenant colonel level and not at brigadier or higher level? What was the thinking there?

Air Chief Marshal Houston—Perhaps I should explain that.

Senator MARK BISHOP—I might put the question in context. The report that was made to me—and I do not say that this is true—was that the decision to appoint a non-star level officer in charge on the ground takes away from him the necessary authority when he is involved in discussions and negotiations with his counterparts within the overall allied operation there. The question is: why was it a lieutenant colonel and not a star rank officer for carrying out our national interests and him having sufficient authority to impress upon others our needs?

Air Chief Marshal Houston—First of all, let me explain how it all works. I will start with the special forces task group. The special forces task group is commanded by a lieutenant colonel. The lieutenant colonel reports, in national command terms, to the brigadier in Baghdad as part of his deployed organisation in the Middle East and Afghanistan. Obviously, the brigadier then reports direct to the Vice Chief of Defence Force through his deputy in Sydney. In terms of operational control, the special forces task group is under the operational control of the American special forces commander in Afghanistan. That arrangement works very well. I think it would be a complete overkill to put a one-star officer in over the top of a very effective lieutenant colonel who is doing a great job in southern Afghanistan.

Essentially, we now have our third commander there. The two preceding commanders did a magnificent job, and the last thing they would have wanted, let me tell you, would have been to have a brigadier or a colonel over the top of them. I think if they were able to talk to you

they would say that they were very happy with the arrangements that were in place. Certainly, that is the feedback that they have given to me. I do not know where you got your information from, but I am very happy with these arrangements. Indeed, since we put the helicopters into place, we have actually created a new structure whereby we do have a colonel who sits in Kabul, and essentially the elements within Afghanistan will report through him to the brigadier in Baghdad.

Senator MARK BISHOP—Have there been any changes to the rules of engagement applicable to Australian forces operating in Afghanistan from those of earlier operations in that country since 2001?

Air Chief Marshal Houston—The rules of engagement that we put in place for the current deployment are specific to the task that we have been given this time around. So, whilst we would extract the lessons learned from the deployment that we did in 2001, we have developed the rules of engagement for this specific task. Rules of engagement are always under constant review to improve and adjust them to the circumstances we face, and during this current deployment I think they have been adjusted at least a couple of times to meet the circumstances that are out there at a particular moment in time. In other words, we are always seeking to continuously improve them to make them as robust as possible.

Senator MARK BISHOP—I understand that. Are the rules of engagement for various deployments regarded by you as in-confidence documents, or are they promulgated pursuant to various regulations?

Air Chief Marshal Houston—There are two elements to rules of engagement. There is the national policy part of it. The national policy guidance is essentially government's policy guidance to me, and we develop the rules of engagement on the basis of consideration of the national policy, the mission requirements and what is required to protect our soldiers and give them what they need to basically effect their mission. So the rules of engagement that come out are always a secret document. They are highly sensitive and they would be very valuable if they fell into the hands of an adversary, so we never talk about them in detail in places like this.

Senator MARK BISHOP—That is fine. I asked the question; you have answered it.

Proceedings suspended from 11.01 am to 11.20 am

CHAIR—We are continuing on the portfolio overview through budget summary to capability development.

Senator FAULKNER—Mr Smith, I asked in another committee about compensation payments and act of grace payments that had been made. I just wanted to explore those. Can you point me to the right program for that?

Mr Smith—That would be best taken up with CDF or the vice-chief when they are here tomorrow if you are talking about the sorts of act of grace payments you spoke about with the department of finance the other day.

Senator FAULKNER—Yes. As you know, they referred questions to Defence. I do not mind if CDF is not here, but—

Mr Smith—The chief or vice-chief would prefer to take them. I will make sure they are alerted to it.

Senator MARK BISHOP—Chair, Senator O'Brien has advised me that after lunch he is going to have some questions of Air Force going to its relationship with Customs, patrols and operation up in the north.

Senator HOGG—Air traffic controllers.

Air Marshal Shepherd—Air traffic controllers or Coastwatch?

Senator HOGG—I was at the same committee he was at and I am sure it is about the relationship you are now developing with Airservices Australia. I have forgotten the name of the project.

Air Marshal Shepherd—The relationship is called Project Genesis.

Senator HOGG—Yes, that is it. I am sure that is where his questions will lie.

Senator MARK BISHOP—I have some questions about the JSF project and costings, particularly about the discussion that has been in the press on our involvement in the JSF project, alternatives such as the F22 Raptors, and the cost differential between the two platforms. There was a report about two years ago by the then Chief of Air Force, reported by the Australian Strategic Policy Institute, as to whether going down the path of the JSF was perhaps not best value for money. At that time he had a view that alternate platforms might be preferable. He was reported under his name, Air Marshal Angus Houston, as saying, 'Our advice to government to move to a more modern fifth-generation aircraft reflected our view that the fourth-generation aircraft would not meet our needs nor be good value for money.' There have been a number of reports from the US Government Accountability Office, the GAO, and the US Department of Defense that point out escalating unit costs, and hence total cost to us, for the JSF and downward costs for the alternative, the F22. Are the government and the Air Force still committed to the JSF project as opposed to alternative platforms, bearing in mind the contracting cost differential?

Air Marshal Shepherd—I may start on that question and then hand over to General Hurley, who will answer the detailed costing aspects. Just to clarify the point made by the previous Chief of Air Force, he spoke about a fifth-generation fighter, and the JSF is exactly that. It is a fifth-generation fighter. It is, indeed, a later generation fighter—not by a whole generation but by an incremental amount—from the F22. It builds on a lot of the capabilities of the F22 and brings in a lot of other, new capabilities. It is the latest generation fighter available on the market today. So, in that sense, there is nothing inconsistent with what the previous chief said. It does offer us the best value for money because it provides an air superiority solution as well as an air-to-ground solution. It is a true multirole aircraft. The F22 is not; it is an older capability.

As I have said at this committee previously and at other committees, the F22 is not for sale to any other country. I had that reaffirmed just recently on a visit to America. By law they are not allowed to pursue its sale with any other countries. Even if that were to be removed, the aeroplane does not come with an air-to-ground solution. It would come with obsolete equipment and capabilities. It would need to be upgraded. So you would not be buying the

capability that you needed in the F22. With regard to specific costings, I will ask General Hurley to comment.

CHAIR—Just before we go to General Hurley, can you confirm with any greater detail that the F22 is not for sale? Can you take us further into the confirmation of that?

Air Marshal Shepherd—They had a law passed by their congress, I understand, that says they believe in their war-fighting doctrine that air superiority is the essential campaign. That is true in air power theory. They believe that the ability to have dominant air superiority to defend American interests and America necessitates them maintaining the best air superiority capability. The F22, I understand, is not allowed for sale by congress.

CHAIR—Have you explored the possibility of a change to that policy disposition?

Air Marshal Shepherd—No, because we are not looking for the F22. It came up in a discussion with a senior US official. He just reiterated the policy in a discussion about a third country.

CHAIR—Was he a military official?

Air Marshal Shepherd—He was employed in the US air force as a US air force defence civilian.

CHAIR—His description was that this aircraft is not for sale—that it is a matter of national security from their point of view and they would retain that capability?

Air Marshal Shepherd—That is affirmative.

Senator HOGG—Are you saying that there is one option and one option only that is being pursued—that is, the Joint Strike Fighter? There is no alternative to the Joint Strike Fighter being looked at?

Air Marshal Shepherd—That is the government's decision in the process that we are undergoing. General Hurley will touch upon the detail of that a bit more. I would like to make the point from a capability sense that, even if the world changed and the F22 was available, we expect the JSF to develop a capability that will be far better for Australia in a value-for-money and full multirole sense. It will be a full air-to-air capability and an air-to-ground capability. So, if it were to be for sale, it would still not change the fundamentals of the way we are looking at this project.

Senator HOGG—All right. I was just curious as to whether there was another option out there anywhere. That does not seem to be the case.

Air Marshal Shepherd—There is not any other fifth generation fighter option. Any other fighter that would be up for purchase is more of a fourth generation activity.

Senator HOGG—This has not gone through the first pass process yet, has it?

Air Marshal Shepherd—That is affirmative. General Hurley will be able to give you more detail on that process.

Senator MARK BISHOP—General Hurley, decisions to purchase particular platforms, in this instance to purchase a fifth generation and not a fourth generation if it was available, are made within a range of parameters such as the demands of our services, the likely threat

scenarios and how they can be used. Of course, one of the issues that I presume you consider is the cost at the time and either escalating or downward cost as the product is developed. We have had two reports: the US House Armed Services Committee's Subcommittee on Tactical Air and Land Forces report and the US GAO report. Both of those reports make the strong point that the developmental costs of the JSF are increasing at a rapid rate. They continue to increase. They anticipate those costs will continue to escalate. In that context, why is it preferable to be purchasing apparently the most expensive fifth generation aircraft for a country this size as opposed to going with an acceptable existing platform or fourth generation alternative?

Lt Gen. Hurley—You are entirely correct in enunciating the factors that we take into account in terms of determining what the capability requirements are for Australia. You would be well aware that the Defence white paper 2000 stated that air combat capability is the most critical Defence capability for the defence of Australia and for the ADF. To ensure that we maintain that over time at a cost-effective level, we are looking for an aircraft that is going to have the capabilities we need to conduct both air control operations and strike operations at a cost we can afford. The JSF fits that model. If we look to try to build those capabilities up from any alternatives—for example, the F22 and F111 have been suggested—it would be at an enormous cost. We are running two fleets of aircraft because we cannot get a fifth-generation, multirole aircraft other than the JSF.

Senator MARK BISHOP—So, notwithstanding the significant reported cost increases to date and likely escalation in costs over the next five to seven years, you still stand by the previous decision?

Lt Gen. Hurley—I do, and in a moment I can ask Air Commodore Harvey, who is the project manager, to go through where the costs are at the present time. But I would say that if five years ago we had been sitting here and we had made the decision to go to F22, you would be giving me a caning today on the same basis: costs are escalating. These are developmental aircraft, with high technology. This is their trend.

Air Marshal Shepherd—I can add from talking to senior American officials both in the military and in Lockheed Martin on a recent visit I made to America that they dispute many of the findings from the GAO report, of course. They have not accepted them and they do not believe that the picture is as dark as the GAO report would indicate.

Senator MARK BISHOP—It is a very black report.

Air Marshal Shepherd—Which is why they do not agree with it.

Senator MARK BISHOP—I might say, 'You would expect them to say that!'

Air Marshal Shepherd—One might say that!

Lt Gen. Hurley—I think you have to put the GAO report in perspective. They are looking at developmental paths to production of this aircraft and trying to work out: is this the right path to production? Some of their cost predictions are viewed on taking alternative paths to what the government and Lockheed Martin are taking at the present time, and that argument will be battled out over this year.

Air Marshal Shepherd—I can add one example for clarification there. The GAO report, to their mind, is based very much on a linear development activity for modern aircraft, as has been the case in the F16 and very many aircraft to date. Lockheed make the point that they are introducing very new production and manufacturing capabilities. You only have to visit the flight line there at Fort Worth to see them making the F16 on one side, still drilling holes and pop-riveting things, and then look at the way the JSF is built: very much carbon fibre, huge autoclaves, tolerances such that when they put the first aeroplane together they did not even have to use any adjustments, what they call shims—little pieces of adjustment material. Nothing like that happened. It was all laser lined up, computer designed, fitting like a glove first time. The fuel tank did not even leak first time. It is a quite amazing manufacturing capability. They believe they will be able to manufacture at that high order of capability while they develop the aeroplane at the same time, whereas in previous aeroplane projects they had to manufacture the aeroplane as a more linear project.

Also, the JSF is effectively a computer—the whole aeroplane is a computer. It does not just have computers in it, so that you can pull out a box and replace a computer; the whole aeroplane is effectively a computer. The skin of the aeroplane and all these systems that are on board are part of that overarching capability. Lockheed is very confident—and, once again, you would expect them to say that; they are a company. But you cannot help but be impressed by the effort they have put into this. We are very involved in that developmental activity. We have our scientists involved. We have our own air crew that go across there. They have a whole range of cockpit mock-ups. They have a whole range of interleaved and interactive computers around cockpit mock-ups so that they are able to develop tactics and computer software loads for the aeroplane as it is being built. Effectively, the aeroplane is being built from the outside in, rather than building a frame, as with old aeroplanes, and then building from the inside out. They are very confident they will be able to come up with a new way of doing business that will negate many of the concerns in the GAO report.

Senator MARK BISHOP—Thank you. A lot of that information is both technical and relevant. My issue is the issue of costs and value for money. That is what I want to explore with either General Hurley or Air Commodore Harvey. Have the published reports from the GAO and the US house subcommittee caused Air Force to make any further recommendations to government as to its decision to be heavily involved in the JSF project?

Air Cdre Harvey—Perhaps I can clarify some of the costing arrangements with the JSF project. There tend to be two elements of it. There is the development project and then the production side of it. The cost increases we have seen referred to in the GAO reports tend to relate to the development side of the project. The US bears those costs. We made our contribution of \$US150 million. That is fixed. So those changes are borne by the US government, which is one of the benefits of being a partner in such a large project.

There has been a recent slight increase in the acquisition price, but it is certainly well within the funding that we put aside to allow for the contingencies of expected cost increases. A key point to note is that, even with those latest estimates of the price, it is cheaper than even the viable fourth generation aircraft. The JSF is a generation ahead, but at the same time it is much more affordable than current aircraft. That is why the fourth generation aircraft are particularly unattractive, because they cost a lot more and cannot do as much. We keep

monitoring the program—how the cost and capability are going—but nothing has happened to date that would fundamentally question our belief that the JSF will provide the most cost-effective solution.

Senator MARK BISHOP—Do you do your own risk analysis of the JSF project?

Air Marshal Shepherd—If I may just pick up one other point from your question—you asked about the American Air Force commitment. I had private discussions with General Moseley, their Chief of Air Staff. They are very committed to the JSF. They need to replace a lot of their range of tactical aeroplanes such as the F16 and the A10. General Moseley firmly believes that once the project really gets under way there will be far more countries around the world seeking involvement in ultimate JSF sales. So he has no fear that the JSF will also provide the US Air Force with the capability that they will provide into the future.

Senator MARK BISHOP—Air Commodore, you refer to the costs increase as being marginal, minimal or slight. I was using the other end of the frame: significant and large. Have I correctly reported what you said?

Air Cdre Harvey—As I said, there are two elements to the cost.

Senator MARK BISHOP—Yes, development and production.

Air Commodore Harvey—Part of it was the development part, and we do not share those costs so that has no impact on Australia. The unit recurring flyaway cost in the last selected acquisition report of December 2005, which came out in April this year, showed there was about a seven per cent increase in the unit cost of the aircraft. Again, that is well within what we have allowed for in our contingency for the expected ultimate cost of the aircraft.

Senator MARK BISHOP—If developmental costs are increasing either marginally or significantly and the time frame of development is blowing out, don't the development costs have to be factored into the acquisition costs when we come to sign up for the contract in due course?

Air Cdre Harvey—They are quite separate costs. The development cost is separate from the acquisition cost. We have paid our contribution, which is one of the benefits of being a partner. The unit cost is basically the cost of cranking the handle to roll out another machine effectively. By joining as a partner in the program we have avoided any future contribution to those costs in the future—

Senator MARK BISHOP—To the developmental costs?

Air Cdre Harvey—That is right.

Senator MARK BISHOP—You are correct to say the development costs are a separate box to the acquisition costs. Let us assume that the development goes ahead, it is eventually successful and it goes to full-scale manufacturing. Presumably the costs that have been expended on the development side, to some extent, are going to be sought to be recovered by the manufacturer who sells the product. In that context, the development costs are part of the unit cost and part of the aggregate cost that we pay for however many we buy. So, if the developmental costs are accelerating more than was planned, by definition the aggregate cost that we pay in due course has to increase similarly.

Air Cdre Harvey—In fact that is not the way it works. By being a partner in the project, the contribution to the development costs has been covered by our \$150 million contribution. Lockheed Martin does not pay those costs; the US government pays those costs and it absorbs that as its cost of developing the project. What will happen in the longer term, though, is that third parties who want to buy the aircraft through foreign military sales will pay a share towards the development costs and Australia as a partner will recoup some of our \$150 million by sales to those third parties. There is quite a clear divide between the development cost and production cost.

Senator MARK BISHOP—There is as yet no indicator of the price of the eventual product when it is determined to be suitable for manufacturing, is there?

Air Cdre Harvey—Yes, there are very good indicators of price. As I mentioned, the recent Senate selected acquisition report updated the expectation of what they call the average unit recurring flyaway cost—the cost of producing a JSF. The average, because this will extend over about 30 years, has gone up to about US\$46.5 million in a fiscal year 2002 baseline. That is the estimate of the average aircraft. Earlier aircraft cost more; later aircraft cost less. So we do have a good reference, we work with the JSF project office with that estimate and we factor that into our budgets.

Lt Gen. Hurley—Senator, you used the words that the schedule was ‘blowing out’. Again, I think we need to consider where we are in the project. There was a period when there was a weight problem with the short take-off and vertical landing aircraft when 12 months or so was taken to correct that. We lost two months before first flight of the conventional take-off aircraft—what was going to be August this year slipped back to October. But to say things are ‘blowing out’ under current indications is not correct. I think there is also an assumption in some questions that come out in the media and in commentary on this that we are not involved enough in the project. I would like the project manager to explain how deeply we are involved in the project. We are not just waiting for the US to develop an aeroplane that we will purchase.

Air Cdre Harvey—We have a project team of about 40 people now, plus we have about 30 DSTO scientists on a full-time basis looking at technical aspects of the project. There is a team of about a dozen in the United States now, some within the JSF project office, some within US industry. We have specialists on mission systems and vehicle systems in the embassy and they engage on a daily basis with the project. So we have a very good understanding of the technical aspects of the project. As I said before, one of the benefits of being a partner in the project is that we get to see how the project is progressing and to actually help. We have DSTO scientists working with the US to help the project progress and, as we move towards the next phase of the project, the MOU we are negotiating now will cover at least another eight or so Australians working in the JSF project office.

Air Marshal Shepherd—Also, as I said before, we have air crew that go across at certain selected times to work operational scenarios and develop the capabilities that will be fielded in the aeroplane. They work collaboratively with other partners—the Americans, the Canadians, the British et cetera. That is all done at Fort Worth in the factory, as I explained before, in a range of simulated cockpits that all link together to work out how the aeroplane will network and all those operational techniques. I should add on costs, too, that the

aeroplane was designed from the start to be using low-cost production techniques. I go back to that example I gave of the difference between the F16 costs and the way they build the F16, in a sort of legacy fashion, and the way that this aeroplane is built. They believe that the costs for production will be efficient. I think there is a blow-out in the schedule. I do not think there is a blow-out in the costs at all. It is still a developmental aeroplane, of course.

Senator MARK BISHOP—All right. General, you don't have any concerns about Australia entering into the next phase of the program—the production, sustainment and follow-on development phase? You are satisfied we should be entering into that?

Lt Gen. Hurley—No, I do have concerns, and we make those quite clear to the United States: that I will not take it to first pass approval for government unless I am confident that we have got the MOU laid out the way we want, we have a bilateral annex that supports Australia's strategic objectives in sustaining the aircraft in Australia, we have assurance of the right levels of technology release that we require and we have an adequate Australian industry participation program. We are pushing each of those points with the US very actively.

Senator MARK BISHOP—All right. Where is the next phase of MOU at? Are we in the process of negotiation at the moment?

Air Cdre Harvey—I am leading the Australian team for the negotiations and I will head off to the US on Saturday with our team for the last round of negotiations for that MOU. We hope to have the draft of that out in mid-June. The aim is to sign that in December, as long as all the various departments in Australia are happy with the MOU and the prerequisites General Hurley mentioned are in place. We will probably get together at some stage before the end of the year just to coordinate, because we have nine countries reviewing the MOU for final coordination. But all the countries are reasonably confident that we can have an MOU in place to sign in December.

Senator MARK BISHOP—Okay. And our signing-up to the MOU is a precondition for first phase approval of the project?

Air Cdre Harvey—What we have done is aligned first pass and PSFD MOU together because it is a convenient milestone, really, to be able to go back to government with confidence that we believe the JSF can do the job and that cost schedule and capability issues are met. It is key to understand that the PSFD MOU is not a commitment to buy aircraft; it is a commitment to go to the next phase of the project and contribute towards developing the production side of the aircraft. So we thought it was very good to align the two of those. You would not want to sign the PSFD unless you have been to first pass; equally, you would not want to do first pass unless you were happy with the MOU. They are tied together.

Senator MARK BISHOP—So whilst you are progressing both at the same time, until we have signed up to the MOU for the next phase there would be no intent on the part of government to take it to the subcommittee of cabinet for first stage approval. Is that right?

Mr Smith—We would go to cabinet for first pass.

Lt Gen. Hurley—We will take them both through the Secretaries Committee process and the National Security Committee of cabinet.

Senator MARK BISHOP—When would you anticipate the first pass approval going to cabinet for consideration?

Lt Gen. Hurley—We are looking at about November.

Senator HOGG—In respect of the project, there have been a number of Australian companies involved in the project. I went to the site at Fort Worth at one stage and was very impressed with what was happening. It seemed to me that the level of participation by Australian companies was then in its infancy and may well have been growing. Has that changed during the development phase and will it change into the next phase as well?

Air Cdre Harvey—At this stage there are approximately 20 Australian companies on contract in the JSF program, and that is generally the development phase because Lockheed Martin itself does not have a contract yet for the production phase. Work to date is approximately \$US82 million and there are promises of additional work into the low rate initial production phase. We had hoped to have a higher level of contracts at this stage of the project. We are working closely with Lockheed Martin to ensure we have a robust industry participation plan in place before the end of the year. As General Hurley said, that is one of the prerequisites for signing the MOU. There are two aspects to that: one, to make sure—it is Australia's largest ever acquisition—we get a reasonable return to Australia in terms of work for Australian industry; and, two, to make sure Australian industry has the capability to support the aircraft when it comes into the country. We continue to have successes on the project; we want to see more success before we sign up to the next phase of the project.

Senator HOGG—Have any Australian companies dropped out of the process?

Air Cdre Harvey—When we first started the project we had more than 100 Australian companies interested—quite a lot there. Part of that was a discovery phase to see the alignment between their capabilities and what the JSF project required. In the JSF project all work must be won on a competitive basis. At various stages some companies have dropped out because there was no alignment there. New companies come in on a daily basis so it continues to move on a daily basis.

Senator HOGG—In respect of the ongoing participation of Australian companies, who is working to see that those companies get a fair crack at the ongoing stages?

Air Cdre Harvey—Part of the feature of the JSF project was to establish this JSF team Australia so all of government and all of industry were working together. It is working at every level from the Minister for Defence and the Prime Minister all the way down to the individual companies all working together to identify those areas where we can provide best value to the project. On the government side the task is largely to make sure the doors are open and any impediments are removed to make sure they can have a fair shot at work on the JSF program. We do work together as a team.

Lt Gen. Hurley—It also involves other departments—the Department of Industry, Tourism and Resources, the Department of Foreign Affairs and Trade and so forth.

[11.54 am]

CHAIR—We will move now to the FFGs and then come back to capability.

Senator MARK BISHOP—I have some questions on personnel levels on Navy ships. Question No. 1690, which I asked last time, you have responded to. It was about the number of ships in the fleet and their personnel levels. The detailed answer you provided showed a significant difference between the optimum crewing of the fleet and the actual. The figures you supplied in that answer show that the fleet is undermanned by some nine per cent. Taking out those undergoing maintenance, the fleet is undermanned by six per cent. That is a total of about 260 people across the fleet, give or take. My questions go directly to the effect of apparent suboptimal personnel levels in fleet and recruitment failure on operational capacity. Looking at those figures you supplied me, what effect does that undermanning by either six or nine per cent have on the manning levels and the optimum operation of the fleet?

Vice Adm. Shalders—Firstly, I make the point that our ships deployed in operations are manned to 100 per cent. Across the fleet, not every ship is allocated to operations all the time. For example, the FFG *Melbourne* is currently in dock undergoing FFG upgrade. She will not have 100 per cent of her manning during that period.

Senator MARK BISHOP—I made that point: the difference between nine and six per cent is operations and maintenance. I accept that.

Vice Adm. Shalders—It is not correct to say the fleet is manned at a suboptimal level. I dispute that point.

Senator MARK BISHOP—Why do you dispute the level when your table discloses two key headings, (1) ‘optimum crew’ and (2) ‘current crew’, and there is a significant differential between the two? Why can I not draw the conclusion that we have suboptimal crewing levels?

Vice Adm. Shalders—I think probably the difference can be explained by the way the ships are being employed. I will come back to the *Melbourne* example. Right now while she is going through upgrades she is manned to 50 per cent. So instead of about 210 people in that ship there are something around 100. She will ramp up, of course, as she comes close to the end of that program. Similarly, 805 Squadron is currently not manned to 100 per cent because of issues with the *Seasprite*, which you have signalled you will be talking about later. I think that is the simple explanation of the two different sets of figures.

Senator MARK BISHOP—With due respect, Admiral, I did say at the outset that I appreciated the difference between ships that are involved in refit or maintenance. Your own figures show that the total fleet is nine per cent undermanned. For those ships that are involved in refit, refurbishment or maintenance, the figure drops down from nine per cent to six per cent. I am not critical of that. We do have ships under maintenance on an ongoing basis but we still have a shortfall of staffing levels and surely that impacts on our ability to deploy. Our maintenance, refitting and refurbishment is planned many years ahead into the future. Otherwise why do you have optimal crew levels for operational ships?

Vice Adm. Shalders—There is no impact on our ability to deploy, if that is where your question is going. We can and do deploy at 100 per cent of ship’s company.

Senator MARK BISHOP—Why do you have optimal crew levels, then?

Vice Adm. Shalders—Each ship has a scheme of complement, which you have described as an optimal crew level.

Senator MARK BISHOP—That is the term your answer used. I have not made it up.

Vice Adm. Shalders—Our philosophy is to man operational ships to 100 per cent of their scheme of complement.

Senator MARK BISHOP—What do you define as operational ships?

Vice Adm. Shalders—Ships that are deploying on an operation will be manned to 100 per cent.

Senator MARK BISHOP—Does that definition of operational include ships that are in particular training or in routine training?

Vice Adm. Shalders—This comes back to our preparedness management system. We have a directed level of capability. As a ship comes through a maintenance cycle it is required to achieve a certain level of capability. We put it through a work-up process in order to achieve that level, whatever it might be. As it goes through that process it will be manned to the level required for the capability that is needed to be delivered. For example, we have recently been directed to send two minehunters to the north of Australia to conduct fisheries patrols. Those minehunters are normally manned with 39 people on board. In this new role they will not require those 39 people. They will not require the same mix of specialisations. In that role—

Senator MARK BISHOP—Because they are carrying out a different function from the one they were designed for.

Vice Adm. Shalders—They are carrying out a different task and a different role; that is correct.

Senator MARK BISHOP—So there is a different crewing level for this particular new task?

Vice Adm. Shalders—It is the effect that you are trying to deliver with the platform, whether the platform is a submarine, a minehunter, a frigate or an air squadron. It is the effect that is required to be delivered and that is the level of capability that I spoke off.

Senator MARK BISHOP—So, in terms of my questions, are you saying to me that figures relating to optimum crew levels for ships in service are really meaningless figures?

Vice Adm. Shalders—No, I am not saying that.

Senator MARK BISHOP—You appear to be saying that because you have made the point that, if ships are deployed on operations, they are manned fully. But ships are not always deployed on operations; they are often deployed on training arrangements or other types of work. So when they are doing those tasks, are they fully crewed?

Vice Adm. Shalders—They may not be fully crewed, no. But I am not saying that the scheme of complement is a meaningless document, which I think you just said that I had said.

Senator MARK BISHOP—It was my take on your response, that you were trying to put the proposition that optimum crew levels only had relevance when ships were deployed on operations. You have contradicted me and said, ‘Optimum crew levels also have relevance when ships are engaged in training purposes.’

Vice Adm. Shalders—Within the level of capability that that ship or platform is required to deliver. It is driven by the level of capability.

Senator MARK BISHOP—And training of crews on submarines, frigates and other warships, presumably, is designed around the men having full ability to deliver maximum operational capability.

Vice Adm. Shalders—It would depend on the task that that ship is being directed to conduct. It would depend on the level of capability that is being directed at that platform.

Senator MARK BISHOP—When I was over at the base in Western Australia, they gave me the courtesy of extensive briefings on the submarines. The commanders in charge of the subs made the point to me that they were constantly engaged in training, that they were constantly required to have themselves as individuals and their crew up to a very high level of capability, that their training was designed to replicate as near as possible operational requirements and that, at short notice, they could be deployed on operations anywhere in our sphere of influence. That being the case, their training is really to the maximum level of capability of that particular platform, is it not?

Vice Adm. Shalders—In that case, they are speaking of what we would call an operational level of capability or OLOC. In the case of the Submarine Force Element Group, for example, presently we have four of the submarines running at sea. Two of them are in Adelaide. Of those four submarines, three are fully manned—that is, they can achieve, and have been certified as having achieved, OLOC, the operational level of capability. The fourth submarine is not manned to its full extent at this stage because of manning shortfalls, and I am the first to admit that we have difficulties, which is, I think, the root of your question. The fourth submarine is not fully manned because she is not required to deliver that full operational level of capability at this stage. The three fully manned submarines can achieve that.

Senator MARK BISHOP—That is a chicken and egg situation. If you do not have sufficient men you cannot operate the platform to full operational capability and you cannot have full operational capability if the crew are not adequately trained. The precondition to both is to have full crew levels to an adequate level of training.

Vice Adm. Shalders—No. In the case that we have just been discussing we do not have a requirement to have four submarines at the full operational level of capability. The way we are managing the shortfalls we have is to have three submarines at that level and the fourth is not fully manned.

Senator MARK BISHOP—If we have six submarines—two are still being worked on in Adelaide—and four are in the field, for want of a better description, why is it that only three and not four of those platforms are required to be at full operational level?

Vice Adm. Shalders—We work to government direction. You had this discussion this morning with the CDF. The directed level of capability for the Submarine Force Element Group does not require all four submarines to be at that level. As a result of some shortfalls, which I admit we have in the Submarine Force Element Group and in others, we could not do that, but we are meeting the level of capability required of us in that force element group by having three submarines fully manned and the fourth less than fully manned.

Senator MARK BISHOP—Are you putting to me the proposition that the below optimal level of crewing in the one submarine and other warships is not having any impact on our ability to engage in operations?

Vice Adm. Shalders—I am not putting that to you; I am saying that we can achieve the required level of capability as directed by government with the manning that we currently have. We are managing a shortfall.

Senator MARK BISHOP—All right. I have asked and you have answered. You made the point that the ships that have been deployed to East Timor and the Gulf are fully manned.

Vice Adm. Shalders—Certainly the ship that is deployed in the northern Arabian Gulf is fully manned. She is at the highest level of capability, OLOC. The ships that are deployed in support of the East Timor activity are largely fully manned for the sorts of things that they are required to do. For example, HMAS *Tobruk* does not have an air warfare defence role and is not expected to need that sort of capability in that theatre of operation so she may not have 100 per cent of her full complement of bosun's mates, for example. But to do the job that she is doing now and for HMAS *Kanimbla* and HMAS *Manoora* to do the jobs that they are required to do now, they are fully manned.

Senator MARK BISHOP—Okay; I take the point you make. You are saying they are fully manned. Before they were deployed to East Timor and the continuing deployment in the Gulf, did you have to relocate personnel from other ships' crews to get them up to full manning operational level?

Vice Adm. Shalders—No.

Senator MARK BISHOP—They were at all times prior to deployment fully manned to operational requirements?

Vice Adm. Shalders—The two ships that were first deployed, the *Tobruk* and the *Manoora*, had, as it happens, just completed an amphibious exercise in New Caledonia. They were fully prepared for amphibious operations and fully prepared to conduct the activities that they are now conducting. The third major amphibious unit, the *Kanimbla*, had just come out of a maintenance period and in fact on the Thursday before she was deployed north was in Jervis Bay conducting flight trials with Sea King helicopters. She departed from Jervis Bay direct to Darwin with no stops. She was at an early part of her work-up phase and was, again, fully prepared to conduct the operations that she has subsequently been conducting. She was augmented by what is known as the primary casualty receiving facility, PCRFB—the hospital part—by reservists, largely; and those reservists and some other augmentees joined in Darwin before she headed north to Dili.

Senator MARK BISHOP—In terms of the table in question 1690, a lot of the ships have optimum crew level, or are so close to optimal crew level that it does not matter. Are any of the shortfalls of crew so serious or great that they are preventing the effective deployment or training operations of those ships?

Vice Adm. Shalders—That can and does happen. We have a personnel deficiency report system. Take the example of, say, a patrol boat, where there is a small number on board and the executive officer suddenly becomes ill. It may be that another executive officer cannot be

found, in which case the ship would raise an urgent defect report—a personnel deficiency report. That could prevent—and in fact in a recent case, for the first time in several years, it has prevented—a ship from sailing. The ship was the *Fremantle*. She was meant to be on patrol out of Darwin. We could not find an operation relief for an executive officer who became ill, so she lost three days, I think, on a schedule program. That can happen, and it can have that impact on operational outcomes.

Senator MARK BISHOP—Which ships are so seriously undermanned that they would not be suitable for either full training or operational deployment at the moment? Referring to the list of ships in question 1690, could you go through—

Vice Adm. Shalders—I am sorry, Senator, I do not have the question in front of me. I will get hold of it and we can go through it.

Senator MARK BISHOP—It is a list of all the ships in the fleet.

Vice Adm. Shalders—I would be happy to go through it and tell you where they are now and whether that is having an impact on the deployment, if that is where you want to go.

Senator MARK BISHOP—While we wait for a photostat of the answer to question 1690, I note that the estimated cost of the repair or refit of HMAS *Melbourne*, the next ship to be refitted, as set out in the FFG contract, will produce significant savings. Can you confirm that that is the case?

Vice Adm. Shalders—I will pass to the DMO, if I may, on that question.

Dr Gumley—The contracts are all in place now. Rear Admiral Ruting, and Kim Gillis, Deputy CEO of DMO, concluded the negotiations late last week. I will ask Rear Admiral Ruting to give you the detail.

Rear Adm. Ruting—Could you clarify your question. Are you referring to the refit cost of HMAS *Melbourne* as part of its upgrade?

Senator MARK BISHOP—Yes. The PBS states that there are going to be significant savings involved in that. Is that the case?

Rear Adm. Ruting—The actual cost of the refit part of the upgrade for each of the FFGs depends to a large extent on the condition of the ship when it goes in for that maintenance. It is also impacted by the age of the ship. Obviously, the older ones, like HMAS *Sydney*, which had the first upgrade, would perhaps require more maintenance than a newer ship like HMAS *Melbourne*, the second one going into upgrade. The actual cost of the refit component of the upgrade for *Melbourne* is highly likely to be less than that spent on *Sydney*. For HMAS *Newcastle*, the fourth ship going into upgrade and also the newest of the six FFGs, it is likely to be less in terms of refit costs than *Sydney* or *Darwin*, which are both older ships.

I do not have the precise figures with me for the actual refit component of those, but the normal docking refit for the FFGs is typically in the order of \$9 million to \$12 million. Where we have found significantly more deterioration in some of the hull structure or something similar, a couple of them have gone out a little higher than that sort of figure. Generally, the newer ships—the *Melbourne* and the *Newcastle*—have been on the lower end of that range.

Senator MARK BISHOP—The 2006-07 PBS states that HMAS *Canberra* and HMAS *Adelaide* are no longer being considered for upgrade under this project. Was the decision made that this capacity was no longer required? Why was there a decision not to upgrade those two platforms?

Rear Adm. Ruting—That was a decision taken by government when it considered the defence capability review in late 2003. It determined not to do the upgrade on two of the FFGs. With HMAS *Sydney* having already commenced its upgrade, the obvious choice of the two ships not to upgrade were the two oldest FFGs.

Senator MARK BISHOP—I accept that. But was the decision not to upgrade the two older ships made because we no longer desire the capability that those upgraded ships would have provided or do we no longer need that capability? What is the rationale for the decision?

Rear Adm. Ruting—A range of factors were considered in the defence capability review of 2003. Understandably, a capability review looks right across at the entire ADF requirements for the future. At that point in time I believe it took into account new capabilities being planned, such as the air warfare destroyers and amphibious ships. In taking a balance right across all of the capabilities required in the shorter term and the longer term, a determination was made that it was better to put future investment into the air warfare destroyers and other maritime and non-maritime capabilities than in fact to continue with the upgrade of the two older FFGs.

Senator MARK BISHOP—But the amphibious ships and the AWDs will not deliver any capability until around 2013. When that decision was made, you say, in 2003 not to upgrade the *Canberra* and the *Adelaide*, you say it was largely made because we would have new capability coming on with those other two projects. Those other two projects are not coming on until 2013. Does that not necessarily mean that we will have reduced capability in Navy in that period or that we no longer desire the level of capability that we had previously sought?

Vice Adm. Shalders—The fact that we have the Anzac ships coming online actually keeps the number of frigate hulls at a fairly constant figure of around 12 to 13, depending on which part of the next decade you look at. By December this year we will have 13 frigate hulls—eight Anzacs and five Adelaide class FFGs. So the capability exists, but in a different platform.

Senator MARK BISHOP—But we will have significantly increased capability when the AWDs in particular come online, won't we?

Vice Adm. Shalders—We will.

Senator MARK BISHOP—So we will have the existing fleet of 13 platforms plus the three AWDs from 2013, giving us significantly enhanced capability after 2013, but you are of the view that we do not need that level of capability between 2003 and 2013 or that the level of capability is supplemented by the other five platforms—is that right?

Vice Adm. Shalders—No, I am not of that view at all. It would be an odd Chief of Navy who said he had enough ships all of the time.

Senator HOGG—I won't ask the obvious question then!

Vice Adm. Shalders—I will just make a slight correction to your statement. We will not have 13 frigates through to 2012 or whenever the first AWD comes online. The *Adelaide* will decommission at the end of next year, 2007, so we will actually have 12, and then, when the AWDs start coming online, hopefully from 2013, that will be an additional three ships.

Senator MARK BISHOP—So you are saying that, in terms of the decision to remove the *Canberra* and the *Adelaide* or not to upgrade them in the current round, their capability is adequately compensated by the other five platforms in the ongoing period?

Vice Adm. Shalders—It is a matter of balance, of course. We would like to have more capability for longer, but we will have a level of capability. We are concerned about the air warfare capability, as it is currently represented by the *Adelaide* class, and that is one reason for extending the *Adelaide* herself by another 12 months. It is also the reason, of course, for the upgrade to the missile systems as part of the FFG upgrade and the SM2 project. The air warfare capability of the *Adelaide* class FFGs is being improved through both the upgrade project and the fitment of the SSM and, subsequently, the SM2 system. We are concerned about the capability, but we have projects in train to address any deficiencies that we think we might have.

Senator MARK BISHOP—So what are you going to do with those two FFGs? Are they going to be mothballed, decommissioned or what?

Vice Adm. Shalders—They will be decommissioned. In fact, the first one, the *Canberra*, was decommissioned last November. The second one, the *Adelaide*, will run until the end of 2007. In terms of their future, the DMO becomes responsible for them once they have become decommissioned. A series of requests for tender have recently been responded to, but I am not sure that a decision has yet been made.

Senator MARK BISHOP—So we are going to flog them off?

Vice Adm. Shalders—I do not think we are going to flog them off.

Senator MARK BISHOP—I thought you said that there was a request for tender?

Vice Adm. Shalders—To dispose of them. I think the Royal Australian Navy has flogged the ships to this point, and I am not sure that anybody would get value for money in buying them.

Senator MARK BISHOP—Okay, I will not use the vernacular. We are going to dispose of the ships, is that right?

Vice Adm. Shalders—Yes.

Senator MARK BISHOP—Admiral, have you got the answer there to question No. 1690?

Vice Adm. Shalders—I do.

Senator MARK BISHOP—Okay, just for the record, the answer to question No. 1690 lists all ships in the fleet by their name, class, tonnage, home port, optimum crew levels and their current crew levels. My question is: which ships, because of crewing levels, are not satisfactory for operational deployment or for training of crew purposes?

Vice Adm. Shalders—I am happy to go through this if you want me to. But I will just make a couple of points before we do that. Firstly, this is a snapshot, of course. This is as it

existed on 21 April. For example, on that day you will see that the *Manoora*, which has an optimum crew of 182, had 220 on board. On that day, 21 April, she was engaged in an activity which required those additional people. The second point I make is that, rather than the somewhat academic figures you have in front of you, on 21 April, four days before Anzac Day, none of our ships was affected to the point that they could not conduct the operations that they were required to conduct. That is zero. All of our ships could do what they were required to do on 21 April. The last time that we had a personnel issue which prevented our ships from conducting operations was the situation I mentioned with the HMAS *Fremantle*, when her executive officer became ill and we could not find a replacement.

Senator MARK BISHOP—So the answer to my question is none.

Vice Adm. Shalders—Zero. And I will just bring you right up to date. HMAS *Bendigo* this morning lost her executive officer and a new executive officer will join this afternoon and, as a result of that change around, the ship will sail one day late. So they are the sorts of pressures that we manage on a day-by-day basis. They rarely have an impact on the operational tasks that we are required to perform. Would you like to go through this list?

Senator MARK BISHOP—Not unless you have something of value to add. You have told me that all ships on the list, as at 21 April, were suitable for deployment on operations if required or for deployment for the purpose of crew training.

Vice Adm. Shalders—On 21 April, there was no ship that was unable to conduct the operations with which she was tasked.

Senator MARK BISHOP—There is no sense in going through the list. You would not seek to deploy a ship for operational or training purposes if its crew level was so inadequate or below par that it could not carry out its assigned task, would you?

Vice Adm. Shalders—No.

Senator MARK BISHOP—Were any ships in that category?

Vice Adm. Shalders—No.

Senator FIERRAVANTI-WELLS—On that point, Admiral Ruting, you answered a question from Senator Bishop about the decision not to refit *Canberra* and *Adelaide*. If I heard your answer correctly, you said that the cost savings would be allocated to other projects, and I think you mentioned air warfare destroyers and amphibs. How much are the proposed savings, how will the savings be allocated and does this mean that you perceive or have projected that those projects could have a cost blow-out, and that may be why you are perceiving these savings as allocated? Could you clarify that for me?

Rear Adm. Ruting—The cost reductions as a result of not continuing with the upgrade of two of the FFGs is in fact not in the project costs per se, but the defence capability review took into account the operating cost savings of not continuing to operate those ships as part of what I call the ‘total balance defence costs’. The total capability into the future, with respect to being able to continue to operate the newer ships as they come online, was being considered in a global sense. It is not a matter of certain costs being saved from FFGs and being allocated to a particular new class because of the additional costs of those particular capabilities.

Senator FIERRAVANTI-WELLS—What is the projected cost saving?

Rear Adm. Ruting—The cost saving listed in the defence capability review was \$678 million over 10 years from the operating budget for the FFGs.

Vice Adm. Shalders—As those ships are decommissioned, the ships' companies are then available to assist us across the rest of the fleet. Right now, the company of the *Canberra*, which was decommissioned in November, is being applied to other ships across the fleet and specifically to HMAS *Perth*, which will be commissioning in August this year.

Proceedings suspended from 12.29 pm to 1.30 p.m.

CHAIR—I call the committee to order. There has been a slight change of plan; Senator O'Brien has some questions—and we have given a little bit of forewarning to Chief of Air Force—on air traffic control and Airservices.

Senator O'BRIEN—I asked the Department of Transport and Regional Services last week about the Genesis project, and I am hoping that you can fill in some of the gaps that they could not. How did Project Genesis come about?

Air Marshal Shepherd—To put Genesis in a bigger framework, it is but one particular activity. The bigger framework is that for many years the military, which has independent legislative rights to airspace under the Defence Act, and DOTARS, Airservices Australia and CASA, which have other independent rights and legislative responsibilities under their acts, have worked as parallel systems—sometimes even in opposition to each other. Clearly, national airspace, the use of it and the ways to get better efficiency out of it are in the interests of all of us. We all train air traffic controllers et cetera.

In recent times we have formed an aviation policy group. It is headed up by Mr Mike Taylor, the Secretary of DOTARS. Greg Russell, the CEO of Airservices, is on it, as are Mr Bruce Byron, the head of CASA, and me. It is not an official policy-making body; it is more a sort of clearinghouse where we can discuss issues communally in a collegiate fashion and get the best effect for Australia out of the airspace and resources we have. It is looking at recommending to both Ministers Truss and Nelson—recognising, as I said at the start, that we each have independent legislative authorities under various acts—the way ahead for a coherent, combined view about airspace. This includes national airspace reform, what sort of technologies we will move into in the future, whether we will replace radar with radar, whether we will go to satellite based technologies, and big strategic issues such as those.

Under that umbrella endeavour, which I think will be a great new story for Australia as we go down this path in the next couple of years, Project Genesis is a specific activity. It looks to cement a deeper relationship between Airservices Australia as a commercial provider of air services in the broad sense of the word to the travelling public and our air activities. It is about management and ownership of airspace, and training systems. Currently, for example, we operate an air traffic system with a bunch of computers. Airservices runs a similar system, but it is different. We have to share information with each other; we each used our capital to procure those at different times. It would make a lot of sense to ultimately have a single system. It would make a lot of sense if my air traffickers and the civil air traffickers were trained together, rather than us training air traffickers and then having them join Airservices so we have to train more. So we are looking for those sorts of synergies.

It would be a lot of use if we could work airspace issues so we in the military do not just automatically block off large chunks of airspace for the civil travelling public. Equally, we need increased access to civil airspace. That is probably part of a broader agenda about flexible use of airspace under airspace reform in the aviation policy group. But there are many practical things we can put into place with Project Genesis, that over time will produce a great benefit to Australia and a great cost benefit to Airservices Australia and to us in Defence. So we are looking joining up capital expenditure for new systems, moving our approach radar services from individual military bases into more of the model that Airservices runs with its approach services in Brisbane and Melbourne. We are looking at a more common workforce and at more joint training and, of course, maintenance and command and control.

We have done great work with our air traffickers in recent years. We have had them across in Iraq, as you know, running the airfield at Baghdad and working on the airfield at Balad, in very difficult circumstances. They have done a fantastic job for Australia. But to keep them employed on every single military base doing military movements alone is an inefficiency. I need enough that I can deploy in an expeditionary capability. I probably do not need the numbers that we are trying to recruit now. We always have trouble recruiting air traffickers and keeping them for the long haul.

Senator O'BRIEN—Why?

Air Marshal Shepherd—In many ways the Defence Force is a volunteer force. People come to a stage in their lives where they would rather stay in one spot. They have the normal pressures that are on all of us: kids, schooling and spouse employment. Airservices offers a very attractive second lifestyle. Perhaps we can combine those two and maybe look at better reserve officer options within Airservices.

Genesis is the nuts and bolts of that. It will hopefully give us in the Air Force a better and more stable military air traffic workforce that will be able to be sustained. It will hopefully give us better management of the whole national air traffic workforce and prevent, ultimately, those cyclic churn factors from people moving around. It will give my people, whether they stay in uniform or go across to Airservices, the ability to stay fixed in one location for longer and will stop that posting churn. We will be able to effectively use the airspace better if my approach controllers are sitting in Brisbane and/or Melbourne, right next door to their civilian counterparts. We will be able to work those issues together, rather than me having people stuck at Townsville, Darwin, Tindal and all those individual places. We of course will still need to run the visual tower air traffic controller service, but we are certainly looking at moving to Brisbane and Melbourne, subject to business cases. We need to do this in a hard-nosed way. We need to go into this with our eyes open. We are doing business cases on all these things.

We also have a national security interest in this, of course. We need to be able to put into place a mechanism whereby if we had to defend Australia in northern Australia we would be able to get air traffic data and move it around not only the air traffic system but our own air defence ground environment system in a secure way. So we will have redundant links to our EASTROC capability, our Eastern Region Operations Centre at Williamstown, that undertakes a lot of those war fighting airspace activities, such as airborne early warning and radar, when we get our ground based intercept radars. So Genesis, I think, is a very good news story. It has

increased morale in the Airservices Australia environment and certainly has increased morale in the RAAF environment. I think it gives our people better clarity and a coherent, combined workforce into the future.

Senator O'BRIEN—I have been given to understand that the RAAF had difficulties encouraging controllers to redeploy to Tindal and Darwin. Is that true?

Air Marshal Shepherd—It is true. Tindal and Darwin are great places, but they are more remote than Melbourne, Canberra and Brisbane. A lot of people are at the stage of their lives where they have children, and spousal employment is an issue. Certainly, when we send people up there it is an impost on their family life. For many military activities you need to be where you need to deliver the military effect, but that is not true about air traffic now. With satellite communications you can beam it back; you can do it. Airservices Australia is proving and has proven for some years that you can do all this from Melbourne and Brisbane. Indeed, they could do it from one centre. They have chosen to use two from a redundancy sense, and we fully support that. So, using new technology, using that concept of reach-back allows you to remove some of those pressures on your people. They will be able to spend a lot more time in a single area. That is good for us, it is good for their families and it is good for the whole system.

Senator O'BRIEN—The Airservices TAAAT system has been in operation for nearly a decade now.

Air Marshal Shepherd—Exactly right, and our ADAT system was in operation just before theirs. We have to share information with them and they have to share information with us. I have not touched upon the safety aspect of this yet, but this will give us a far safer outcome. We need all the feeds from the civil radars so that we can work our airspace management solution in a war fighting sense. We need to be able to monitor the airspace and identify what is out there, and we need all those civil radar feeds. You have to put into place a system to share information between the Airservices Australia TAAATS and our ADATS. In the future, if we got together when TAAATS and ADATS are up for replacement, if we lined both those ducks up and bought one big duck that would obviously be advantageous to all us.

Senator O'BRIEN—I hope it is a bit better than a duck! This question of the attraction for your air traffic controllers: is there pay parity between your controllers and Airservices' air controllers. or are people looking at a better package if they go to Airservices?

Air Marshal Shepherd—When you look at the reasons—and the head of the Defence personnel executive might care to correct me if I get this wrong—why people leave the service, pay is not No. 1; it is down at six, seven or eight. There are lots of other issues—lifestyle, job satisfaction. I suppose I tend to look at the whole package. If you look at just the money, yes, we do not pay as much money as the people in Airservices do. But we offer them an exciting job. They don't get an opportunity to deploy to Baghdad with Airservices Australia. They do not get an opportunity to serve their country in many real and meaningful ways. We have air traffickers right now in Dili assisting with the flow of aeroplanes in and out. You do not get to do that in Airservices.

Senator O'BRIEN—I have great respect for your officers who agree to be deployed to Iraq, but I do not think it would be a selling point for air traffic controllers.

Air Marshal Shepherd—It is, because they do a great job.

Senator O'BRIEN—There may be some air traffic controllers who are in the reserves who may be able to pick that up, but let's not quibble about the campaign you need to use to attract more air traffic controllers. The RAAF Pearce radar services were originally scheduled to be integrated into the Airservices Australia Perth control unit in March this year. This was then extended to early June this year. Will it happen in June?

Air Marshal Shepherd—Yes, it will. In fact, I have just had a phone call; I think it has been delayed by one more week. I understand that there are just a couple of technical issues. We need to finalise the business case so we can expend our money, but it really is just a matter of process. There is no desire not to do it. We look forward to that as the first practical manifestation of the Genesis outcome.

Senator O'BRIEN—It has also been suggested that the Darwin and Tindal approach services will be integrated into the Airservices Brisbane centre by late this year. Is that going to—

Air Marshal Shepherd—That will probably be more towards mid next year. That is certainly our intent in the short term. I will also put in a caveat there that we will need to have a contingency fallback capability out of our EASTROC regional operations centre in Williamstown should we get into a defence of Australia type scenario in the north where we need to be able to move information around by secure networks. The civil TAAATS network is not a secure network. But our intent is to move into the Brisbane centre by mid next year.

Senator O'BRIEN—So there will be the facility for you to subtract your input at a given time without in any way interrupting the other services of the Airservices Australia function?

Air Marshal Shepherd—If you are talking about the EASTROC contingency fallback plan, I would not say 'subtract' our information. It would be to maintain the integrity of our information, and not just air traffic information but information coming from our air defence radars, both fixed on the ground and, in the future, from the Wedgetail platform.

Senator O'BRIEN—So it is just an information control system, rather than—

Air Marshal Shepherd—What EASTROC does for us is compile what we call a recognised air picture—the picture of what is moving in the air in our area of interest.

Senator O'BRIEN—Perhaps you might be able, on notice, to give the committee details of the complete time lines for Project Genesis.

Air Marshal Shepherd—I am more than happy to do that, but Genesis is a work in progress so a lot of those time lines are not exactly fixed yet. As I said at the start, each of those moves need a hard-nosed business case around them. We need to make sure that Greg Russell, from Airservices, and I, from Air Force and representing the whole of the defence aviation environment, go into this with our eyes open and fully aware of the costs involved and the cost benefits. I am more than happy to send across to the committee an update on the Genesis project. Some of those time lines are still being worked out.

Senator O'BRIEN—That would be very good. Once the project is complete, will it be RAAF air traffic controllers sitting in the Airservices facilities who are controlling military air movements, or will it be anyone in the TAAATS centres?

Air Marshal Shepherd—Broadly, it will be uniformed air traffic controllers controlling air movements, be they civil or military, in military air space, and civil controllers will control movements, be they civil or military, in civil air space. But with the flexible use of air space concept that we are discussing and looking at under airspace reform, we will be able to better use the airspace that we have available.

Senator O'BRIEN—With regard to the integration of your systems and the Airservices systems, I was wondering about the impact of integration. You have discussed that in a general sense. The Department of Transport and Regional Services advised me last week:

We have not, as yet, quantified the savings. They will largely be to the defence budget, but I can assure you that they will be substantial.

What cost savings are predicted from the integration of the two systems for Defence?

Air Marshal Shepherd—We have not quantified those savings either. I would be more than happy to have quantitative savings and qualitative savings, of course, in the sense of better job prospects for our air traffickers and our technicians. I think there will be savings in the civil environment as well. We fully understand the motives and rationale for the Airservices Australia organisation. We fully understand their need to make a commercial return on that investment. We have not quantified it. I would rather not give you hard figures here and now. As we work through the Genesis process I think opportunities will be realised and maybe we will have to rescope some specific activities there as the business cases are presented.

Senator O'BRIEN—I take it—and perhaps I am taking it from their answer—that you will be able to quantify the savings you make from this approach and that it will not simply be a case of achieving efficiency but spending the same amount of money, if I can put it that way.

Air Marshal Shepherd—Ultimately we will be able to, but our ADATS is not due for replacement until early in the next decade. So a lot of these quantifiable savings will not be realised until we work through this process. Genesis will be a work in process for a fairly lengthy period of time. We are looking for a longer term strategic engagement with Airservices rather than a short-term expediency engagement. In the Genesis brief that I will send across to the committee we will put in there our estimations. But I stress that utmost in my mind is more an efficiency dividend, the effectiveness of our air traffic control people and their careers and being able to sustain the proper workforce within the Air Force.

Senator O'BRIEN—So how many fewer RAAF air traffic controllers would you predict will result from this integration?

Air Marshal Shepherd—Once again, it is pretty much a work in progress. There are some small figures. We will probably move about 21 or 22 people out of Darwin and Tindal down to Brisbane centre. We currently have a workforce in air traffic that is, as I said at the start, generally unsustainable because we need more air traffickers in peace than we actually do in times of conflict. If we want to focus on expeditionary capabilities, we need to have a workforce that is trained and ready to deploy but that is of the right sustainable size. We are always looking for good air traffickers. Like anything else, when you lose experienced people and replace them with junior people you suffer an experience gap for a short period of time. Once again, I do not want to put numbers on this, because it depends on some of the outcomes

of moving to Brisbane and Melbourne centres, moving Pearce radar to Perth and things like that. But I would be looking to be able to maintain a sustainable, deployable capability that is what I require for operations.

Senator O'BRIEN—So there is a core force of air traffic controllers that you would need, for example, for the maintenance of traffic control capability which is also deployable to different theatres?

Air Marshal Shepherd—That is true.

Senator O'BRIEN—Do you have a base number that you have to maintain?

Air Marshal Shepherd—Part of the baselining activity to start the Genesis point will be to define that. We are currently in that process. I will put that in the brief as best we can now. But we are currently defining exactly what that deployable expeditionary war fighting capability requires.

Senator O'BRIEN—Are you aware of any consultation taking place with civil airspace users about this project?

Air Marshal Shepherd—If you are talking about more the reform of national airspace then that is probably outside of the Genesis specificity and more in the dealings that we are working as the aviation policy group. Currently we are staffing a joint cabinet submission that will go to both ministers on what our recommendations are about the ongoing national airspace reform. Certainly there are a range of consultations going on under that. Recently, at the senior level, Secretary Taylor from DOTARS, Mr Byron from CASA and I—Greg Russell from Airservices was to be there but, unfortunately, was sick that night—held meetings in Sydney with chief pilots of all the major airlines. There will be a scope of consultation across the industry as part of that activity.

Senator O'BRIEN—If there is an established timetable for that consultation I would appreciate it if the committee could be supplied with that.

Air Marshal Shepherd—That will be part of the cabinet submission, so I would rather that went up through the ministers and see about their approval first off.

Senator O'BRIEN—So it is not approved yet—is that what you are saying?

Air Marshal Shepherd—We are still developing that cabinet submission and our recommendations for national airspace reform.

Senator O'BRIEN—Okay. Thank you for that.

Air Marshal Shepherd—That is a pleasure.

Senator MARK BISHOP—I want to talk about some of the announcements by the government in the last budget. I ask that the people who will be answering the questions have before them page 92 of the PBS, table 4.1, and Budget Paper No. 1, pages 10-31, table A5, because I will be asking some questions about those, as well as Dr Nelson and Minister Billson's statement.

The budget announced that an additional \$194 million would be available for recruitment and to retain ADF personnel, and the money would be spent over four years on measures designed 'to grow the military workforce numbers'. Various press statements disclosed that

only \$25 million will be spent on recruitment programs, with the remainder going to retention and completion bonuses for critical trades across the services. Navy will receive \$56 million from this announcement for retention and completion bonuses for their critical trades. Can you advise why Defence is spending an additional \$170 million over four years on retention and completion bonuses for critical trades but you are predicting an increase of only 64 personnel across the ADF? It strikes me as a bit odd. The figure of 64 personnel comes from table 4.1.

Mr Veitch—The \$194 million that you speak about comes from money that would otherwise be paid on salaries if our numbers were at the authorised strength. We are currently about 1,000 under in number. What the government agreed as part of the budget is that we could retain those funds and use those funds on recruitment and retention initiatives in order to grow the ADF back towards its authorised strength. When you say that the numbers are going to increase by only about 64—

Senator MARK BISHOP—That is in column 3 of table 4.1.

Mr Veitch—that increase is what we project will occur in 2006-07. If we were to go further out over the next three years of the program, we expect the ADF numbers to be fully restored inside the next three years. Air Force and Navy expect to recover their numbers over the next two years, but Army expects to take about a year longer. By the end of the four-year program we expect to be back to the authorised strength levels.

Senator MARK BISHOP—You say it will take a full three years for the three services to get their approved staffing levels back to current approved levels—is that correct?

Mr Veitch—That is what we anticipate at this stage. We are beginning to see signs of stabilisation and are starting to grow the numbers. For example—

Senator MARK BISHOP—Does that include the 1,500 people in the new battalion to be relocated to Adelaide?

Mr Veitch—Yes. We are intending to grow the Army by about 1,485 people, from memory, but that is a decade-long program, so it will take some time longer than three years to grow the Army to that strength.

Senator MARK BISHOP—So it will take three years for Army to get back to current levels and it will take another seven years on top of that for Army to get the additional 1,485 people. Is that correct?

Mr Veitch—Because of the way the money is spread for the hardening and networking the Army initiative, the whole program will take us about 10 years to achieve fully, including the relocation to Adelaide.

Senator MARK BISHOP—The permanent force numbers for Navy in table 4.1 show a decline in the next 12 months from 12,800 to 12,784, a decline of 16. Navy is to receive most of the funding under the project, so, firstly, why do we forecast a decline in the 2007 financial year and, secondly, do we anticipate change in the two out years?

Mr Veitch—We have tried to target the most pressing of the critical trades. There are about 27 critical trades, where we are well below our strength. In other words, we are facing separation rates in those trades that are more than the average that we are facing in other

areas. They are the ones that we have looked at initially. Some of the initial money that has been allocated—the \$57 million that you talk about—was in relation to about four or five of the most pressing Navy trades. There are two elements. One is that they needed attention; the other is that Navy, I think, was just a little bit ahead of the game compared to the other two services in getting some proposals forward for consideration. That is not to say that the others have not been attended to. There are currently a range of other proposals being worked up for committee and ministerial consideration. We expect that there will be further announcements made in the next few months.

Senator MARK BISHOP—So you are telling me that the bulk of that \$56 million for Navy is going to be spent in four or five of the 27 critical trades areas but, having said that, we still expect a net decline in the 2007 budget year?

Mr Veitch—Yes.

Senator MARK BISHOP—What about in the two out years: 2008 and 2009? Are our projections for a return to normal staffing levels in Navy or do we anticipate further declines?

Mr Veitch—No, we are expecting Navy to recover its numbers inside two years if everything goes according to plan. We expect to see a turnaround by the 2008-09 financial year. That small decline is only small relative to this year. It must be borne in mind that, as part of the budget this year, the government required that we rationalise our command and control structure. We are planning to save, over the next two years, 241 military positions in the command and control structure. So part of that reduction in Navy reflects that being progressively implemented, commencing this financial year.

Senator MARK BISHOP—Can you turn to table A5, which is on page 10-31 in Budget Paper No. 1. When you look at the figures for the Department of Defence military, you see that the staffing level for 2005-06 was 51,189. That figure is consistent with the figure in the PBS that we were discussing earlier; those figures are identical. When you look at the projected figures for 2006-07, the 2007 financial year, you will see that the figures for Defence go down further, from 51,189 to 51,091, a net decline of 98, which is different to the growth by 64 projected in the PBS. That is a difference of about 170-odd bodies, give or take. Can you explain to the committee that discrepancy between the PBS and the budget paper?

Mr Veitch—I am not sure I could answer that question now but, if I could speculate, it may be that the numbers in Budget Paper No. 1 were an earlier set of figures and did not reflect the budget measure that I have talked about—in other words, the commencement of the rationalisation of the command and control structure. But the numbers that we have in table 4.1 are very definitely the latest planning figures we are working to.

Senator MARK BISHOP—It strikes me as odd that there are two conflicting sets of figures.

Mr Smith—Yes. The other numbers are consistent across the two years, but that one is not. I cannot explain that. I had not seen that.

Senator MARK BISHOP—Mr Veitch, perhaps you could take some advice and get an answer to that.

Mr Veitch—Yes.

Senator MARK BISHOP—While we are in that table, if we go down two lines further we see that there is a really large increase in the civilian employment levels in the Department of Defence. They go from 13,355 up to 14,148, a net increase of 793. In terms of the DMO, which is separately identified, there is a further net separate increase of 194. That is an increase of almost 1,000 bodies on the civilian side; but, as we have identified, there are increasing problems on the military side. Why is there such a significant increase on the civilian side when the ‘pointy end’, as I am repeatedly told, is what matters.

Mr Smith—Let me respond to that first. As you understand, we have an integrated workforce in Australia—not on deployments, of course. In Australia we have both military and civilian people working alongside each other in all of our groups. Something in excess of 12 per cent of our positions in the non-service groups are filled by military personnel. When we have, firstly, a shortfall in military personnel, as we now have, and, secondly, unusually large numbers of people on deployment, preparing for deployment or reconstituting, there is a significant drain on that 12 per cent factor in the non-service groups. To replace that workforce we have had to recruit more civilians, many of them nonongoing, as they say—temporary—and many full time. As well, there is a big throughput of projects as a result of the government’s Defence Capability Plan and, as far as DMO is concerned, to sustain the level of spending needed we need a growing number of project managers and project staff.

Thirdly, in order to achieve what we have to achieve, which you will know well, in the area of the financial statements and our remediation we are having to put in some additional staff, particularly in the logistics command, for instance, and in other areas of the organisation which handle logistics, because there is much to be caught up on there. Mr Veitch can outline some further details there if you wish. I think it would be useful to do so.

Mr Veitch—On page 93 of the PBS we give an explanation of the increase of 793. Overall, the total size of the integrated workforce is lower this year than it has been for a couple of years. Part of the increase of 793 reflects what the secretary says about providing temporary relief to the military workforce—the vacant positions in the non-service groups. If you go halfway down page 93, you will see that we have civilianised 199 positions in this last year. We have provided for 253 for the backfilling of temporary military vacancies. Our numbers in 2005-06, because of the recruitment and retention problems we are having generally, are 102 below our authorised strength and we are planning to recover that next year. We have been provided with an extra 33 positions by government: 20 for hardening and networking the Army and 13 for intelligence and security measures. There are an additional 27 civilian positions for the military justice inquiry outcomes. We have substituted 20 professional service provider positions with more cost-effective civilian employees. The secretary mentioned our stocktaking and remediation financial controls work. For this coming year we have budgeted for another 159 in that area. All up, that is an increase on the Defence side of 793, and there is the 194 on the DMO side that you also mentioned.

Mr Smith—Dr Gumley may also wish to address that issue. As you know, the PBS is presented in two parts this year. Section 2 is DMO.

Dr Gumley—The DMO numbers have gone up by about 200 people—a little bit higher than that—but our budget has gone up in real terms by about 20 per cent. We have a lot of extra projects under way. The Defence Capability Plan is starting to turn a lot of projects into

reality now and, of course, to get the projects under way you have to have the staff to do it. A very good metric from the DMO at the moment is that our value added per employee between 2003 and 2007 will have lifted by over 20 per cent in real terms. That is a very substantial productivity improvement by anyone's standards and it is particularly encouraging in the Public Service.

Senator MARK BISHOP—Mr Veitch, can you explain to me the first two dot points. Firstly, the civilianisation of military positions is up by 199. Does that mean you are pulling out almost 200 positions currently filled by military people for operational or deployment reasons and they are now being filled by a genre of civilians?

Mr Veitch—No, definitely not that. As part of our rationalisation and reform program we have a dedicated program of looking at positions and how they might best be filled. Under our integrated workforce approach, if a position can be best filled by a civilian who will cost on average about \$26,000 to \$27,000 less and can perform the same function, it is more cost effective for us to do that. These are positions that we have judged that over time can be done by civilians just as effectively, and we substitute by reducing the numbers on the military side and increasing the civilian staff. The second dot point covers the point that you were making, and it is more a temporary measure. As the ADF recovers its numbers over the next two to three years, as I have mentioned before, we would expect these positions to revert to military positions and for the civilian numbers to decrease in that area.

Senator MARK BISHOP—So you have pulled out 253 people from a civilian role to put them into vacant military positions. Is that 253 then subsumed in the figures in table 4.1 in terms of the permanent force? Do they get added in there as well?

Mr Veitch—The table reflects that the military numbers are down compared to the authorised strength, yes. In fact, there are more than 253. We are only substituting 253 this year, because we have difficulty in substituting all positions as it is a fairly tight labour market. That number reflects a reduction of 253 and more on the military side and an increase on the civilian side, but if you were to cast forward in a few years time you would see that wash through and reverse out.

Senator MARK BISHOP—But is the figure of 51,253 in column 2 of table 4.1 inclusive of the 253 that are being backfilled from vacant military positions?

Mr Veitch—No. The 253 are reflected further down the table under the civilian numbers of 14,148. The increase is reflected as part of the 14,148. To put it another way, the 51,253 figure in the top part of the table is currently about 1,000 below our authorised strength.

Senator MARK BISHOP—So the figure for the APS of 14,148, showing an increase of 793, includes the 253?

Mr Veitch—Yes, the 253, and over time that 253 will wash out as military numbers increase back to their authorised strength.

Senator MARK BISHOP—When the people who have been relocated are no longer needed, they will go back to their prior positions—is that correct?

Mr Smith—The 253? It is not to say that the civilians were in prior positions. It means that they have been temporarily recruited.

Mr Veitch—Yes. Most of the people we recruit in that category are what we call ‘non-ongoing’, so we bring them in for two or three years and then we have an ability for them to move to other positions or to move out of the organisation altogether.

Senator MARK BISHOP—Okay. The government has set aside some \$68 million in 2006-07 for recruitment and retention initiatives. I am also advised that that measure provides for a temporary increase in civilian staff in non-combat roles, including management and personnel services, according to the press release from the minister. Will any increase in civilian staff numbers in the department and DMO be met from this source, the \$68 million?

Mr Veitch—Yes. That is exactly for that. That is part and parcel of the 14,148 that we have just talked about.

Senator MARK BISHOP—So the entire amount of \$68 million will go to funding the increase of civilian staff?

Mr Veitch—That is right.

Senator MARK BISHOP—Is that in just this budget year or the next three years?

Mr Veitch—The \$68 million is in respect of this budget year but it forms part of the total of \$194 million that I have talked about that is spread over four years.

Senator MARK BISHOP—Can I ask you now to turn to Budget Paper No. 1, table No. 20.

Mr Smith—Do you have a spare copy? We usually work off the PBS.

Senator MARK BISHOP—The budget papers have a bit of influence too, I think.

Senator HOGG—Just a bit. We will see if we can rent you one.

Senator MARK BISHOP—Senator Hogg will ask a couple of questions while we are getting a copy made of table 20.

Senator HOGG—I am curious about page 95. I do not have the corresponding page for you, Dr Gumley. Table 4.3 outlines employee expenses. It talks about permanent salary, allowances, superannuation and leave. The same sort of table would be repeated for your section, Dr Gumley, I would imagine. That is an increase of \$164 million, or 3.9 per cent, over the projected result. Then you detail housing, health services and other expenses, including fringe benefits. What are the ‘other expenses, including fringe benefits’?

Mr Veitch—The fringe benefits tax is the main element of that. In fact, that would take up about 95 per cent of that category. There is a small increase in that category of the budget that relates to fringe benefits tax. That in turn relates directly to the housing budget, where the cost of the rental we pay the DHA for housing has increased, and that has a consequent impact on the FBT estimates. It is a small impact of about \$1.3 million in this coming year.

Senator HOGG—The next question I have is in relation to the overall expenses that you have outlined there: \$6,609,000. Does any of that \$6,609,000 include performance bonuses that are paid to officers in the department? Is that budgeted for at any stage?

Mr Smith—It includes an element of what we call salary progression, which, for most of our officers, we use rather than bonuses. But a few of our senior staff are on performance bonuses and that would be included in there.

Senator HOGG—In the \$6,609,000?

Mr Smith—To the extent that that is an estimate then there is provision for it.

Senator HOGG—Where would it be included in the other categories?

Mr Veitch—It would be included as part of the salary allowance, superannuation and leave line.

Senator HOGG—How many people are subject to a performance bonus, then?

Mr Smith—I do not have a number before me for the people who are subject to a performance bonus or money at risk, as you would call it, rather than progression.

Senator HOGG—A piece of paper is being passed around here. That is not it?

Mr Smith—No, that does not help it. It is a small number. I will take it on notice. It is more people in DMO than in Defence proper, but we will get it between us.

Senator HOGG—I suspected that it might be. I was trying to find out. I was not after the names of the people. How many people received a performance bonus and at what level are performance bonuses paid? I would imagine that it is probably one star and above.

Mr Smith—Yes, and it is not all of them. As I said, we will produce that data for you.

Senator HOGG—Yes, I am just making it clear for you. Also, can you give the amount that is budgeted for in the figures that are before us? I would imagine that it is far more significant in DMO than it is in other areas.

Mr Smith—That is correct. As we have recruited to the culture change in the DMO, we have deliberately focused on performance in that way. We will produce those figures for you.

Dr Gumley—In DMO there are probably about 20 or 25 people on performance bonuses. They are typically set at a maximum of either 10 per cent or 15 per cent of base salary, earning up to that figure. Most of the people are either EL2 or equivalent project managers or band 1 and band 2 APS.

Mr Smith—But you have asked a specific question and we will get an answer for you.

Senator O'BRIEN—All right. Thank you.

Senator FIERRAVANTI-WELLS—Just in addition when providing that answer, could you also specify what triggers the performance bonus—what are the conditions and does that include stages of contracts? Can we have a detailed—

Senator HOGG—What are the milestones?

Senator FIERRAVANTI-WELLS—Yes, thank you, Senator.

Senator HOGG—Or the millstones?

Senator FIERRAVANTI-WELLS—The angle that I am coming from is that obviously that then affects your views in terms of performance appraisal of different contracts and scheduling of different contracts. That is the angle that I would like you to provide details on.

Mr Smith—We do not actually hold our officers responsible for the failure of companies to deliver. It is for their management of the contracts that we hold them responsible. But we will respond to you.

ACTING CHAIR—You have taken that on notice, Dr Gumley?

Dr Gumley—Yes.

Senator MARK BISHOP—You have a document from page 6-26, which is table 20 from Budget Paper No. 1. That table 20 is headed, ‘Estimates of net capital investment by function,’ and it outlines a whole range of departments. Firstly, I presume, as the title suggests, that is the amount of net capital to be spent on a range of projects, in particular the departments that are listed there. Why in that context is Defence down \$211 million in the 2006 financial year, a further \$10 million in the 2007 financial year and a further \$234 million in the 2008 financial year? Does that mean that there is a net capital return to government? What does this table tell me?

Mr Veitch—This table is a little bit confusing to a layperson like me. We talked about this in previous estimates committees. The budget for Defence is presented in about three different ways. Under some of those methodologies the investment capital equipment is expensed rather than brought onto the books as an asset. This is a presentation of the capital investment by function using the GFS, with SME means special military equipment being expensed.

Senator MARK BISHOP—Go slowly!

Senator HOGG—Yes, I think we need to get into real language. It seems that we are going into mumbo-jumbo.

Mr Veitch—What I would rather do is take you to page 58 of our yellow book and then I can explain the real dollars in our investment program for you.

Senator HOGG—Don’t you trust Treasury for some reason?

Mr Veitch—I always trust Treasury.

Senator HOGG—You have gone to the PBS twice now to defend yourself!

Mr Smith—That table 20 is a table that I do not think I have ever hesitated over, but I just do not understand why we are negative, given what we are spending, while everybody else is positive.

Senator MARK BISHOP—When you look below table 20 you see there is a description of the net capital investment for all of the other line departments. The point is made that the net capital investment in the 2006 budget year is \$881 million, and that is going to be spent on the sorts of things you would assume it would be spent on: construction of the Christmas Island Immigration Reception and Processing Centre, various other construction projects, investment by ANSTO in a new nuclear reactor, acquisition of land and refurbishment, and all the sorts of things that government departments would spend capital on in purchasing assets. But, according to the table, over the next three years Defence has a decline in capital outlays of almost \$500 million. That seems so counterintuitive to me, according to the programs I am familiar with. What does ‘estimates of net capital invested by function’ mean?

Mr Veitch—If we go to page 58 of our yellow book—

Senator MARK BISHOP—I am happy to go there in a minute—I am not trying to put you off—but that has been put in there for a reason. It is attempting to disclose something, I presume. What does it disclose about Defence?

Mr Smith—Our CFO, Mr Prior, who has come from the Department of Finance and Administration, may be able to contribute to the answer on this esoteric subject.

Mr Prior—I could go on for some length to talk about GFS. This is a table constructed by the department of finance in compiling the GFS, the government finance statistics, numbers. The primary documents in the white books that you refer to are based on the GFS framework. Defence numbers in the yellow books are put together on the AAS, the Australian accounting standards, framework. The conversion from the Australian accounting standards to the government finance statistics standard is done by Finance. This table is constructed by them to try to indicate the net capital investment flows from both the disposing and acquiring of capital, as defined by the GFS framework.

It is a table that we in Defence do not get deeply involved in, as the department of finance pull the numbers together to construct the table from information they glean from our data. With respect, how to unravel and find out the precise details of what comprises the line item we are looking at would be a question better put to Finance; they could unpack the components that they pull together to get to that point. But the table indicates the net capital flow, as defined by GFS—capital in and out. It is not just expenditure, as such. It is not just outflow.

Senator MARK BISHOP—But capital outflow is the return of capital by the line department to government.

Mr Prior—No, this table represents the capital flows from the government, or the public sector, to and from the private sector. It is a GFS construct of flows between those two—

Senator MARK BISHOP—To and from the private sector?

Mr Prior—Between the general government sector and the broader economy of the private sector. It is a GFS constructed table for the whole of government. It is trying to indicate the capital flows to and from the general government sector to the private sector and back.

Senator MARK BISHOP—General flows to the private sector?

Mr Prior—General government sector to the private sector.

Senator MARK BISHOP—And general government sector to the private sector means spending by the line department on capital acquisition items, such as ships, planes and buildings?

Mr Prior—It is a net flow, both in and out, from the sectors.

Senator MARK BISHOP—Why is the net in the negative to the tune of \$500 million?

Mr Prior—That is what I am saying. We are not a party to the construction of that table. We do not get involved in how they pull those components together. For instance, if Defence were to dispose of or sell an asset, it would be a flow of funds in from the private sector to the general government sector; if we were to acquire, it would be the other way. As I say, to get precision on what constitutes the elements of that number—

Senator MARK BISHOP—On this GFS, does the Department of Finance and Administration conclude that you are selling off more assets and returning more proceeds to government than you are being provided for in capital transfer from government to purchase new assets? On your explanation—

Mr Prior—I have not got the table.

Senator HOGG—Defence is virtually the only department in the negative.

Mr Prior—That is right.

Mr Smith—It is a mystery. If you go to 58—

Senator HOGG—If it is a mystery to you, Mr Smith, it is an even bigger mystery to us.

Mr Smith—I can assure you that there is nothing in that that drives our business. We are all in here. On page 58, the good news is set out.

Senator HOGG—I do not know about that. You are a little bit presumptuous there. One would have thought that before they stuck this in Budget Paper No. 1 they would have at least consulted you as to your view on whether this was a true and reasonable reflection of the transaction of your business. Otherwise, it comes to people such as us—and there are more people than just us who are silly enough to read the budget documents and those other people might equally come to the same conclusion. Given the size of the Department of Defence, it would then become quite reasonable to ask the questions that are being asked now. I know that you are not saying that they are not reasonable questions; it is just that it seems that you have no explanation.

Mr Veitch—The best thing we can do is get something from Finance which we can provide to the committee on what the construction is.

Senator HOGG—In English, not in mumbo-jumbo form.

Mr Smith—We will not ask Mr Prior to write it out, then.

Senator HOGG—We trust Mr Prior; he has seen the light and come to Defence.

Mr Veitch—We explain our investment program in quite precise terms on page 58, if you would like to—

Senator MARK BISHOP—This is just your spend in the current year and the out years, isn't it?

Mr Veitch—That is right.

Senator MARK BISHOP—I can understand that.

Mr Veitch—There is nothing negative in that.

Senator MARK BISHOP—No, there is not, is there?

Mr Veitch—In fact, the investment program increases by \$1.3 billion in this coming year.

Senator MARK BISHOP—Is that from \$3.9 billion to \$5.1 billion—the total capital component? The fourth bold heading?

Mr Veitch—That is right. If you think of it in terms of the total investment, including the operating component of our investment program, it goes up by \$1.265 billion.

Senator MARK BISHOP—That is what we thought.

Mr Veitch—That includes about \$800 million for the C17s.

Senator MARK BISHOP—If you do not mind, can you take on notice the provision of an explanation of table 20 in Budget Paper No. 1?

Mr Smith—We will all be interested in that.

Senator MARK BISHOP—While we are there, I have a couple of other curly ones for you. With the budget figures in the PBS, the Army figures are at page 146, the Navy figures are at page 132 and the RAAF figures are at page 157. However, the PBS does not provide anywhere a complete budget for the three services. The tables at those three pages do not contain any budget allocations as income. The question therefore is: why not? Could a complete explanation be provided in the future so that we can do a total performance assessment of each service as opposed to trying to extrapolate figures from the corporate entity as a whole?

Mr Veitch—What was the first page?

Senator MARK BISHOP—Page 146—the total budgeted cost to government, outcome 3, Army capability for the defence of Australia. The other two are for the Navy and the RAAF. They do not show any budget allocations as income, so you cannot get a picture of what is going on.

Mr Veitch—We receive our revenue at a higher level. What we have tried to show there is the cost of the Army capability, including the constituent elements that flow to it from the other enabling groups. If you like, that provides an outcome/output view of Army capability. In other words, in this year we assess that the cost of running the Army, including all other elements of the budget—including the DMO and the corporate service and infrastructure group and other groups—will be \$5.9 billion.

What we have shown separately in the document, which I think may answer your question, is how the group budget allocations contribute to each of our six outcomes. On page 110, we have a one-page matrix with the group budgets down one axis and how they contribute to our six outcomes across the other axis. So, using the Army budget as an example, \$3.4 billion is directly allocated to Army but the total cost of running the Army capability, including contributions from other groups, is \$5.9 billion.

Mr Smith—Can I say that that table is a very succinct summary of the way the organisation works, because it shows the money that is directly attributable to each of the services then the money that other groups spend in support of that service.

Senator MARK BISHOP—So that is the whole picture in table 5.e?

Mr Smith—Yes.

Senator MARK BISHOP—Is there a table that aggregates the budgeted costs to government of the three services and the other three outcomes in the same form as, for example, table 5.2.1, on page 132? It is the same for the Navy and Air Force, in that you have a range of income headings and operating expenses but it has a different set of headings to table 5.e and presumably is not directly comparable. Is there a table that shows me the total

budgeted cost to government for the entire ADF in the same form as those RAAF, Navy and Army tables?

Mr Veitch—I think the only difference between the tables relates to our own-source revenue, so the figures would be close. If you add the own-source revenue, you would get the total picture.

Senator MARK BISHOP—But the series of line items in table 5.e, ‘Group contributions to defence outcomes’, are quite different to the line headings in the other three tables, ‘Total budgeted cost to the government’. I am asking if there is an aggregated table in the PBS or the budget papers for the budget figures of Army, Navy, RAAF and other outgoing areas.

Mr Veitch—There is table 5.c on page 107.

Mr Smith—If we could build a three-dimensional table or logarithmic table, that would be the way to show this, but we cannot.

Senator MARK BISHOP—This is a variation—

Mr Veitch—What we are required to show in this documentation is the income statement for each of our outcomes, which we have and which you have correctly alluded to, but we are not required to show that by group. We have tried to add some information with that group table that I showed you to give you a picture of how our budget is built up from groups and attributed to our various outcomes.

Senator MARK BISHOP—Yes, I understand the process. I think table 5.c might well answer my question. I will think about that and come back to you.

[2.40 pm]

Senator MARK BISHOP—Thank you for that. Could we turn now to the cost summary for outcome 7, Superannuation and housing support services for current and retired defence personnel, and table 5.7.1, which is headed ‘Total budgeted price to the government’. It seems rather odd or anomalous that other administered revenues appear here. I take it these revenues include interest on bank accounts, interest from the US and foreign exchange profit and loss. Why are they accounted for here and not in chapter 2, on resourcing in total? I will not say they are buried down here, but why were they put down here? I presume it is a fairly significant sum.

Mr Veitch—Sorry, I am not sure I have picked up the intent of your question.

Senator MARK BISHOP—In output 7.3, Other administered revenues and expenses, includes interest received on official bank accounts maintained by Defence to support its activities, interest received from the US government on foreign military sales advances, UN revenues and receivables, and associated net foreign exchange losses and gains. Why is that included here in the table on superannuation and housing support, and not in a more appropriate place in the total budget documents?

Mr Veitch—What we try to do with outcome 7 is show the totality, because it is an administered item—revenue and expenses. It is a self-contained document, whereas with the other six outcomes we are only showing own-source revenue and our expenses. It is an

attribution of our expenses to make up the price of the output, so it is a slightly different construct of the table.

Senator MARK BISHOP—Yes, but losses and gains on foreign exchange, interest from domestic accounts and interest from accounts maintained for progress payment on projects from overseas are serious sums of money. Why have you lumped them in with superannuation and housing support? If I wanted to find out what we are doing with all those accounts in administered revenue, I would not have thought in a million years to go to the superannuation table.

Mr Veitch—This is an administered item, so we show the totality of the function, whereas the other six outcomes come to us as departmental funding and we are not permitted to retain the proceeds of those. They go back to government; therefore they would be shown elsewhere in the budget documents, not against each of the six outcomes.

Senator MARK BISHOP—What have foreign exchange losses and gains or interest on bank accounts maintained in the United States or the United Kingdom got to do with military superannuation benefits, housing subsidies or retention benefits? Maybe Mr Prior can come forward and tell us. Do you know? My question is, why are administered expenses lumped in with superannuation and housing support?

Mr Prior—Because they are all administered items. They are not all of the same typology, except that they are administered rather than departmental. The system that is used in government budgeting classifies expenditure and revenues as either departmental—that is those items that are under the control of the department—or administered, which are those items which are managed on behalf of government. There are different budgeting rules around those two different classification types. What you see before you are those items which are administered in their classification type, so it is not to suggest that superannuation gives rise to foreign exchange; there are just different types.

Senator MARK BISHOP—So the title of that table is perhaps a bit misleading.

Mr Smith—I think that is right.

Mr Veitch—I can see the intent of the question now. At the top of page 172, you will see that that outcome 7 is broken into three separate elements: one is superannuation, another is housing assistance and the third is for other items. They are the sorts of things that you have just been talking about. They are all lumped in one ‘other items’ category.

Senator MARK BISHOP—I understand the explanation. I just make the point that there might have been a more appropriate heading for that table. Say I wanted to find out the detail of foreign exchange gains or losses, interest on accounts or interest on overseas accounts. Are they disclosed somewhere in the PBS?

Mr Veitch—Yes, they are, but I would probably have to get someone to point me to where they are. We definitely disclose those. Essentially, the foreign exchange gains or losses are generally fairly small. I think they average somewhere between plus and minus \$20 million a year. Essentially, they come about from variations—

Senator MARK BISHOP—I am not asking for an explanation. I just want to know where the detail of those sorts of administered revenues are disclosed in the PBS. Is it in chapter 2, Resourcing? That would be the logical place.

Mr Veitch—If you turn to page 221, you will find that, about a third of the way down the page, there is a net gain on foreign exchange, and we are budgeting that to be zero. Part of the reason for that is that we cannot predict with any certainty whether that is going to be a plus or a minus during the year. We find that that can fluctuate throughout the year and, given the size of the business of our overseas transactions, we generally find that falls within the range of plus or minus \$20 million. We have found that the safest bet each year is to budget for zero and then report the actual—whatever that turns out to be.

Senator MARK BISHOP—At the top of table 7.1, it has ‘Revenue from Government, \$16 billion up to \$17 billion; ‘Goods and services’, \$258 million to \$530 million; and ‘Other Revenue’, \$228 million down to \$65 million. What is that ‘Goods and services’?

Mr Veitch—That comes about from the stores and equipment that we sell or the proceeds we get from the sale of those on disposal. It also comes about from proceeds that our own people pay into the system as their contribution to their rations, quarters, housing and those sorts of things. We term those two line items of \$530 million and \$65 million as own-source revenue.

Senator HOGG—What about property?

Mr Veitch—Property would fall into the ‘Other Revenue’ category. We find that the majority of the proceeds we get from the sale of properties goes back to government, but net of the sale costs that we incur in selling those properties.

Senator MARK BISHOP—The net gain on foreign exchange shows zero. Is that a policy call by the accountants not to disclose gains or losses on an annual basis, or are there no gains or losses?

Mr Veitch—No, it is a policy call by me, because I have found that I cannot accurately budget for it. As I said, in the scheme of things it is usually no worse than plus or minus \$20 million, and I find that if I budget for a plus it will turn out to be a minus. I just cannot predict the exchange movements. So I would rather take a middle-of-the-line approach, and it will fall somewhere either side, and then we adjust it in the estimates and report the actuals.

Senator HOGG—I am not going to ask you for the winner of the Melbourne Cup.

Senator PAYNE—I have a question I flagged earlier about financial training. It is perhaps not in the budget summary area, but it is in the overview area and probably best directed to Mr Prior.

Mr Smith—I will begin. We have found that, firstly, because of our own challenges in having to improve our act in financial management and, secondly, because there is a very tight market in that area, we have had to launch very significant financial training programs of our own, ranging from encouraging people to take up their CP and CPA qualifications to the kind of financial methodologies needed in day-to-day work. As at the end of March, I think, we put some 9,178 people through varying levels of financial training courses—

Senator PAYNE—You have not turned them all into CPAs, have you?

Mr Smith—No, but we have had to encourage people whose qualifications might be lapsing. Mr Prior can detail that. It is a very significant skilling program which our staff have needed.

Mr Prior—As the secretary said, until March in the year to date we have put some 9,178 people through various training programs within the department. The training programs that I refer to are finance related. Dr Gumley may also want to refer to the training programs that take place in DMO. For financial business training, which is the area I am concerned about, the 9,000-odd people go through training programs about financial management training and the use of financial literacy with regard to our financial systems, our computer systems. There are also training programs directed at our senior people in terms of their responsibilities as managers of finances within the department and their responsibilities under the various acts of parliament, regulations and so on. As the secretary said, we have quite a number of training programs. We also support—

Senator PAYNE—Before you go on, who provides the ones that you have already referred to? Are they externally or internally provided?

Mr Prior—It is a combination of both. We outsource some components of our programs, but we also do them internally. We also use e-learning. We have put quite a significant amount of effort into computer training. Regarding the e-learning space, well over 3,000 people have made that facility available to themselves to train as well. As the secretary referred to, we also support individuals who are doing their CPA or ACA qualifications. We have programs in-house to support them through that training, but of course that training is provided by the various accounting bodies.

Senator PAYNE—Of the 9,178 individuals that you referred to, are they mostly civilian members of the department? How does that number break down?

Mr Prior—I do not have that breakdown in front of me.

Senator PAYNE—Could you get that for us on notice, please?

Mr Prior—I certainly could.

Mr Smith—There would be quite a few military people, particularly for the higher level courses.

Mr Prior—Indeed.

Senator PAYNE—I am interested in the balance. Mr Prior, I interrupted you. You were going to say something else.

Mr Prior—I was just going to say that, as the secretary referred to, we see quite a few uniformed people at those courses and the feedback we get from them is very positive. Certainly for the senior courses that we are running, the senior officer training—and I present to that—I see quite a number of military people and the feedback is extremely positive. They find it extremely useful to gain a broad understanding of the financial framework and how the activities that they are involved in, with regard to financial management, fit into the FMA Act and the other regulations.

Senator PAYNE—When you are outsourcing, what sorts of providers are you using?

Mr Prior—Again, it depends. It tends to be small training organisations in and around Canberra, to some extent. We also utilise the facilities at the Canberra Institute of Technology. I recently visited one or two of the courses that we sponsor at the Canberra Institute of Technology. I talk to the students and encourage their attendance. They find that quite beneficial as well.

Senator PAYNE—On notice, can you provide the committee with a list of outsourced providers, please?

Mr Prior—I can.

Senator PAYNE—Is the number in excess of 9,000 meeting the department's expectations or do you have much further to go?

Mr Prior—To compare it to the comparable number for the full year 2004-05, 3,769 people went through courses that we offered last year, and there were 9,000 to March this year. There is clearly a demand. We are continuing to look at opportunities to provide more training as required. There are 90,000 people in the organisation, many of whom are involved in financial management in some way, so we will continue to look at opportunities to provide training to those people. I must say that, as often as we run courses, there does not seem to be a lack of people wanting to participate.

Senator PAYNE—In the courses that you are providing are you also giving participants the opportunity to pick up skills in auditing or, at least, in recognising what auditors are looking for?

Mr Prior—Indeed we do run those sorts of courses. When I present them, I certainly make a point of talking to participants about what it is the auditor is looking for, what the auditor's responsibilities are and the sorts of things that we need to do to ensure that we are up to audit standard, so to speak. I recall that, soon after I joined the department in January, we ran a course on audit expectations; it was run by the Institute of Chartered Accountants, if my memory serves me correctly. So we do cover those aspects.

Mr Smith—And, certainly, at the higher-level courses, people from ANAO—either the Auditor-General or the Deputy Auditor-General—come along and present to our people.

Senator PAYNE—I was going to ask about that.

Mr Smith—People get a chance to ask questions such as 'Why do you go this way?' or 'Why do you do that?' That has been very helpful at the one-star and above level.

Senator PAYNE—When you joined in January, Mr Prior, did they warn you about estimates?

Mr Prior—No, they did not.

Senator PAYNE—That is unhelpful for you. A warning would have been nice.

Mr Prior—I am accustomed to estimates, from my time in Finance.

Senator PAYNE—Mr Prior has dobbed in Dr Gumley in relation to training matters. What is DMO doing, particularly on acquisition and project management skills?

Dr Gumley—We are doing a lot of work at the moment. Picking up on the financial theme, one of the deficiencies we have found in DMO is, perhaps, a lack of business acumen. If you are going to be dealing with the private sector on, roughly, \$8 billion or \$9 billion worth of contracts a year, you really need to have a bit of business acumen in the people who are doing all those transactions; so we have set up business acumen courses.

There have been 23 courses run so far, and 538 of our staff have been through them. There is another 525 to go through in the remainder of this year. The intent is to get several thousand DMO staff understanding how the private sector thinks, how a contract is made, what can go wrong in a contract and what the sources of revenue in a contract are, so that we can get better value for the taxpayers' dollar in making sure it is, intellectually, an even playing field when we are doing this large amount of contracting.

Senator PAYNE—Who runs the business acumen courses? Are they internal, outsourced or both?

Dr Gumley—A bit of both. As you are aware, we have recruited a number of senior private sector executives into the DMO. Each of the courses is run by a senior person—mentoring, helping and sharing their experiences—and then we have a range of external providers who give the more detailed information. It is a mixture of internal and external.

Senator PAYNE—In terms of building the sorts of skills in dealing with contracts that you are talking about, what sort of feedback are you getting from the private sector on how useful that is for them in their dealings with DMO?

Dr Gumley—We are getting positive feedback. I think the private sector—certainly, the executives in the private sector I have talked with—are pleased that when they sit down for a negotiation or a discussion we can talk the same language. Enabling both sides to understand each other's point of view has been very important to getting the dialogue going between the private and public sectors.

Senator PAYNE—On notice, can you provide the committee with a list of external providers, please?

Dr Gumley—Yes, we can provide a list of providers. One of the more interesting things we have done this year is set up a thing called the DMO institute, which is run by DeakinPrime, of Deakin University. We are putting most of our courses under that institute, and we are building up a range of courses not just in business acumen but also in a lot of other areas.

Senator PAYNE—Like what?

Dr Gumley—Project management. We have a catalyst for a transforming leaders course and an emerging leaders course. It is a gradual building up of people's confidence as they work in more and more difficult areas.

Senator PAYNE—You said 538—

Dr Gumley—Yes, 538 people have done the business acumen course. Over and above that, we have the project management training framework, and that has been a very interesting story indeed. When I got to DMO about 27 months ago, there were 10 certified project managers in the DMO. We have now got that up to about 325, with another 200 or so in

training at the moment. There is a range of project management qualifications you can have. You can start off with small projects and work your way through to the very large ones. We are treating it virtually as a separate career stream in DMO. Project management is core to delivering capability on time and budget, and you only get that when you have enough project managers under training, and that is what we are doing.

Senator PAYNE—What is the incentive for a member of your staff to take up a project management or business acumen course?

Dr Gumley—The business acumen course is general education. People find it very interesting to understand how business truly works and it enables them to do their jobs better. It might be a little draconian but, if you have not got your project management certification, you are not going to run a project. We have made it compulsory. Given that DMO is one of the largest project management organisations in the country, it makes it very hard for staff to do well in DMO if they have not got their certificate.

Senator PAYNE—You said that there are 538 currently and 525 to go this year, but you want to move to a point where several thousand, at least, have been through the business acumen course. What is your time frame to achieve that?

Dr Gumley—We find that, because we are putting in so much internal effort and having coaching by our senior leadership in DMO, there is only so much that we can do. The maximum we can do in a year is about 1,000 people. We would run out of time to do our core job. It is a big effort from our executive team to do as much coaching as they are doing.

Senator PAYNE—Over two or three years you think you will—

Dr Gumley—Over three years I hope to get up towards the 3,000 mark.

Senator HOGG—You mentioned that you have a career stream there. Who does the career management within DMO—or is that done externally?

Dr Gumley—It is done internally. We have the smallest projects—the minors—at what we call the ACAT5 level, then you work up to the very biggest projects, like an air warfare destroyer, which is at the ACAT1 level. There is a set of certification you have to do. You have to do courses, you have to have experience and you work your way through to the bigger projects.

Senator HOGG—But do you have people who manage the careers of individuals within DMO? There is a career management path in the other side of Defence.

Dr Gumley—No, we do not have a formal career management section. We have a people development section in the organisation, but we do not take every individual and map out their career for the next 10 years. We believe in people being self-starters. We give them the clear signals that they will need to do certain things to get the promotions and the best jobs, and then we use management by merit selection of those who have achieved the certificates in giving the best jobs.

Senator MARK BISHOP—In response to Senator Payne's question you used the word 'certificate'. Is this project management course that people are doing through Deakin of a higher level than a certificate?

Dr Gumley—There are a number of ways that you can get to the senior levels. For example, to get to the ACAT2 and ACAT1, there are Master of Project Management courses. It is a competency standard, and that is why I called it a certificate. You get your piece of paper once you have completed it.

Senator MARK BISHOP—It is not like a pre-diploma certificate from TAFE or something like that?

Dr Gumley—No, there is a series. It is true that at the lowest levels the courses are much simpler than when you are doing a Master of Project Management at the most senior levels.

Senator MARK BISHOP—So you are really just introducing line personnel to some of the basic concepts of accountancy and finance in contract management and those sorts of things?

Dr Gumley—No, that is in the business acumen course. The project management course has a much more defined syllabus that they have to complete to get through. There are exams and tests and so on to get there.

Mr Smith—I would say, if I may, that the three skills most in demand in the Public Service generally are financial management skills, project management skills and contract management skills. We are all constantly caught out by failures in that area. I have said historically that I thought we were underprepared for accrual accounting, and this is one of the ways in which we were underprepared. We are playing catch-up with that. You asked before what the incentives are. I was distracted and I did not hear Dr Gumley's reply. But one of them certainly—and we know this from the negotiations we have had with our staff and unions for the certified agreement—is that people want to feel that they belong to an organisation that is succeeding. They feel that, if they can acquire those skills, they will get there. That has worked particularly well with the staff in DM0.

CHAIR—Before we go to the Hawk trainer, can I just raise, as foreshadowed, the matter of Frontline and the Army-Air Force canteen. Who has that?

Mr Smith—That is Mr Prior. The chiefs of Army and Air Force may want to speak on it.

CHAIR—My questions are relatively simple. Why have we been late with our annual reporting for the last two years? Also, the numbers look a bit problematic in terms of the deficit, the bad debts and write-off. What is happening with Frontline?

Mr Prior—With regard to the Frontline annual reports, with respect, the submission of their annual reports is the responsibility of Frontline's board. I cannot really offer a view as to why they are late with their annual reports.

CHAIR—Who is the board?

Mr Prior—The board comprises eight members—four commercial members and four senior level Army and Air Force members.

CHAIR—What does 'senior level' mean?

Mr Prior—Brigadiers and air commodores.

CHAIR—How often do they meet?

Mr Prior—I do not know how often they meet.

CHAIR—Are there minutes of the board's meetings?

Mr Prior—I would imagine there would be.

Mr Smith—The Frontline board reports directly to the minister. When the Uhrig reforms take effect on 1 July—

Mr Prior—Post the Uhrig reforms—that is, once the minister for finance has approved the Uhrig reviews, which would be essentially around 1 July—

Mr Smith—they will then report to me and to Mr Prior quarterly.

Mr Prior—there will be a parallel reporting process.

CHAIR—So we have an operating deficit in excess of \$1 million for last year. What does that mean? Are we selling goods at a loss? Is it a matter of bad management? What is the story?

Mr Prior—Again, I am a bit cautious in responding to this question because, as I said, the board has a responsibility to attend to the operations of that organisation. It may be inappropriate for me to second-guess the board as to what is driving their business and causing the outcomes that you are seeing in the annual report.

Senator MARK BISHOP—Haven't they got a senior officer or an officer in charge who reports to the board?

CHAIR—A CEO?

Senator MARK BISHOP—Who is he? Who runs the show?

Mr Prior—The chair of the board. It is like a normal board. The board has responsibility for that organisation.

Senator MARK BISHOP—Yes, but who is the line manager or the CEO? Who runs the show?

Mr Prior—I do not have the name in front of me. I have the names of the board members, but I do not have the name of the CEO. I think there was an acting CEO for a period of time.

CHAIR—Are you suggesting that, with the Uhrig report, there will be a change such that it comes through the service chiefs or the secretary? What is going to happen into the future?

Mr Prior—In essence, the aim of the Uhrig review was to review these bodies—not just Defence bodies but also bodies across the government—and to make recommendations about their governance arrangements. As a result of that, there is a process that all agencies have been going through with bodies that are part of the portfolio. In Defence's case, with Frontline, like nine other bodies that have been reviewed, there will be a parallel reporting process whereby financial information will regularly come to the secretary and to me.

CHAIR—Where does the appropriation for Frontline come from now?

Mr Prior—I do not believe Frontline receives an appropriation directly.

CHAIR—Who buys the goods for it? It is a retail facility, isn't it?

Mr Prior—That is correct.

CHAIR—Who buys the goods?

Mr Prior—Frontline buys the goods.

CHAIR—Where do they get the money from?

Mr Smith—From sales. They are a business.

CHAIR—So they have a carry-over of profit.

Mr Prior—That is correct.

CHAIR—According to the figures I have, they are making a loss.

Mr Smith—Yes.

CHAIR—That is of concern.

Mr Smith—We have had to provide support for them over the last year and a half or so, and we are working with them to assess what the future model has to be to enable them to operate without depending on us. Of course, the problem here is that the patterns of living for people have changed. We used to use Frontline a lot. It is now just as easy to go downtown and buy whitegoods there as it is to buy them on the base. That said, there are some areas that CAF and Chief of Army will say are utterly dependent on this, such as Tindal and forces deployed overseas, so we do not want to let it go.

CHAIR—So Frontline is the equivalent of an American PX type situation.

Air Marshal Shepherd—In a very conceptual sense, but in a very small way. To put the cultural context that the secretary was talking about, many of our people lived on base a decade or two ago. There were lots of married quarters on base and there were lots of single, living-in members. As our members in uniform have reduced over the years and as our DHA housing has moved mainly off base—in fact, nearly exclusively off base—Frontline do not have the captive audience they once had. Nevertheless, they provide a service in remote areas. I was in Tindal a week or two ago. They run a little 7-Eleven type store in Tindal. If you want to buy a bottle of milk or a newspaper at Tindal, you have to drive the best part of 20 kilometres to Katherine, which is in itself a small town.

CHAIR—So they perform a vital service?

Air Marshal Shepherd—They perform a vital service in certain areas. I had a discussion with the lady who runs that store. They have a few cameras and electrical goods on sale. Clearly they need to restructure themselves. No-one is going to go to a little shop to buy a camera. They would rather drive to Darwin or something like that to get it cheaper. So they need to pick the winners and restructure their service to provide us with the service that we require in the remote areas. It may be that on some bases, where they are in close proximity to major capital cities, they do not provide things that you can just, as the secretary says, easily drive down the road for. Chief of Army will probably have a different perspective than me and Air Force. Air Force is mainly located near major population centres.

Lt Gen. Leahy—We have a similar view. Deployed forces would be our priority—for example, those deployed in Timor. I am very keen to get Frontline into Timor so that the guys can buy cigarettes, razor blades, candy bars and things that they might want. We have a number of bases—and I would instance Bandiana, the logistic training centre, Puckapunyal,

and where there is recruit training at Wagga and other places where we have young soldiers who do not as yet have access to a car and where there is very limited public transport. There is no place for them to relax. Frontline provide that very vital service for us, and we are very appreciative of what they do. We hope that that would continue in some form in the future.

What we now find, though, as the secretary and CAF have suggested, is that there are changing patterns. In Townsville the town is joining the army base. Townsville is growing in a very quick manner. There are frankly more entertaining places in town that the soldiers can go to. There is a Harvey Norman and there are other places where they can buy their whitegoods. We have been working with the Frontline board, which is a very cooperative and, I would say, very sincere board that is trying to provide a service, but it is becoming quite difficult for them, because many of the places where they have been providing services are just not making money, and that balances out over the Army and the Air Force across our bases in various locations.

It is now clear, with the changes in spending patterns and the way that soldiers wish to be entertained, that they will have to look at their business. They are doing that now. I am aware that they are looking at their whitegoods sales. They have a pay plan whereby soldiers, at pretty good interest rates, are able to purchase goods through their pay. They are looking very carefully at whether that can be considered, because it inhibits their cash flow. There has been something like \$4 million tied up in this and that has been a difficulty for them. I am very comfortable that the Frontline board, in concert with Minister Billson, are working to try and ensure that we can provide that vital service both offshore and for our soldiers who are in remote localities and do not have the ability to get into town.

CHAIR—Very good.

Lt Gen. Leahy—Essentially, the difficulty is that it is an expensive business to run. We need to look at how we can support them in running that. What we are moving towards is a more fee-for-service arrangement—that is: ‘We want you to do this. This is what it is going to cost.’ We will have to look at that.

CHAIR—So the review and the assessment of the delivery of Frontline services is happening now—

Lt Gen. Leahy—Absolutely.

CHAIR—and we can leave it until the next estimates or some estimates down the track to see how they go. We would simply like to see the annual report documents come in on time so that we can be kept abreast of what is happening.

Lt Gen. Leahy—I hope that by the time of the next estimates we will have a much better picture for you.

CHAIR—Very good. I am happy with those answers. Thank you for that.

Mr Smith—Chair, you asked us to table the CDF’s directive on procedures for the repatriation of deceased ADF members who die on duty. We have it here. We have copies for all the members, and I understand some media people are interested in them.

CHAIR—Thank you.

Senator MARK BISHOP—I have just one question to wrap up this section. Could we turn back to page 173 of the PBS, to the table that we were talking about before on superannuation and housing support. If you go down to ‘Administered Expenses’ and the heading ‘Retention benefits’, it shows that \$46 million will be spent this year and in the three out years. What does the total of \$184 million represent?

Mr Smith—Mr Veitch will provide the response as to which retention benefits are under that heading.

Mr Veitch—I do not have the information with me. I will check that. I think it is the benefit that we pay in relation to the MSBS. There is an incentive for people to sign on beyond a particular period, and at that point we pay them an amount of money as a benefit for staying on for extra years.

Senator MARK BISHOP—Is it just a book transfer and you pay it into the scheme?

Mr Veitch—No, we would pay that from the administered item, which is managed by Finance on our behalf, direct to the member.

Senator MARK BISHOP—Is this a sort of bonus after X years of service that is paid annually for staying on?

Major Gen. Evans—I understand that it is part of the MSBS. Originally, part of the scheme was that at the 15-year point people would sign on for a further five years to receive that retention benefit. That is currently being phased out. I understand that that is what that would be.

Senator MARK BISHOP—It is not related to any of the recruitment retention benefits announced in the budget?

Mr Veitch—Absolutely not. They are separate. They are being funded through departmental appropriations as part of the Defence budget, not as part of the administered item.

Senator MARK BISHOP—You think this is a cash payment made to re-signing personnel under the military superannuation scheme?

Mr Veitch—Yes, that is correct.

Senator MARK BISHOP—But you also say you think it is being phased out—did you say that, General?

Major Gen. Evans—It is being phased out; I forget the number of years that is going to take. It is part of the benefits scheme that we are removing. We are using other retention initiatives aside from the MSBS program.

Senator HOGG—If it is being phased out, why is the amount static out till 2009-10?

Major Gen. Evans—I cannot answer that question.

Senator HOGG—It would seem to me that it would be a decreasing amount if you were phasing it out.

Mr Veitch—We review the estimate each year, based on the take-up rates at the time. I guess the good news from that for us is that, if it is going to take some years to phase out and

it has actually increased in this year's budget, it means that more people are availing themselves of the retention benefit, and that will flow through well in our numbers into the future.

Senator MARK BISHOP—But I am hearing Major General Evans say that you are phasing out one form of retention payment, which currently costs you \$46 million a year, but instituting another set of retention payments that will cost \$194 million over four years.

Major Gen. Evans—The issue there is that the MSBS retention benefit was not part of a targeted retention scheme. What we are introducing are targeted schemes, particularly against the 28 critical trades.

Senator MARK BISHOP—I hear you and I understand. But we are told in the budget papers that the government is spending \$194 million in the next four years on retention and recruitment allowances across the three services; then I hear you say that sometime in the future you are going to be getting rid of the current retention payment system in the superannuation scheme, which is worth \$46 million a year. You are robbing Peter to pay Paul.

Major Gen. Evans—We are changing the way we are dealing with the issue of retention and becoming far more focused on that particular issue.

Senator MARK BISHOP—But the net cost to government is going to be hardly anything after 2009-10, according to this table.

Major Gen. Evans—I cannot answer.

Senator MARK BISHOP—Caught and bowled. In reaction to the crisis in retention rates in the services you have, for the last three months, been yelling from the yardarm about the \$194 million that you have been spending on the retention and recruitment bonuses. You are building that up, but you are telling me that a policy call has been made by the government to knock off the retention bonus in the military superannuation scheme that costs almost the same amount per annum.

Major Gen. Evans—I am saying that we are focusing on or targeting particular trades, rather than having a broad retention bonus attached to the superannuation scheme.

Senator MARK BISHOP—I hear you say that you are focusing on retention and recruitment in the 25 critical trades areas that have been identified. I know there are five priority areas that are a particular problem in Navy. I know that you have allocated \$194 million over four years across the three services, and I know that that is targeted at particular hotspots. Take that as read.

What this document shows, though, is that, of the \$194 million you are spending over the four-year period, you are clawing back the best part of \$182 million through making these changes to the Military Superannuation and Benefits Scheme. So the net extra spend for the crisis problem we have in armed services recruitment and retention is the difference between \$182 million and \$194 million, some \$12 million. That is the state of the crisis.

Mr Veitch—Senator, I do not think you can draw that conclusion at all.

Senator MARK BISHOP—Tell me where my logic is wrong.

Mr Veitch—I think the first thing we should do is get the facts and follow up on what the MSBS policy change is, because the two are not—

Senator MARK BISHOP—They are your documents!

Senator PAYNE—Chair, could Mr Veitch be allowed to finish? I am actually listening to the response—unlike, apparently, Senator Bishop.

Mr Veitch—The document, on page 173, clearly shows that it will not discontinue before 2009-10.

Senator MARK BISHOP—No, when will it discontinue?

Mr Veitch—I am unaware of the facts and I would like to check that before we draw that correlation, because I do not think the correlation exists. If we were changing the superannuation arrangements we would be changing them with some other benefit or form of incentive.

Senator MARK BISHOP—With due respect, Mr Veitch, Major General Evans just told us that the government had made a decision to abolish the generalised retention payments system for serving personnel sometime in the future. That is what I understand Major General Evans to be saying. If that is the case, the decision has been made and it is only a matter of implementation. Am I misrepresenting what you have said, Major General?

Major Gen. Evans—I am saying that the intention is to phase out that particular retention element and move to a more targeted approach.

Senator MARK BISHOP—That is right; that is what you have been saying. When is that intended to come into effect?

Major Gen. Evans—I will have to take that on notice.

Senator MARK BISHOP—Who makes that decision? Is that within your responsibility, Major General, or is it somebody else's?

Major Gen. Evans—That is within my area.

Senator MARK BISHOP—Is that decision made by you or the board of the MSBS?

Major Gen. Evans—The MSBS retention element was to attract DFRDB people across to the new scheme. That will cease when the last member reaches the 15-year mark.

Senator MARK BISHOP—When will that be?

Major Gen. Evans—I will have to take that on notice.

Mr Smith—We might be getting into an area of speculation here. We are clearly not certain about the superannuation issues. Let us try to sort it out with the MSBS overnight and find out what they are doing.

Senator MARK BISHOP—When do you suggest that you will do that?

Mr Smith—We will try to do that overnight.

Senator MARK BISHOP—That is fine.

Senator FERGUSON—Did the MSBS start in 1994? I remember asking questions of the then minister about the time allotted for people to choose between DFRDB and MSBS, and I

am sure the scheme started in 1994. When you are talking about 15 years, are you talking about people who have been in MSBS for 15 years?

Major Gen. Evans—Take me as an example. When the scheme was introduced I was on the 15-year mark. I elected to cross over to MSBS and, with that, I got the five-year retention bonus.

Mr Veitch—Senator Ferguson, the brief I have here suggests that the scheme commenced on 1 October 1991.

Senator FERGUSON—But it was in 1994 that they phased out DFRDB.

Mr Veitch—There was probably some transition period—

Senator FERGUSON—Put it this way: they did not offer DFRDB to people after that, after 1994.

Mr Veitch—Yes.

Senator MARK BISHOP—I take the point that Mr Smith has made. When answering the questions for us tomorrow, you might directly address the issues of the future of the MSBS; the future of any current retention bonuses that are contained in that scheme; if and when the decision was made to abolish the 15-year retention bonus that the major general referred to or any other retention bonuses; the expected savings to revenue from such means; when it is to be implemented and if it has been approved by Finance and Defence as a savings measure; and whether the figure as suggested by the budget papers, of \$46 million a year going into the future, is correct or, if not, what the actual figure is. Could you do that, instead of me engaging in speculation?

Mr Smith—We are on it.

Proceedings suspended from 3.29 pm to 3.48 pm

CHAIR—I call the committee to order. We will continue with questions from Senator Bishop.

Senator MARK BISHOP—I want to talk about the alleged problems with the Hawk lead-in fighter trainer aircraft, particularly the auxiliary power unit. I am advised that RAAF 76 Squadron operates the BAE Systems Hawk 127 lead-in fighter trainer aircraft at Williamstown in New South Wales, and the RAAF 79 Squadron operates the same aircraft for tactics training at Pearce in Western Australia. I am advised that each aircraft has an auxiliary power unit, APU, which provides power to start the engine initially and support systems such as airconditioning and electricals on the ground prior to engine start. Accordingly, as you can glean from that, the APU is a flight-critical component of the aircraft. I am advised that a number of them are not functioning and there are problems with contractors. I want to explore that.

Air Marshal Shepherd—The Hawk does have an APU. It is a necessary piece of equipment—I would not say it is essential for flight; it is used on the ground for starting, as you say. You could also start the aeroplane with external battery power so it is not fundamental to flight in that regard. Frankly, I have not heard about any problems with the APU. I have a sophisticated traffic light system that reports to me every month on the issues

we are having around the Air Force. There may well be a small problem. There are often technical issues around a range of aeroplanes that are solved at the working level. Air Commodore Col Thorne here with me is from our Defence Materiel Organisation. He handles the systems project office that runs the Hawk. Have you heard anything about this?

Air Cdre Thorne—No, I have not.

Senator MARK BISHOP—You have not been advised of any problems with the operation of the APU?

Air Marshal Shepherd—No. I can add some background on the Hawk. We are very happy with the Hawk. It has suffered a number of technical issues in the couple of years that we have had it. Each of those technical issues has been able to be overcome and rectified. That is normal; these are complicated pieces of machinery. The Hawk was just recently deployed to Malaysia for a major exercise up there. That is the first time we have sent it offshore. We have cleared it now for air-to-air refuelling. We drop high-explosive weapons off it. We can now shoot missiles off it, which enhances the fidelity of the training we do on it. We are very happy with the aeroplane. In fact, I think we are leading the world in the way we fly the Hawk. Certainly, other air forces have approached us to see how we have brought the Hawk into operational service so efficiently and effectively.

There may well be a small issue with the APU. It is not of a consequence that inhibits its operations. The aeroplane exceeded its serviceability requirements in April. And, as I said, it has just done this major deployment to Malaysia. If it is an issue it is an issue that is able to be contained and handled at the working level within the squadron.

Senator MARK BISHOP—You have not been advised that the APUs fitted to the Hawk aircraft are prone to overheating and subsequent shutdown?

Air Marshal Shepherd—That is exactly right; I have not been advised. If it had affected the Hawk's operations I would have been advised. The inference I draw from that is that the Hawk is still able to achieve the training effect that we need, despite occasional problems.

Senator MARK BISHOP—In the period since the Hawk aircraft was brought into service into Australia, no instances of overheating on the APUs have been brought to your attention?

Air Marshal Shepherd—They have not been brought to my attention; therefore, they are not of a consequence that affects the operation of the aeroplane or the effect that we need to get out of it.

Air Cdre Thorne—I am also not aware of the details of the APU problems. They have been problems in the past and as a consequence of that the contractor, BAE Systems, has put two extra APUs into the pool of spares to ensure that availability is not compromised. I believe that part of the problem was due to start-up procedure publications. The APUs are used to start the aircraft and there were some issues with the way that some of the procedure publications were written, which caused difficulty operating the APU. They have been corrected. I will go with what Chief of Air Force is advising: under the contract we contract BAE Systems to provide a pool of available aircraft and on average—we have ups and downs—the contractor has met that pool of available aircraft, notwithstanding this problem.

Senator MARK BISHOP—When you say ‘notwithstanding this problem’, there is a problem. Is there a problem with APUs starting the aircraft?

Air Cdre Thorne—I do not believe that is a problem at the moment.

Senator MARK BISHOP—Was it a problem in the past?

Air Cdre Thorne—Obviously, if there is a need to inject at company expense additional APUs into the supply chain and if there is a need to correct publications there was a minor problem in the past, yes.

Senator MARK BISHOP—What is your position, Air Commodore?

Air Cdre Thorne—Air Vice Marshal Rossiter is head of aerospace systems division. Unfortunately, he is overseas at the moment and I am acting for him.

Senator MARK BISHOP—If there had been problems with the operations of the APU in terms of starting the plane and providing operation of airconditioning and electricals on the ground, you would say to me that it would have been brought to your attention?

Air Cdre Thorne—Yes, it may have been, although I must confess that I am not in the line management for that particular aircraft type. I would also say that, in general, we manage that under a total support contract with BAE Systems. There are a couple of headline metrics, one of which is the aircraft available to our pool. One of the other metrics is spares available. We have a demand satisfaction rate for different types of spares. To my knowledge, this particular issue has not affected any of those headline contract deliverables, nor has it affected operations.

Senator MARK BISHOP—How many Hawks do we have in 76 to 79 squadrons?

Air Marshal Shepherd—There is a total of 33.

Senator MARK BISHOP—How many of them are operational?

Air Marshal Shepherd—Once again, that is a figure that we do not carriage. It is a figure that, frankly, is irrelevant because we contract for a certain availability of aeroplanes and a certain flying rate. It is a different contract. It is not contract which says, ‘You will have X aeroplanes online.’

Senator MARK BISHOP—I understand. How many do you contract for availability?

Air Cdre Thorne—I do not have the number. I can take that on notice. I think it is 30-odd.

Senator MARK BISHOP—So 30-odd of the 33 are contracted to be available?

Air Marshal Shepherd—It is 33, I am told.

Senator MARK BISHOP—So all of them are contracted to be available?

Dr Gumley—My understanding is that the contract is for 9,000 operational hours a year. It is a level of effort contract.

Air Cdre Thorne—I am advised that 19 from 33 is our daily pool.

Senator MARK BISHOP—And as long as 19 of the 33 are serviceable and operational, the contract has been complied with—is that your advice?

Air Cdre Thorne—That is correct, in addition to provision of other services, such as provision of spares.

Senator MARK BISHOP—You say there has not been any APU problem or any consequence drawn to your attention?

Air Cdre Thorne—That is correct.

Mrs BRONWYN BISHOP—And that is what the air marshal is saying?

Air Marshal Shepherd—That is correct.

Dr Gumley—It is a performance contract. If there is a problem, it belongs with the contractor.

Senator MARK BISHOP—So servicing and maintenance responsibilities for the Hawks and the APU part are all the responsibilities of the contractor?

Dr Gumley—Yes, BAE Systems have that contract.

Air Marshal Shepherd—At that level, the first line servicing is done by uniformed people.

Senator MARK BISHOP—Is there any down time at the moment of the contracted provision for flying hours for the Hawks?

Air Marshal Shepherd—I am not quite sure what you mean by ‘down time’. Certainly, the limiting factor in flying the delivered contracted flying hours appears to be our own uniformed maintenance effort rather than BAE Systems.

Senator MARK BISHOP—What is the problem there?

Air Marshal Shepherd—We set the Hawk up. We have not had it for that many years. It is a very capable aeroplane, as I said. We have been able to do very good training with it. When we set the squadrons up originally we set them up on a forecast maintenance strength of what we understood from the operations of the previous training aeroplane—the Macchi 326—and we forecast ahead our estimation of what the additional maintenance would be on the Hawks, because it is a far more capable and complex aeroplane. We were on a learning curve for the first couple of years, of course. It is a brand-new aeroplane and complex, as I have said. We now realise that we have actually got the maintenance structure in uniform in both squadrons not quite optimal. So we are looking to rebalance some of those maintenance people across so that we can achieve the flying rate that we require from the contract. So, if anything, the contract is delivering more than we can accommodate at the moment.

Senator MARK BISHOP—In 2004-05 reporting period, I am advised that the 33 Hawk aircraft obtained 9,000 flying hours. Is that correct?

Air Marshal Shepherd—Nine thousand was what we contracted for. In 2004-05 I do not think we achieved 9,000. I think we have been sitting at anywhere between 7,000, 7 ½ thousand or 8,000. We are looking to forecast 8,000. That is on page 159 of the PBS. Our forecast for 2006-07 is 8,000 flying hours.

Senator MARK BISHOP—If they are contracted to do 9,000 hours and are capable of doing so, why are they only carrying out 7,000 or 8,000 hours?

Air Marshal Shepherd—As I explained before, the limiting factor is in our own uniformed maintenance capability, which is on the front line. Initially, it was a learning curve with the new, complex aeroplane. Now we have some limiting factors in our own maintenance people which we need to balance up and adjust so that we can get the optimum throughput and the optimum combat.

Senator MARK BISHOP—Are you now satisfied that you have travelled up the learning curve, that your own maintenance people are sufficiently on top of the demands and that the Hawks will be able to meet the contracted time of 9,000 hours?

Air Marshal Shepherd—I am confident that our people have the skills necessary to operate the Hawk and to maintain the Hawk. We will not achieve 9,000 hours next year because we need to balance some of our maintenance people across the Air Force and that will take a period of time to do. But we seek to increase the Hawk hours into the future. It is a very capable training platform. As we move through the transition into the new air combat capability, the Hawk will be a key part of that and we will seek to increase the hours. The limiting factor at the moment, as I said, is our own key people. For the want of a couple of key supervisors in the maintenance area—sergeants or key people like that—we are unable to use the full extent of the contract.

Senator MARK BISHOP—Is that just an example of a recruitment problem in a very highly skilled technical area?

Air Marshal Shepherd—We do not have a big recruitment problem in Air Force. Our loss rate in Air Force for enlisted ranks is 7.8 per cent, which is actually optimal.

Senator MARK BISHOP—What you have said to me is that the Hawks will not for some time be able to fly at the contracted hours. You say that the cause of that problem is not problems with the plane itself or the APUs. You say it is a maintenance problem in house, not a maintenance caused by the contractors, and you say you are short of a couple of senior level supervisors.

Air Marshal Shepherd—That was an example. It is a structural imbalance in the maintenance workforce we have set up to do first-line maintenance on the aeroplane.

Senator MARK BISHOP—What does ‘structural imbalance’ mean?

Air Marshal Shepherd—It means we do not have enough supervisors. We are short of weapons technicians, minor things like that. We may lose some people as they transition to civilian life. That is why we need to increase the permanent manned strength of the squadrons so that they will be able to fully utilise the contracted hours. We are seeking to do that over the normal posting cycle and as we can spare people from other major platforms.

Air Cdre Thorne—I could clarify with a point on the contracted hours. The company is contracted to provide a daily pool of 19 aircraft. It is contracted to do that within a band of tolerance up to 9,000 hours, so it is not contracted per se to provide 9,000 hours.

Senator MARK BISHOP—What do you mean by a ‘band of tolerance’?

Air Cdre Thorne—A level of effort. Obviously, the company needs to structure its maintenance workforce for a rate of effort. The contract is struck at a firm price basis for being able to achieve a band of rate of effort up to 9,000 hours. The fact that the Air Force

flies a lesser amount still means that you are inside that band of tolerance for the workforce capacity of the company.

Senator MARK BISHOP—Thanks for that. I want to turn to the C130J Hercules aircraft now. Are the C130J aircraft currently operating in a tactical environment in the Middle East area of operations?

Air Marshal Shepherd—That is affirmative. We have two J models currently based in the Middle East area of operations, conducting operations into Iraq and Afghanistan.

Senator MARK BISHOP—Have problems with the C130J engine cooling been identified or become apparent in the tactical operating environment with respect to the ingestion of ferrosilicate material?

Air Marshal Shepherd—That would be the sand, Senator. That is very prevalent around the bases where we are based in the Middle East. Once again, it is the same answer as I just gave you for the Hawk. These aeroplanes are operating in extremely hazardous and difficult environments.

Senator MARK BISHOP—Understood.

Air Marshal Shepherd—The J model is a much more electric aeroplane, shall we say. It is a very computerised aeroplane. They are based in the Middle East, in the host nation there, where the sand—or the ferrosilicate substance—is extremely fine. It is of talcum powder like capability and it gets into the aeroplane. Of course, the aeroplane is a more computer based and a more advanced Hercules than our old H model, which is a bit more ‘mandraulic’. It has had an impact over time, but we have been operating the J over there for well over 12 months. In fact, we led the Americans and the British in the tactical operation of the J, and it has been a very successful aircraft. Such problems as we have had have not stopped us from achieving the effect we need to, and the servicings have been able to keep the flying rate at the level we want in the Middle East. Only rarely are there occasions when both aeroplanes are broken, and we are always able—with the odd case-by-case exception—to meet the tasking that has been given to us.

Senator MARK BISHOP—How many of these Js do we have?

Air Marshal Shepherd—We have 12 Js.

Senator MARK BISHOP—How many do we have in the Middle East?

Air Marshal Shepherd—We have two in the Middle East at any one time. Occasionally we will fly a third one across to take sustainment. CDF was talking this morning about the leased aeroplane we have; we cannot take explosive ordnance on that aeroplane, so every two or three weeks we fly a C130—it might be a J or it might be an H—across to the Middle East carrying those dangerous cargoes. On occasions, at times of a busy workload such as the recent rotation in place of the Al Muthanna Task Group, that third aeroplane may stay there for a week or two longer and give them a slight surge capacity for a busy period.

Senator MARK BISHOP—We have two in operations over there. Do we fly them both at the same time, or do they do it sequentially?

Air Marshal Shepherd—Sometimes they fly both, sometimes they fly together or on the same day but at different times, and occasionally they are both not flying. There is a roster, which is dictated by the Combined Air Operations Centre. This is the centre that controls all military air activity in the Middle East region—American, British or whatever. Our people are in that centre and look after the tasking for all military aircraft in the Middle East, including our Hercules.

Senator MARK BISHOP—Is the sand causing blockages in the cooling holes?

Air Marshal Shepherd—It may well be, but once again it is a tactical maintenance issue that the people get on and fix up. It has not been of sufficient magnitude to cause us to cease our operations or to impact in any meaningful way on them.

Senator MARK BISHOP—Have other nations operating in these sorts of environments experienced similar problems to those that have been identified in this discussion?

Air Marshal Shepherd—The Middle East is characterised by sand, as you would expect. But there is different sand, in all truth. Many parts of the Middle East have coarser sand that does not blow around. Where our Orions are based there is a sea of sand around them, but it is a coarser, beach type of sand; it does not blow and is not as mobile. As I said, where the Hercules are based the sand is very fine and gets into things. Where the British have their Js based, in Basra in southern Iraq, I understand the sand is more granular as well. We very much led the world. We put our Hercs in a tactical environment at around about the same time as the British but well in advance of the Americans. As I said, sand is not always sand. We have experienced that sort of difficulty there and we have overcome it and been able to maintain our tasking as appropriate.

Senator MARK BISHOP—You advised me that the problems with the cooling, because of the fine sand where the Hercs are located, are not on such a scale that they have caused any interference with operations or required excessive downtime for maintenance, repair or replacement.

Air Marshal Shepherd—That is affirmative.

Senator MARK BISHOP—Has a decision been made to not carry forward minor unserviceabilities on the H model aircraft?

Air Marshal Shepherd—Once again, it is a very shop floor level question. Every aeroplane invariably has minor unserviceabilities. You can keep carrying some unserviceabilities on an aeroplane; you can wait until the aeroplane gets home a couple of weeks later, if it is away. Obviously there are some critical maintenance errors that would cause an aeroplane to stop flying. I would be very surprised if any aeroplane that has worked hard on an operation deployment does not have some minor unserviceabilities carried forward—that is the nature of aviation. When you sign on to fly an aeroplane you check the signature page to see that the aeroplane has been replenished with oil, fuel and all those things, and you normally check the unserviceabilities sheet.

It is an issue that is very much handled at the squadron level—it is very much handled by the senior engineering officer in the squadron, who uses his professional judgment, and by the

technicians in charge of maintenance. Once again, there are no red lights flashing on my traffic light system to indicate any issue in that regard.

Senator MARK BISHOP—Have any change management directives been placed on the maintenance of the H fleet in relation to carried forward unserviceabilities?

Air Marshal Shepherd—Once again, and without trying to avoid the question, I will answer it in a more conceptual sense—but it is a very tactical thing. We are always very mindful of maintenance practices. In aviation, the three legs of the stool are: an appropriate maintenance culture, an appropriate engineering culture and an appropriate flying culture. We are very concerned to keep those cultures at the best level at all times. Certainly we are always aware of issues in our cultures, be they flying, engineering or maintenance. We currently have a maintenance improvements program running where we believe we can make enhancements to our maintenance culture, and that program is still playing out. We have changed our maintenance practices over the years. We have become an authorised maintenance and engineering organisation, meeting set standards under our airworthiness process. Within that constant seeking of improvement and optimal performance on each of those legs of the stool, there will always be practical outcomes, such as issues that you may well raise.

Senator MARK BISHOP—I appreciate your comments, but has the level of carried forward unserviceabilities with respect to the H aircraft over in the Middle East been of such significance that new management directives for their maintenance have had to be issued?

Air Marshal Shepherd—Not to my knowledge. In fact, we do not have the Hs in the Middle East, and we have not had them there for effectively this calendar year. In fact the H will probably not do a lengthy deployment in the Middle East again.

Senator MARK BISHOP—Has the government made a decision about what it is going to do with the Hs when the C17s come on line?

Air Marshal Shepherd—No. I might ask General Hurley to explain that in more detail, but certainly now that we have the C17 end of the airlift equation fixed it gives us the opportunity to look at what we will do with the medium fixed wing lift—the Hercules capability—what we will do with the light fixed wing capability—currently resident in the Caribou—and where the Chinook and the rotary capability fit into that equation. We are currently working on a submission to government, and I think the first pass is going up to government with a range of options around about June or July. Within that construct, the situation about whether to replace or refurbish the H model, based on a range of criteria, will be addressed.

Senator MARK BISHOP—So, to date, there has not been a decision made to do anything with the Hs when the C17s come on line?

Air Marshal Shepherd—That is a slightly different question to what you asked. We have not made a decision about the long-term future of the H. Of course, in order to staff the C17 workforce a decision has been made to take that workforce from the H model fleet. So we will be operating the Hs at a much reduced rate of effort.

Senator MARK BISHOP—A less demanding level.

Air Marshal Shepherd—We will effectively have to retire some Hs—though it is not as simple as that. What you do is use the whole fleet at a lesser rate, but we will produce less H flying hours, and we have taken those people from the H world to give us those start-up people for the C17.

Senator MARK BISHOP—So is the decision to be made by government to retire the Hs, refurbish the Hs or maintain the Hs to work in tandem with the C17s? Are they the three options?

Air Marshal Shepherd—Very broadly. You correctly identified earlier that we operate the J. How many Hercules we need to operate in the whole lift equation is important; also, how many Caribou type aeroplanes—refurbish the Caribou, replace the Caribou; what to do with the rotary wing Chinook type element of that. There is a whole range of options within that. We need to look at the whole lift equation, the whole capacity, the volume that we need to lift and when we need to do that. That is part of the studies that have been going on for a long time. We will go to government with those first-pass options. A range of outcomes would be affected by what we require. As well, there is the commercial reality.

Senator MARK BISHOP—Do you currently have any H aircraft grounded because of minor unserviceability problems?

Air Marshal Shepherd—There are always aeroplanes that are unfit to fly, but in essence you make an aeroplane fit to fly for when you need it to fly. It is not like everyone goes to work, we finish flying for the day and everyone slaves all night to make them fit to fly tomorrow morning when you do not need them. There are always aeroplanes that are out of flying activities for maintenance activities. In general, that is of a temporary nature. We have no H model grounded at the moment, permanently or for the long-term, for maintenance issues. There will be ones, however, that are down for upgrades. The H is an old aeroplane. We have found cracking in it, so we have put in place enhanced inspection regimes to ensure us of the safety of the aeroplane. Those enhanced inspection regimes take a bit longer than normal. So, once again, it would be like getting your car serviced every 2,000 kilometres instead of every 5,000 kilometres. That is a very crude analogy.

Senator MARK BISHOP—Is the availability of the H aircraft significantly different from what it was 12 months ago?

Air Marshal Shepherd—Yes, it certainly has pressures on it because the aeroplane is old. It takes more effort to maintain it. Over the last couple of years, we have also put a lot of survivability equipment into the aeroplane: foam suppressant in the tanks, ballistic matting, electronic warfare self-protection and things like that. That has impacted overall on H availability in recent times.

Senator MARK BISHOP—What is the reduction in availability over the last 12 months?

Air Marshal Shepherd—I do not have those figures with me. If I may, I will have a quick look at my notes, because I have flying hours for recent years here.

Air Cdre Luke—I could jump in here. Out of the fleet of 12, we normally have about four aircraft on the ground at any one time—

Senator MARK BISHOP—Of the Hs?

Air Cdre Luke—yes—locked up in deeper maintenance. Certainly over the last 12 months, the inspections that we need to do for the structure of the aircraft have increased. We are finding that the aircraft are spending a longer time in the deeper maintenance operations.

Senator MARK BISHOP—When you use the phrase ‘deeper maintenance’, do you mean something different to the minor unserviceabilities that I was discussing earlier with the air marshal?

Air Cdre Luke—That is correct. Deeper maintenance is the cycle of heavy maintenance, where the aircraft disappears into the maintenance shop for some considerable time. There is usually quite a bit of disassembly and a lot of detailed inspection.

Senator MARK BISHOP—So four of the 12 are in deeper maintenance. How many, if any, are temporarily grounded because of the minor unserviceabilities?

Air Cdre Luke—We normally expect that there would be one or two more aircraft available to the squadrons to fly that have a minor problem at the time. They may have a system that is not working properly that needs to be remedied. They do that at squadron level. It is just normal business.

Air Marshal Shepherd—If I may, I can give you a figure that is pertinent in this regard. Once the aeroplanes are out of deeper maintenance and they are available for use on the line, we find with the Hs that the average serviceability rate is around the 70 to mid-70 per cent mark. So, if you had 10 on line on a normal day, about seven of them would be available to do the missions.

Senator MARK BISHOP—If you have 12 and four are in deeper maintenance, it means that there are eight. Probably on a good day we would have five or six that are available for operations?

Air Marshal Shepherd—Yes, in rough figures.

Senator MARK BISHOP—So, at any given time, a couple are off the list due to those minor unserviceabilities?

Air Marshal Shepherd—That is true, but there are peaks and troughs, of course.

Senator MARK BISHOP—Yes. The Hs are significantly older than the Js, aren't they?

Air Marshal Shepherd—That is an affirmative.

Senator MARK BISHOP—How many Js do we have?

Air Marshal Shepherd—We have 12 Js as well.

Senator MARK BISHOP—How many of those are in deeper maintenance at any one time?

Air Cdre Luke—We are just doing our second deeper maintenance operation on the Js. They are a quite new aeroplane. We would have a similar number once we get to the mature state. Hopefully they will not spend as long as the Hs currently spend in deeper maintenance, because they are nowhere near as old.

Senator MARK BISHOP—You are advising me that, of the 12 Js, at any one time possibly up to four are in deeper maintenance?

Air Cdre Luke—That is correct.

Senator MARK BISHOP—Does the same equation apply to the Js at the moment as it did to the Hs: an operational level of about 70 per cent—that is, we have about five or six that are available for operations?

Air Cdre Luke—I think it would be a slightly better figure for the Js across the board. It is a newer aeroplane and has newer systems and, although they are more complex in terms of the computer controls, they also have terrific diagnostic systems that help keep the aircraft online.

Senator MARK BISHOP—Is this downtime with either deeper maintenance or minor unserviceabilities of up to about half the fleet of the Hs and a little bit less of the Js consistent with your planning for their use, for training and for keeping up to date the skills that the aircrew require to be able to engage in regular flying?

Air Marshal Shepherd—That is part of the daily job for the leaders of Air Lift. There are certainly requirements like conducting operations now. There is certainly a need for us to continually train and regenerate the fleet to qualify our people and to bring new younger people on with the aeroplane. At times, those requirements are in competition. Last week, when we needed to deploy at very short notice, as the CDF indicated, the force into Timor, it is ‘drop everything and do that job urgently’. That is an operational requirement. That lasted for a number of days. Already we have been able to meet the requirement for the force build-up and the sustainment of the force and to be able to bring some of the aeroplanes and crews back to conduct training. Those requirements are often able to be conducted in parallel, without any friction with each other, but often, of course, in times of high operational tempo for short, sharp periods we have to put our priorities one way or the other.

Senator MARK BISHOP—When we are involved in operations as we are currently, does your routine planning involve up to about six of both the Hs and the Js being engaged in what I call downtime, be it deeper maintenance or minor unserviceabilities? Having answered that, do you know if that is consistent with the need for aircrew to maintain their skills on schedule and to go through into more senior levels on schedule?

Air Marshal Shepherd—It is. I will not say that it is six and six, because the numbers of aeroplanes unavailable due to maintenance or modifications change over time, but we are able to, in a steady state sense, project forward across the year. That is what we do in the PBS, and on page 161 we have said that next year, with the introduction of the C17, we will look to fly 10,000 Hercules flying hours—that is between both the Js and the Hs. We will plot forward our activity schedules. We know when the major exercises are coming up. We know when the work for the Hercules is to be done. We know what conversion courses we need to do. We will do the job with the resources we have been given. Of course, things that pop out of the blue, like Timor or emergent crises, have to get accommodated within that, and within a closed system we have to adjust and provide flexibility.

Senator MARK BISHOP—I want to go back to the decision on the future use of the Js and the Hs when the C17 comes online. When do we expect the C17s to be online and operational?

Air Marshal Shepherd—We expect the first C17 to turn up in early December. In fact, I was in Long Beach, California just the other week. Our first bit of the roof would probably cover all of you sitting there; it is not a huge bit. It is quite amazing to think that that will be here as a fully flying and functioning aeroplane in December. We will then need to put that aeroplane through a period of transition training and testing. Our crews will need to understand it. That will take us pretty much through to August. We will have a second aeroplane arrive about June or July next year. We aim to declare the first aeroplane operational and available for consistent regular tasking in August 2007. In the lead-up to August 2007, the aeroplane will be available. Despite it doing its testing and training, it will be available on a case-by-case basis—that is, if the crew need to do some long-range flying for their own practice, they may as well carry some stuff down the back and take it somewhere. The aeroplane will be usable to a certain extent, but we aim to declare the first one operational for contingency, crises and regular tasking in August. The numbers three and four aeroplanes will arrive in the first quarter of 2008. Throughout that period as well, leading up to probably the end of 2008 or early 2009, we will not only be developing the aeroplane in its Airlift role but be looking at tactical roles such as para drop and stuff like that. We have a very well mapped out schedule until about mid-2009, when we will have the four aeroplanes and all the crews fully capable in the whole range of different activities that Air Lift can do.

Senator MARK BISHOP—We had a discussion earlier as to the future of the Hs, the Js and the C17s; that is why I wanted to get on the record what it is you are doing with the incoming C17s. Is that a decision of the National Security Committee of Cabinet?

Air Marshal Shepherd—In that regard, yes, it will be a decision as part of the DCP project. As I said, first pass will be going to government mid this year.

Senator MARK BISHOP—When will the recommendation from Air Force go to the NSC for a decision?

Air Marshal Shepherd—The first pass process is in, I think, June or July this year. That will give government a range of options—I think it is five options that they require. But, the options across the whole spectrum, as I have said, from what to do with the Hercules, the Caribou and the Chinook and the whole continuum of lift now that the C17 heavy-lift end is pegged down to the process between the first pass and second pass, as in the Kinnaird process, will be refined over the next couple of years as we come up with a final option for government.

Senator MARK BISHOP—So five options go forward for first phase in June and July this year?

Air Marshal Shepherd—That is affirmative.

Senator MARK BISHOP—Would you be breaking confidence to succinctly summarise the five options?

Air Marshal Shepherd—Probably. Conceptually, it is exactly what I have said. If you think of the lift equation as a wriggly snake, we have the head pinned down with the C17. We now need to pin down the rest of the body and see what to do with the medium fixed-wing lift, the Hercules; what to do with the light fixed-wing tactical lift; and, of course, what to do with the rotary wings, because rotary wings are a very important part of that equation as well.

So there is a range of options that have come up, from, I suppose, the suggestion that we get a whole bunch more of new Hercules and nothing else down to one that we get a whole bunch more Chinooks and nothing else—those are not among the five options, I might add, so I am not breaking confidences there. Within that sort of broad spectrum, we need to look at what our average lift capacity has been over the years and what we have historically needed to do. We have a lot of historical data now on Timor, the Solomons, the Middle East—

Senator MARK BISHOP—But you are unable to disclose the five options that go forward for consideration at this stage. Is that right?

Air Marshal Shepherd—I do not think—

Senator MARK BISHOP—Yes or no? And if the answer is no, tell me the five options.

Air Marshal Shepherd—They are not options in the sense that there is one that says: two Hercules here, a couple of things there and a couple over there. They are not fixed options like that. There is a range of capability options, pretty much as I have said, that look at the whole lift equation. The detailed numbers and costings will be developed between the first- and second-pass processes.

CHAIR—For those of us who are a little bit ignorant about these things, the C17 aircraft has a lift capability comparable to a C130 as a factor of—what?

Air Marshal Shepherd—About a factor of four, in a load and volume sense. In an operational planning sense, you would probably consider it to be a load factor of about two to three.

CHAIR—But it can be up to four?

Air Marshal Shepherd—Yes, in the weight and volume it can carry. But the big advantage of it of course is that it can carry big things—they do not necessarily have to be heavy big things, although it can carry them as well—like the Black Hawk and Chinook without having to pull them down.

CHAIR—Can it carry an M1A1 Abrams?

Air Marshal Shepherd—That is affirmative.

CHAIR—One or two?

Air Marshal Shepherd—It can carry one. But it can carry supporting equipment. I do not have the figures with me, but it can carry a number of ASLAVs, a number of APCs and a number of Black Hawks. It can carry one Chinook; Chinooks are a big aeroplane.

Senator FAULKNER—I have been very disappointed, Mr Smith, to see what appears to be an exodus to the private sector from DMO at the senior management level. Is that a fair interpretation of what has happened?

Mr Smith—I think ‘exodus’ might be overstating it, Senator. I think two senior people at the band 2 level have left over the last three months; one of those we had recruited from industry a couple of years ago and, perhaps, it was not surprising he went. The other was the deputy CEO, Mr Gray, who received a very attractive offer from elsewhere.

Senator FAULKNER—Who was the second person?

Mr Smith—That was Mr Gray. The first was Mr Croser.

Senator FAULKNER—You have mentioned the last three months. What about if we look at the last six months?

Dr Gumley—It was very stable through 2005.

Senator FAULKNER—So only two what you describe as senior managers from DMO have gone to the private sector. Is that the sense of this?

Dr Gumley—Yes. This year two people have gone to the private sector.

Senator FAULKNER—But there had not been a pattern prior to this year.

Dr Gumley—No. There was not a pattern prior to that.

Senator FAULKNER—In the last financial year were there any other examples of this occurring?

Dr Gumley—No. In the last financial year there were two band 2 DMO staff who went to the private sector.

Senator FAULKNER—It is a broader problem, it seems to me, Mr Smith, than just DMO. I think that is fair to say, isn't it? No doubt you will correct me if I am wrong. There are other examples of senior officers or senior managers in Defence recently going to the private sector.

Mr Smith—Yes. This will happen, particularly among military officers who are nearing the end or anticipating the end of their careers and who will look for opportunities and very often find them because they are highly trained and well-regarded people. We have to expect that that will happen. On the whole it is a good thing. We do not want to grow two separate worlds—a defence related private sector and a defence government sector. There has to be some cross-movement. We expect it will happen and it does.

Senator FAULKNER—I have seen in the press reportage of the fact that Major General Clifford, the former deputy chief of the information office, has recently gone to the private sector.

Mr Smith—He has not left yet. He is still with us.

Senator FAULKNER—So he is on leave?

Mr Smith—He is not on leave. I think he will be going to the private sector in July. The Chief of Army is aware of the case, of course.

Senator FAULKNER—Are there any other cases? The three that you have mentioned have received some coverage in the media, which I am sure you are aware of. Are there any other examples that have come to your attention in recently about which there has been no public comment? I am trying to establish whether there is a pattern here, you see, Mr Smith.

Mr Smith—I think that there was a two-star Air Force officer who went to work for the South Australian government, promoting defence industry and relationships there.

Senator FAULKNER—Who was that?

Mr Smith—Air Vice Marshal McLennan. I would see if the chiefs can recall any of their senior colleagues, apart from those we have mentioned.

Senator MARK BISHOP—A couple of them have gone to the Western Australian government

Mr Smith—Commodore Deeks is there, yes. But that is what we expect. As I said, people either anticipate or reach the end of their careers and seek opportunities elsewhere, because they are generally, at that stage, still quite young men and women.

Senator FAULKNER—When we have a situation of a move from DMO to the private sector, given the responsibilities that DMO has, Mr Smith, does that bring any particular challenges to the department or any particular considerations?

Mr Smith—Yes, it does, for DMO. We have to assess whether there is a real, potential or risk of perceived conflict of interest and deal with it. There are a number of ways in which we do that.

Senator FAULKNER—Let us go through the three examples that there has been some public mention of. This is Mr Gray, Mr Croser and General Clifford. Let us take the case of Mr Croser first. Can you first of all say to the committee, please, when Mr Croser resigned from DMO?

Mr Smith—I will ask Mr Lewincamp and Dr Gumley to deal with that because they handled that matter, although they kept me informed.

Mr Lewincamp—Mr Croser advised the CEO on Monday, 23 January 2006 that he had accepted an offer of employment outside the organisation.

Senator FAULKNER—Did he go on leave then? What was the situation?

Mr Lewincamp—He did go on leave. We have some well-established processes within the DMO for managing that situation which I can outline for you if you wish.

Senator FAULKNER—I would appreciate that. Perhaps this would be a good time for you to do that. We might come back to the specific instances. If you would not mind, either Dr Gumley or Mr Lewincamp perhaps can outline what those well-established processes might be.

Mr Lewincamp—When we have a senior officer of the organisation notify us about an approach from a prospective employer or when the officer advises us that he is considering employment outside the organisation, we put in place the following elements. We place restrictions on the flow of information to the officer and on the officer's access to information systems. The officer proceeds on leave or absence from the workplace until the employment situation is resolved. We conduct a review or audit of the officer's access to specific information which might be relevant to his future employment. We ask the officer to complete a statutory declaration on departure regarding any access to information relevant to his future employment and confirming his understanding about the obligations that he has not to disclose or make improper use of sensitive information gained during his employment with DMO and asking him not to participate in some activities with his future employer.

Senator FAULKNER—What are those activities that you ask him not to participate in?

Mr Lewincamp—They might be any engagement in relation to a particular project with which he had some association while he was with the DMO. There are three or four other measures that I might just quickly outline.

Senator FAULKNER—I am sorry—I thought you had concluded.

Mr Lewincamp—We also get specific advice from a probity adviser about the contents of the statutory declaration and any other measures that the adviser thinks are warranted. On departure, we give the officer supervised access to files and systems so that he can deal with any personal material.

Senator FAULKNER—Can you run that one by me again?

Mr Lewincamp—He can remove personal material from his computer and look through his office. We supervise that access when the officer departs from the organisation.

Senator FAULKNER—So you ensure that no Defence material is removed?

Mr Lewincamp—That is right. There also may be liaison by DMO management with the future employer regarding any restrictions on the participation of the officer in specific activities with the company. There is also the possibility of DMO management liaising with other companies who may perceive themselves to be disadvantaged by the move of the officer. For example, there may be competitor companies in a forthcoming tender.

Senator FAULKNER—Again, can you run that last one by me again?

Mr Lewincamp—Other companies may perceive themselves to be disadvantaged by the move of the officer. If there is a forthcoming competition, for example, and a competitor company sees that the move of the officer gives a particular company an advantage, we will liaise with that other company to reassure them about the processes that we have in place. Even in some cases we may contemplate providing some additional information to those companies to ensure that the level playing field is maintained. We have not yet had to do that.

Senator FAULKNER—These particular requirements are obviously in written form, are they? Are these requirements available to everyone who works in DMO?

Mr Lewincamp—No, they have not been broadly publicised across the organisation.

Senator FAULKNER—So they are not available. When did these requirements come into existence?

Mr Lewincamp—We put them in place at the time of Mr Croser's departure.

Senator FAULKNER—So they are new requirements?

Mr Lewincamp—They were introduced in January and we applied them in the case of Mr Gray's departure.

Mr Smith—That was the first time we had faced somebody at such a level with a potential involvement in industry matters leaving. So we seized that opportunity to get some advice and put the whole range of new measures that Mr Lewincamp has outlined in place.

Senator FAULKNER—You are saying to me, Mr Smith, that there were no requirements prior to Mr Croser's leaving?

Mr Smith—There were requirements but I do not think they were as rigorous as we have now made them.

Senator FAULKNER—What were the requirements then?

Mr Smith—I am not familiar with them off the top of my head. They were broadly about an assessment of the officer's involvement in any particular project or knowledge of projects and a judgment about whether that was likely to involve real or perceived conflict of interest. What is new here is, firstly, the statutory declaration and, secondly, the depth of inquiry. In my time here I have not seen a case as significant as these two, and I am happy that those arrangements have been developed.

Senator FAULKNER—That it is helpful to know but what I was asking is: what were the requirements prior to Mr Croser leaving DMO and were those requirements recorded somewhere?

Mr Lewincamp—There are a range of requirements that are set out in relevant legislation and manuals. For example, the APS code of conduct.

Senator FAULKNER—That applies to every public servant.

Mr Lewincamp—There are also some requirements under the Crimes Act.

Senator FAULKNER—What legislation are we talking about? Surely not just the Public Service Act?

Mr Lewincamp—No. There is the Crimes Act, for example, about the disclosure of information, and the Criminal Code Act. There are also the Defence Instructions (General) on post separation employment, which require current staff who are considering employment outside the organisation to seek approval for that employment. There have been cases where we have denied employment to employees who have asked for that type of work because of the conflict of interest or the perception of conflict of interest.

Dr Gumley—Over and above that, in most of the tenders there is a requirement on the company that might be doing the recruiting that they cannot take Defence personnel who have been involved in assessing the tender or writing the specifications. Depending on their level of involvement there is either a 12- or a 24-month prohibition.

Senator FAULKNER—But you are very cleverly, Dr Gumley, anticipating that I might go to tender processes. I have not raised tender processes.

Dr Gumley—You asked what other written documentation we had; that is in most of the tender documents.

Senator FAULKNER—It seems to me that the only thing specific to Defence, from what I have heard—and do not bother holding the front page of any newspaper for this—is that public servants working within Defence are subject to the provisions of the Public Service Act, the Criminal Code or the Crimes Act. I actually knew that and I think most people would have accepted that. What seems to me to be unique to Defence—from what I have heard in the evidence so far provided to this committee by Mr Lewincamp—are the Defence Instructions (General), which relate particularly to Defence employees. I just want to be clear on this. Is it fair to say that the Defence Instructions (General) are specific to Defence

employees but apart from that there is nothing else witnesses can point to for guidance in a situation where a senior official or an officer goes to the private sector?

Mr Lewincamp—There is one additional document of which I am aware—the defence workplace relations manual has guidance policy advice for employees in relation to post-separation employment. Mr Sharp may have further details.

Senator FAULKNER—We might come back to that. When were the Defence Instructions (General) about those transferring from Defence to the private sector written and when were they last changed?

Mr Sharp—I am unsure of the date of the original issue of the DI(G), the Defence Instructions (General), but they were revised in October 2005, and that concerns DI(G) PERS 25-4, 'Notification of post separation employment.'

Senator FAULKNER—Can you table the Defence Instructions (General)? These things are publicly available, anyway.

Mr Sharp—We can table it.

Senator FAULKNER—That has not changed since 2005?

Mr Sharp—It was revised in 2005.

Senator FAULKNER—What was the revision that occurred in 2005?

Mr Sharp—We attempted to make more explicit the obligations of a person who is contemplating a separation in terms of perceived and actual conflict of interest—to make a declaration to that effect to his or her supervisor. That is the principal emphasis that was given in those revisions.

Senator FAULKNER—I would appreciate it if you could table that. Thank you. Mr Lewincamp, when you went through that list of matters you indicated that from the beginning of this year, after Mr Croser's resignation, you would be requiring those who went to public sector employment to confirm their understanding of the obligations.

Mr Lewincamp—Yes.

Senator FAULKNER—What obligations were you asking them to confirm?

Mr Lewincamp—Not to disclose any sensitive or confidential information that they may have come across in the term of their public sector employment and not to make any improper use of any information they may have come across in their employment with us.

Senator FAULKNER—Where do I find those obligations recorded?

Mr Lewincamp—They are in the APS code of conduct.

Senator FAULKNER—That is right. There is no obligation specific to Defence at all? That is just the broad obligation that applies to each and every of the tens of thousands of Commonwealth public servants. Is that right?

Mr Sharp—The Defence Workplace Relations Manual is fairly explicit on this. It requires APS employees who receive an offer of employment within two years of separation to apply for approval to take up that employment if in their opinion an actual or perceived conflict of interest could be seen to exist. That is prior to and after separation.

Senator FAULKNER—It may do but of course there is nothing to prevent, as we can see, any senior official or military officer serving in DMO going straight into the private sector. If there is, I have not been told about it so please tell me if that is wrong. Can a person go straight out of the Defence Materiel Organisation and get plonked into the public sector or the private sector with a company dealing with Defence contracts?

Mr Lewincamp—As indicated by Mr Sharp, if the person is a current employee they will seek permission to do so. In the case of Mr Croser and Mr Gray, the CEO gave that permission. In the case of some other employees that position was not granted.

Senator FAULKNER—Are they still serving employees of Defence?

Mr Lewincamp—In at least one case, yes.

Senator FAULKNER—Let us go then to Mr Croser's specific case. He indicated his intention to leave on 23 January.

Mr Lewincamp—He did, yes.

Senator FAULKNER—He took leave immediately?

Mr Lewincamp—He was already on leave at that point. He started leave when he notified that he was participating in a process of discussion about the job.

Dr Gumley—He did come in for a day under supervision to tidy up the office and do a couple of debriefs.

Senator FAULKNER—What was the date of separation for Mr Croser?

Mr Lewincamp—Mr Croser wrote to the CEO on 25 January, asking permission to take up the employment, and Dr Gumley signed it on that day.

Senator FAULKNER—Did you say 25 January?

Mr Lewincamp—That is when he formally asked permission to take up that post-separation employment.

Senator FAULKNER—I thought you said that was on 23 January.

Mr Lewincamp—He notified Dr Gumley of his intention on 23 January, and that he had had a firm offer of employment from the company.

Senator FAULKNER—What is the date of separation?

Mr Lewincamp—I do not have that date here. He was on leave for a period of almost two months, so I think his formal separation was not until early March this year.

Senator FAULKNER—Mr Gray was the deputy chief of DMO, so was he your deputy, Dr Gumley?

Dr Gumley—Correct.

Senator FAULKNER—Mr Smith, the deputy of DMO is a very senior officer in the organisation; I am sure you accept that is the case. Is that right?

Mr Smith—Yes.

Senator FAULKNER—Does that necessitate even more careful consideration of post-separation employment and the sorts of issues we have been canvassing in relation to perceived conflict of interest and real conflict of interest? Do you accept that?

Mr Smith—I think, in the case of a deputy, the perception issue is probably greater. In the case of a real conflict, the issue has to be: what is the range of projects that they might have knowledge of, and the deputy would not necessarily have a deeper range.

Dr Gumley—Can I add to that. What we did with Mr Gray was get two public servants to review virtually every computer file he had looked at in the last couple of years. We looked through all the paper files and sorted them according to what might represent a real conflict of interest or otherwise. It is unusual for a deputy CEO to go to the private sector, and it required an unusual amount of our resources to make it a fair situation for any other tenderers or contractors. We put a lot of effort in and went through everything he had looked at, so as to work out what was fact and what might have just been perception.

Senator FAULKNER—So quite considerable resources went into this?

Dr Gumley—Absolutely. It was two or three people for two or three weeks. It was a constant review of documents.

Senator FAULKNER—And the cost of that exercise was borne by Defence?

Dr Gumley—It was borne by DMO.

Senator FAULKNER—I think you or Mr Sharp mentioned that Defence also engaged in some monitoring of possible outside employment or outside employment prospects. Did I understand that correctly?

Mr Sharp—Not quite. What we ask our civilian employees to do is, for the two years after they have left us, still seek our permission to take up a job where they perceive there is a conflict of interest.

Senator FAULKNER—So there is no Defence monitoring of this; this is a requirement that is placed on separated employees?

Dr Gumley—And their managers. My job is to ensure that DMO acts efficiently, effectively and ethically, and under the ‘ethically’ bit I had an obligation to ensure that future tender competitions would not be distorted by these moves.

Senator FAULKNER—Yes, I understand that completely. My question was: to what extent was there Defence monitoring? I have been told by Mr Sharp that that was not exactly what he meant. He talked about the self-assessment, if you like, of separated employees. I accept that. Are you now saying that Defence managers do monitor this? I am not clear on this. It seems to me that the evidence is not consistent. I just want to understand the situation. I have two different pictures now, and one of them is right and one is wrong—or they are both wrong. But they cannot both be right.

Mr Sharp—I think there is a sense in which we monitor. We do that through the contractors. We deal with the contractors and we generally have knowledge of people who are working with us. Equally, in our contracts we seek to place conditions on contractors that they

observe the same sorts of rules that we are talking about here in relation to conflicts of interest.

Senator FAULKNER—What do your managers do in this regard, Mr Gumley? Do they do anything in addition to what Mr Sharp has said? Is there any monitoring undertaken by senior managers in DMO in relation to this, beyond what Mr Sharp has just informed us of?

Dr Gumley—The general system is as Mr Sharp describes. When it was my very senior executives who were leaving, I imposed these additional measures that Mr Lewincamp has taken you through.

Senator FAULKNER—In terms of ongoing consideration of this, let us talk about someone who might have left the DMO six or 12 months ago. Is it your plan to monitor the circumstances that might surround their new responsibilities? It would be a bit difficult to do.

Dr Gumley—Of course it is difficult to do, and also you cannot deny people a living. People are entitled to use their skills in a future job. In the private sector lawyers jump firms and merchant bankers jump firms to their rivals; that is going on all the time. If you are in the private sector, the only way you can stop that is with lucrative contracts that, effectively, pay people not to work for a year or so. The Public Service does not have those arrangements, to my knowledge.

Senator FAULKNER—I think you are saying to the committee—if I can try to distil what you and Mr Sharp have said, Dr Gumley—that the onus is on the individual.

Dr Gumley—Yes, and I think I made a comment to a journalist about this some time ago; at the end of the day it is the ethical standards of the individual that we rely on. On that level, I cannot fault in any way what either Mr Croser or Mr Gray did. For example, Mr Gray had a conversation with me at about seven o'clock one evening; at eight o'clock the next morning I informed the secretary and at about 8:10 am we put in the IT restrictions and other things that we had to do. Mr Gray did not even have the job when he informed me; he just said he had been approached and he was going for an interview. At that stage I felt there was sufficient perception of conflict of interest that I needed to do something, and I did.

Senator FAULKNER—Did you engage any outside consultant or assistance with the separations in these two cases?

Dr Gumley—We learnt a lesson with Mr Croser. When I say a lesson, I mean we consulted Sir Laurence Street about the generality of the issue. He helped us compose a statutory declaration that we needed, and then we used very similar wording—not that any two stat decs can be identical—for Mr Gray's situation.

Senator FAULKNER—With what Sir Laurence Street did for Defence, was he engaged specifically to look first of all at both instances or to work on a generic statutory declaration?

Dr Gumley—No, it was an instance-by-instance situation.

Senator FAULKNER—So he did examine two discrete individual circumstances?

Dr Gumley—Yes, he did. He was available because he is the senior probity adviser for both the AWD and amphib projects. Therefore he was accessible to us, and was able to offer us the advice at short notice.

Senator FAULKNER—But you engaged him as a Defence consultant?

Dr Gumley—Yes, effectively.

Senator FAULKNER—In other words, did you pay him?

Dr Gumley—Yes, we are paying him.

Senator FAULKNER—How much did you pay him?

Mr Smith—I understand it was part of the contract that he has anyway, for the senior probity advising role on the AWD and amphibious ship projects.

Senator FAULKNER—So he is the Defence probity adviser, or one of them?

Mr Smith—He is the senior probity adviser for those two projects.

Senator FAULKNER—But is he a Defence probity adviser or is he the company's probity adviser?

Mr Smith—He is ours. He is engaged by me, yes.

Senator FAULKNER—So when I say 'Defence probity adviser' am I using the wrong terminology?

Mr Smith—No.

Senator FAULKNER—So he is the Defence probity advisor. You appoint a probity advisor. That is part of the normal process in relation to these major projects, isn't it?

Mr Smith—Yes.

Senator FAULKNER—The probity advisors are normally from outside Defence, aren't they?

Mr Smith—Yes.

Senator FAULKNER—Always?

Mr Smith—Yes. They are, for instance, from the Australian Government Solicitor, KPMG or someone like that.

Senator FAULKNER—So the point you are making is that it was not a special consultancy to deal with these particular circumstances. You actually had Sir Laurence Street available because he was undertaking this broader role.

Mr Smith—Yes.

Senator FAULKNER—What was Sir Laurence Street tasked to undertake in relation to the cases of Mr Gray and Mr Croser?

Dr Gumley—He was tasked to help construct the wording of an appropriate statutory declaration where Mr Gray and Mr Croser undertook not to use any sensitive Defence information in their future commercial activity.

Mr Smith—We recognised here that we were in a developing world—a more important world of probity—and because Sir Laurence was available to us and because the case of Mr Croser was a significant one, Dr Gumley said to me: 'Let's take this a step further than usual. Let's ask Sir Laurence for some advice on the best way to handle this issue.' That advice

included some of the steps that Dr Gumley took and, in particular, the notion of a statutory declaration, which Sir Laurence helped to prepare. I think from that we are developing a new body of practice, which I think will take us into the realm of best practice in this area, where we should be.

Senator FAULKNER—I do not think anyone would argue that you should not be in the realm of best practice. So I am clear on this, you are saying to committee that the broad parameters that need to be dealt with by any official or officer who is separating were provided in draft form, or shell form, by Sir Laurence Street as part of the functions he undertook. Is that right?

Dr Gumley—That is correct.

Senator FAULKNER—And this all happened post the separation of Mr Croser?

Dr Gumley—Yes. This happened about two weeks after we were aware that Mr Croser was leaving. He was on leave. As I said earlier, we felt that, because of the seniority of the people who leaving, we needed to take extra steps, so it is correct to say it was policy under development in reaction to a situation. What we learned out of the Mr Croser episode was rolled in within hours on the Mr Gray episode and worked very well there. There is another level to all this as well. In both cases I talked to the chairmen of the receiving companies and had discussions about the role, what that would mean and what the impact might be. I also talked to the chairmen and chief executives of the competitors of those receiving companies to hear of any concerns about fairness that they might have. So, again, in each case it was very resource intensive for, frankly, me to manage the probity framework appropriately for the separations.

Senator FAULKNER—Yes, but these separation procedures were developed after Mr Croser landed his new job.

Dr Gumley—That is correct.

Senator FAULKNER—But they were not developed after Mr Gray landed his new job.

Dr Gumley—No, because we used Mr Croser's version for Mr Gray.

Senator FAULKNER—That is right. I am just getting the timing right. They were developed after Mr Croser got a new job but before the matter regarding Mr Gray was finalised. Is that right?

Dr Gumley—Yes.

Mr Lewincamp—Just to clarify the time line here: Mr Croser signed the statutory declaration on 25 January, the same day on which he sought approval for the post-separation employment.

Senator FAULKNER—When was Sir Laurence Street engaged to do this?

Mr Lewincamp—Between the 23rd, when we were first notified about the possibility of the job, and the 25th.

Senator FAULKNER—So it was done pretty quickly.

Mr Lewincamp—It was done very quickly.

Senator FAULKNER—Obviously. This, I assume, is not a matter for Dr Gumley because in the other instance that has been mentioned, General Clifford, he did not work for DMO, did he?

Mr Smith—No. He is currently the head of the Information Capability Management Division within the CIO group.

Senator FAULKNER—The first and most obvious distinction, apart from not being in DMO, is that one is a uniformed officer and we talked previously about two public servants. Can you or General Leahy explain to the committee what different procedures might apply in the circumstance of a uniformed officer separating or leaving the ADF and taking an appointment in the private sector, which of the arrangements that Mr Lewincamp ran through apply and what are the circumstances surrounding General Clifford's separation?

Lt Gen. Leahy—The first thing I would say is that there are no provisions within the Defence Act or regulations or other legislation which restrict the type of employment that may be undertaken by ADF members after they leave the ADF. So we start from that premise. However, we do note that there may be either actual or potential conflicts of interest. Therefore, the DI(G) PERS 25-4—and you have mentioned that previously—was revised in October 2005, as Mr Sharp has suggested. This DI(G) encourages ADF members to submit a letter of notification through their chain of command if they receive an offer of employment that could give rise to a perceived or actual conflict of interest. It says that such employment should not be seen to give the proposed new employer an unfair advantage. The DI(G) further states that commanding officers are to ensure that ADF members wishing to take up post-separation employment are made aware of their obligations regarding disclosure of official, commercially valuable or in-confidence information gained in the course of their ADF employment. There is no time frame for ADF members to seek approval for employment after their separation from the ADF. That is the background, Senator.

Major General Clifford—who, as the secretary said, is the head of the Information Capability Management Division—wrote to me on 11 May this year. He addressed post-separation employment in an offer that had been made to him as managing director of General Dynamics Systems Australia Pty. Ltd. On 30 May—that is, yesterday—General Clifford's boss, Air Vice Marshal Monaghan, the Chief Information Officer, wrote to the secretary—and, Secretary, if you are happy, I will make some mention of what is in this letter—

Mr Smith—Sure.

Lt Gen. Leahy—about the potential conflict of interest for General Clifford. I will paraphrase from the letter: General Clifford has not been involved in any capacity nor had access to information related to the evaluation of tenders or source selection for this project. I will explain here that the project in question is joint project 20-72, and General Dynamics Canada has phase 1, which is a small part of a larger project.

General Clifford, as a senior officer, has had access to the Defence Capability Plan. He sits on various committees, including the Defence Capability Committee. The CIO made a further assessment that his involvement in these types of committees has not provided him with access to specific information of enduring value to General Dynamics in competing for future defence business. He might be aware of the scope but, given the stage of development—that

is, pre first pass—the value of this information is extremely limited. Conclusions were then made in that letter.

Again on 30 May—yesterday—the Deputy Chief of Army, who is my delegate on this matter, wrote to General Clifford addressing the post separation, and indicated to him that in his view—and this was after legal advice—there is no direct conflict of interest involved in this, although we will have to manage a perceived conflict of interest. He goes on in the letter to remind him of his responsibilities. I think it is appropriate that I quote what the Deputy Chief of Army wrote to General Clifford. When reminding him of his responsibilities, he quoted section 70(2) of the Crimes Act 1914, which states:

A person who, having been a Commonwealth officer, publishes or communicates without lawful authority or excuse (proof whereof shall lie upon him), any fact or document which came to his knowledge, or into his possession, by virtue of having been a Commonwealth officer, and which, at the time when he ceased to be a Commonwealth officer, it was his duty not to disclose, shall be guilty of an offence.

He noted that the penalty for that is imprisonment for two years. He then wished him warm regards and signed the letter. Yesterday, General Clifford—and we have been very conscious of the advice from the secretary and from Mr Gumley on watching what happened with the two gentlemen you were discussing previously—signed a statutory declaration stating clearly that he was aware of his obligations under the Defence Act, the Crimes Act and the Public Service Act and that he has undertaken not to make any improper use or disclosure of information.

Senator FAULKNER—Was it a requirement for General Clifford to sign that statutory declaration?

Lt Gen. Leahy—Not under any of the regulations, but I think it was a requirement in practice. I make the same comment about General Clifford: a very good and a very ethical officer. He is concerned about his position with his new company and certainly his position within Defence. I think he has done that in very good order.

Senator FAULKNER—So the nonrequirement—as I interpret it from your answer—for General Clifford to sign the statutory declaration nevertheless comes about as a result of the changes that Mr Smith and Dr Gumley have spoken about, which, of themselves, have come about from recommendations from Sir Laurence Street in relation to the two separations in DMO. Is that fair?

Lt Gen. Leahy—I think it is fair in that the DI(G) was last amended in October 2005. We saw the procedures develop with Sir Laurence Street on 23 January this year and we have developed that through, and I would not be surprised if the secretary or someone else would be saying that we probably need to review and include these new procedures in practice into the regulations.

Senator FAULKNER—Can you explain to the committee how Air Vice Marshal Monaghan was able to write in the terms that you outlined to the committee? Was some investigation undertaken by the air vice marshal or a delegate of the air vice marshal to allow him to come to these conclusions? I am not doubting the conclusions—I just want to understand the process of how he was able to draw them.

Lt Gen. Leahy—I would not feel confident doing that. I think it is properly a question for Air Vice Marshall Monaghan. I have his letter—

Senator FAULKNER—And he is also with us.

Lt Gen. Leahy—There we go—he is here.

Mr Smith—I should add two things to this. Firstly, in light of what Sir Laurence has advised and the way we have developed in the last few months, we will indeed amend that DI(G). Secondly, in the case of Major-General Clifford, CDF, Air Chief Marshal Houston, has asked for my advice to him on the matter. I will take into account all of this. I have a couple of other elements to follow up and I will give the CDF a final view on it.

Senator FAULKNER—I do not know if you heard my question, Air Vice Marshal—

Air Vice Marshal Monaghan—There was indeed an investigation undertaken. It is my understanding that there were two dimensions to this. The JP 20-72 was a project in process of management between the Capability Development Group and DMO. The DMO was asked for some advice with respect to their knowledge of 20-72. Of course, it would be quite unusual for DMO to share sensitive commercial information, but the question was asked anyway. Then within my own group I had an officer review for me the work of the Defence Capability Committee and advise me on any matters considered by the committee in the time that General Clifford has been with the group which might have some significant relevance to the General Dynamics parent company or the Australian subsidiary. The outcomes of that were that, while there were some minor matters that came before the committee, nothing of significance or value commercially would have been discovered through the committee processes. You would understand that, at that level, it deals far more with strategic acquisition issues than particulars of the commercial arrangements.

Senator FAULKNER—Did you task that officer yourself?

Air Vice Marshal Monaghan—I did. He reported directly to me.

Senator FAULKNER—Did you seek any legal advice or advice further up the chain of command as to the appropriate way of dealing with this? I would not be critical if you did.

Air Vice Marshal Monaghan—I did not. I provided the information back to the secretary, as did the CEO of DMO, and the information was brought together from there.

Senator FAULKNER—Are you able to say, General Leahy, why the Deputy Chief of Army sought legal advice? It seems a prudent thing to do, I have to say, but I wondered what the background to that was.

Lt Gen. Leahy—I am happy to say that I asked him to seek legal advice. I saw General Clifford's letter of resignation and I was aware that there had been other resignations or departures of this note. I thought it prudent, as you said, to seek legal advice. The deputy chief has done that.

Senator FAULKNER—Who did you seek legal advice from? Was it internal to Defence?

Lt Gen. Leahy—I cannot answer that specifically. The deputy chief has done that. You would have to ask him.

Senator FAULKNER—You might perhaps take that on notice.

Lt Gen. Leahy—Yes, I will take it on notice.

Senator FAULKNER—Thank you. I know there are some matters that Senator Bishop wants to follow through on with this. Mr Smith, you mentioned the need for Defence best practice in this area. I think that is a worthy objective. I am sure those of us on this side of the table would want you to have that as an objective. Isn't it true, though, that in a lot of other countries there are quite significant periods of separation—that is, officers or officials who are in similar circumstances to the cases that we have mentioned at this committee are prevented from taking such employment for a minimum period of time, often two years? That is pretty common. I think you would know that that is a pretty common practice. I am not sure how you are able to say to us in this circumstance that, if there is no such cooling-off period, Defence can hope to achieve best practice when you compare the situation with what is happening in comparable Western democracies.

Mr Smith—I have to say that, personally, I do not know what the practice is in other countries. What I am seeking is best practice within the Australian context, including the context of Australian law, in which I am advised that it is very difficult to constrain a person from selling his or her services. So it is in that context that we are working. That was the advice Sir Laurence gave us and, on that basis, we have developed a model which, as was explained, we have applied three times now.

Senator FAULKNER—Do you undertake any work to try to assess the sensitivities of the tasks that senior officers are undertaking in DMO with an eye to the sorts of issues that we have been canvassing here?

Dr Gumley—I am not sure of the question.

Senator FAULKNER—I am just wondering to what extent you, Dr Gumley, in your role, have to take account of these sorts of sensitivities in advance of being confronted with a decision or an approach by someone to move employment.

Dr Gumley—Of course, people are free to move employment whenever they like. Therefore, we have to have a system that protects us in the best way it can when they do choose to move. I can give another example of a military officer who left about nine months ago. He was going to go and work for a company. He did the correct ethical thing and said, 'I've been out fishing for nine months,' or whatever he was doing, 'and now I want to go and work for a defence company. I want to do project X, Y and Z.' I reviewed what he had done in his career previously, what he had been up to, and I said, 'I do not think there is a conflict; go ahead.'

It is actually in Defence's interest that good people move to industry and good industry people move to Defence. If we set up a system that stops that happening, we will have two tribes heading in opposite directions. We will have no understanding between Defence and industry. Very quickly I think you would find that our projects would slow down and the military would have less capability. So it does become a reasonable compromise in how we handle these issues.

Senator FAULKNER—I will ask this in a different way: can the fishing exercise that you just spoke about then—

Dr Gumley—I think this gentleman literally was fishing.

Senator FAULKNER—But can such a process itself have probity implications? I would have thought it certainly could. It is one thing to be made an offer; it is another thing to go looking for an offer. That is the sort of distinction I am trying, however effectively, to bring to your attention.

Mr Smith—It is a question. As I said, though, senior military officers in particular, knowing that their career is going to come to an end at the age of 48, 50 or 52, must be alert. We depend very much on their values. As we develop this new model, I have in mind something where officers, at the point where they make what they think is a pretty good application for a position or perhaps just when they are short-listed for it, would notify us. I do not think we can preclude them from keeping their eye open for opportunities.

Senator FAULKNER—Mr Smith, both you and Dr Gumley have stressed to the committee that these new procedures are a significant step forward. I think that is fair to say.

Mr Smith—I hope they are. I know they are.

Senator FAULKNER—Does that mean that the previous procedures and requirements were less than adequate?

Mr Smith—I think they were less adequate for the times than what we have now, but I think as well that it is part of the new culture of DMO that we have moved them up. The rest of Defence, in a number of areas, has learned something from DMO's business experience and is going to apply it.

Senator FAULKNER—I do not doubt that the procedures have improved. Obviously what has been outlined is better than the situation that existed prior to the latter part of January this year. But it does beg the question of whether the procedures that existed then were adequate and whether it was in a sense fortuitous that these improvements have been made, because circumstances came to bear that the existing Defence guidelines and procedures were not adequate to deal with. It seems like that might be a reasonable conclusion to draw.

Mr Smith—There is an element of that. There is also this element: Dr Gumley has been very quick to draw our attention to those sorts of issues—in a way that perhaps was not so in the past—because of his experience in business.

Senator HOGG—What happened in the pre-Croser situation, if I can put it like that? How many significant people have left—let us say within the last 12 months? What did you do with the people who left in that period if they were senior people? How many senior people left DMO during that period?

Mr Smith—The CEO left in September 2003. A couple of band 1 and band 2 SES officers left DMO to go elsewhere in the Public Service.

Senator HOGG—I am not talking about people who went elsewhere in the Public Service.

Mr Smith—I do not have an inventory in my head of people at that level who went from Defence to industry.

Senator HOGG—I am prepared to come back to it at a later stage. We still have a fair bit of time on this. If you could check which senior people have left in the last 12 months or so—and I am using when you became aware of Mr Croser's situation—from roughly 2005.

Mr Lewincamp—Can we put some boundaries on that question? Is it somebody who departs and then goes to private sector employment?

Senator HOGG—Yes. That is what I am looking at. I am not interested in anyone who has gone to anything unrelated to defence or who has gone elsewhere in the Public Service. I would like to contrast it with what has happened. One of the things that I can express—and I do not speak on behalf of people on another committee that I am on which is conducting an inquiry into shipbuilding matters—is that I have been concerned at the number of ex-Defence or ex-DMO people that we seem to be running into. That is why I am interested to get some sort of feel for what you did and how you treated those people in that period.

My second question, which you might also be able to address for me later, is about any people who left DMO with no other employment prospects, similar to your person who went fishing for six months, and subsequently took up employment within defence related industries. Have you identified any of those people and, if so, how many? What have you undertaken by way of approach to those people and are there any people who have knocked back your approaches?

Mr Smith—We will take that on notice. Let me say two things. As Senator Faulkner rightly suggested, and we did not disagree with this, the new procedures—let us say post-Croser—are undoubtedly more rigorous than before. That is not to say that the previous procedures were inadequate. Secondly, you are quite right about the shipbuilding inquiry. I would not say that it is a closed business, but it is a tight business. It is ex-Navy personnel and ex-shipbuilding personnel working with us. They go around. It is not as though there is a community of 1,000 people.

Senator HOGG—I am not looking at a conspiracy theory.

Mr Smith—It is absolutely fantastic, too, that some people from industry come and join DMO.

Senator HOGG—I am glad you raised that because that is one of the other things I was going to ask you about. We have heard of people going from DMO to industry. I would also like examples of people going from industry to DMO. I am glad you have raised your hand; you cannot leave the room!

Mr Smith—Three of our trumps have done this, and I take it that their companies have dealt with the probity issues they are in.

Senator FAULKNER—Mr Smith, do we have any examples—and Senator Hogg has asked a couple of questions to be taken on notice, and that sounds reasonable to me—in Defence over the last couple of years where disciplinary action had to be taken as a result of a conflict of interest issue? Has that matter come before you as secretary?

Mr Smith—It would come before me if it was at the one star or above sort of level. I do not believe that one has. As to whether there has been anything below that—

Senator FAULKNER—I ask Dr Gumley then the same thing for DMO. Are you aware of any cases?

Dr Gumley—I am not aware of any cases that have been band one star and above.

Senator HOGG—The other part of this question that I would like you to find out an answer for me on—and if we can we will come back to it at some stage—is this: have any people who have left DMO participated in part of a tender process of any significance led by DMO—let us say in the last 12 months, since 2004-05—and then gone to work subsequently for a successful tenderer?

Dr Gumley—We really only have visibility of the senior officers here. We do not have visibility of every single person who has left Defence.

Senator HOGG—I am aware of that. I am looking at the senior officers. Again, I am not inferring any impropriety whatsoever. I am just trying to get a feel for what has been the movement and what might have taken place in this pre-Croser situation. If you can get back to us on that, it may well mean then that we do not need to go down the path of any lengthy debate and discussion on this issue.

Mr Lewincamp—Yes.

Senator MARK BISHOP—I am aware that Senator Faulkner has raised the matter relating to former Air Vice Marshal Gray. I just apologise if I cover the same ground. When Air Vice Marshal Gray left DMO to take up his position with ADI earlier this year, no regulations were in existence requiring him to wait any period of time before he could take up such a commercial position, were they

Dr Gumley—No, there were no formal regulations.

Senator MARK BISHOP—It required probity and—

Dr Gumley—It required him to do the right thing. He did it precisely.

Senator MARK BISHOP—That is fine. I just wanted to check that there were no regulations. Air Vice Marshal Gray was the deputy of the DMO, was he not?

Dr Gumley—Yes.

Senator MARK BISHOP—I take it that there is a board of directors or a committee of management or some sort of control organisation that you report to?

Mr Smith—It is called the cabinet!

Senator MARK BISHOP—No, within the organisation itself.

Mr Smith—Firstly, he reports to the minister, of course, and through the minister to government. Secondly, in some respects, he reports to me but, more importantly, to the Defence Procurement Advisory Board, which was established as an outcome of the Kinnaird process. That board, of course, does not get into project management. It just oversees the change management program.

Senator MARK BISHOP—Is the Defence Procurement Advisory Board to be regarded as akin to the board of directors of a public company?

Mr Smith—No, it is not. It is an advisory board rather than, say, a managing board. As I said, its role is to advise on the implementation of the Kinnaird recommendations and the continuing process of change in DMO, but it does not have responsibilities, for instance, to oversight the budget or make staffing decisions. It does not have any involvement in particular projects.

Senator MARK BISHOP—Within the DMO—and Dr Gumley is the chief executive officer—is there a supervisory body, a supervisory committee or a reporting body that Dr Gumley reports to on a regular basis as the chief executive officer of a public or private company would report?

Mr Smith—It is the Minister for Defence.

Senator MARK BISHOP—Air Vice Marshal Gray's position was as deputy director—is that correct?

Dr Gumley—Yes.

Senator MARK BISHOP—He was your No. 2 man and he reported to you?

Dr Gumley—Yes.

Senator MARK BISHOP—Not separately to the minister?

Dr Gumley—No.

Senator MARK BISHOP—Or to the secretary of the department?

Dr Gumley—No, he reported directly to me.

Senator MARK BISHOP—In terms of major capital outlays for projects—ships, planes and that sort of thing—Air Vice Marshal Gray would have been reasonably familiar with the activities of the DMO, as you are, Dr Gumley?

Dr Gumley—Yes, but probably not as familiar. He does not, for example, sit on the senior committees, like the Defence committee. He did sit on other committees. There is a bit of a graduation there.

Senator MARK BISHOP—If you should, for whatever reason, be required to take a significant period of time off for illness, does the act provide for the deputy to automatically act in your position or is that subject to the decision of cabinet?

Mr Smith—It is a decision that Dr Gumley would take. He would probably discuss it with me and we would advise the minister. The automatic thing is that as deputy he would act in Dr Gumley's absence.

Senator MARK BISHOP—I presumed that. I just wanted to establish that. So Air Vice Marshal Gray would have had deep familiarity with the major work carried out by the DMO in terms of projects of acquisition?

Dr Gumley—He had knowledge of the projects. The question is: how much extra knowledge did he have over other officers or even over what is in the public? When you get to the more senior levels in DMO, you are not actually involved in every tender on a tender-by-tender basis.

Senator MARK BISHOP—I accept that.

Dr Gumley—So it is more general knowledge; it is more a management skill rather than a deeper project or tender situation type problem. When we looked at what he had been working on, we looked at his files and the knowledge that he had and then we worked out if there was a real conflict of interest against any of those tenders or projects.

Senator MARK BISHOP—But—correct me if I am wrong—Air Vice Marshal Gray is now the chief executive officer of ADI in Australia. Is that correct?

Dr Gumley—Yes, and effectively the country representative of the Thales group as well.

Senator MARK BISHOP—And the ADI is half owned by Thales and half owned by Transfield in this country?

Dr Gumley—Yes.

Senator MARK BISHOP—So he may not have a deep familiarity with particular contract specifications or particular contract documentation—I accept that comment—but, nonetheless, ADI are central to the second largest project over the next 10 years in terms of acquisition in this country. Is that right?

Dr Gumley—Yes—ADI is one of the top three contractors.

Senator MARK BISHOP—Yes. If it is successful it stands to gain government contracts in the area of shipbuilding, to what amount?

Dr Gumley—If they were successful on the amphibious ship project, it would be whatever the \$1 billion to \$2 million value is of the amphibious ship project. It is whatever is written in the DCP.

Senator MARK BISHOP—What is that?

Dr Gumley—I think it is \$1 billion to \$2 billion.

Senator MARK BISHOP—It is a little bit more than that, isn't it, for the amphibious ships?

Dr Gumley—It is very interesting that, when we went through and looked at the knowledge we had, I am prepared to reveal that part of the statutory declaration is that Mr Gray will not be involved with ADI's amphibious bid because we felt there was an element of conflict there.

Senator MARK BISHOP—You thought there was?

Dr Gumley—He has signed into his own statutory declaration that he will not be involved with constructing the bid until the very end, just before the bid might be put in, when, as managing director, he has a statutory duty of care to his company to check it through.

Senator MARK BISHOP—Yes, that is what I want to talk about.

Dr Gumley—So he himself recognised that there was a potential for conflict and has disqualified himself from that part of the business.

Senator MARK BISHOP—My problem is this. He is the chief executive officer of what you have called the third-largest contractor in this country.

Dr Gumley—It is one of the top three.

Senator MARK BISHOP—It stands to gain contracts worth many billions of dollars in particular projects in the next few years. The CEO of such a company—and you referred to him as the country representative of Thales, and that is correct—necessarily is responsible for the growth, development and wellbeing of that company of which he is CEO. At the moment, for ADI, that contract is absolutely fundamental to the wellbeing and growth of that company. How can a person such as he, who has been recruited to advance the interests of that company, just divorce himself from skills, knowledge, expertise and information that he necessarily built up during the period of his employment and his career with DMO? They hired him to use his knowledge.

Mr Smith—They hired him because he is a very competent man. He knows about project management. There is no question of it. We welcome him going there, incidentally, in that sense.

Senator MARK BISHOP—But, really, the conflict is just so apparent and so untenable.

Dr Gumley—I disagree with you. At the general level he has the skills and he will be a very good managing director for ADI and Thales in this country. He has disqualified himself from the specific information as related to the amphibious ship project. Any person is entitled to leave a job in this country, go to somewhere else and use their general skills.

Senator MARK BISHOP—They are. I am not saying that he is not entitled to leave the DMO. I am not saying he is not entitled to make himself available for a position in private industry. My concern is what I regard as just such a clear potential for conflict in his carrying out of the job of that major company—ADI. I just do not know how the head of any organisation can ignore or not have regard to a potential contract of that size and divorce himself from the future wellbeing of the company that employs him. You could not do it in the DMO. Mr Smith could not do it in the Department of Defence. Why should Mr Gray be expected to do it in working for ADI? How can you divorce yourself?

Dr Gumley—He did not have access to specific information on the amphibious ships project. Despite all of that, he has been quite prepared, because of the perception issue, to disqualify himself from the individual detail of this project.

Senator MARK BISHOP—Do you regard that self-disqualification as acceptable?

Dr Gumley—Yes, I do. I made a statement earlier that it ultimately comes down to the ethics of an individual. I have no question or doubt about Mr Gray.

Mr Smith—Moreover, he will be transparent to us. All of his work, pretty well, is with us. We will know what he is doing. If he appeared in that project contrary to his statutory declaration, we would know.

Dr Gumley—ADI will have to be careful, because, if he does appear and do the wrong thing by the statutory declaration, the chances of ADI winning the tender, I think, would be very small.

Senator MARK BISHOP—Does DMO have any involvement in the tender preparation committee within ADI apart from the provision of information and the like? Do you observe their process?

Dr Gumley—No, they are a private company. They have their own process.

Senator MARK BISHOP—That is right. They are a private company and they have their own rights and processes.

Dr Gumley—This is a constant theme. This goes on in companies, and has done, for 30 or 40 years. People leave one employer and work with another employer which might be in competition or in the supply chain. It is very regular.

Senator MARK BISHOP—I accept that—people change companies every day of the week. But Air Vice Marshal Gray is charged with the responsibility of the future of ADI, and its future is inextricably linked to success or otherwise in the amphibs project. And I just do not understand—

CHAIR—With respect, I think that misses the point that ADI's future success rests with successful project management. If I might say so, former Air Marshal Gray has a very strong track record in management of projects—the Wedgetail project he delivered, if I might be so bold. There are management issues here. It is not about taking information from DMO and how the tender process works. It is project management that I think ADI is seeking. If you are saying that there is a conflict between taking the skills of project management—

Senator MARK BISHOP—No, I am not.

CHAIR—Well, I think that is why he is in ADI: he is the managing director because of the management skills.

Senator MARK BISHOP—I am not raising the issue of project management at all. That is an issue raised by Dr Gumley. I am raising the issue of Air Vice Marshal Gray's responsibility as the most senior officer in ADI. I am arguing that is linked to the future of the company. That is the conflict, not project management.

Senator FERGUSON—Chair, I think if we are going to resort to having a debate on this issue then the place to debate it is in the Senate chamber not at estimates.

CHAIR—That is right.

Senator FERGUSON—Estimates is a totally different process, and we are here debating the merits of one or another appointment. If we are going to start debating at estimates we will be here for three weeks not two days.

Senator MARK BISHOP—I accept the comments made by Senator Ferguson. I will cut to the chase. I put on record the concerns of the opposition in this area, and it will be attended to in another place. I am happy to move on. But I have not finished the discussion yet—I want to turn to another alleged conflict of interest. It involves Dialog Pty Ltd and Australian Base Service Pty Ltd. I refer to a press article in the *Fin Review* on 14 December 2005 and a subsequent article in the *Fin Review* on 24 February 2006 concerning a then serving RAAF officer who went on long service leave and sought and received approval to engage in employment, whilst on long service leave, with a company involved in tendering for a contract. He was particularly involved in, hired and approved by the RAAF, as I understand it, to participate and assist in that tender process. I understand that series of events has been the subject of investigation by the inspector general and that the inspector general brought down a report on the matter. Are you familiar with the facts of the case, Dr Gumley?

Mr Smith—Dr Gumley is not but I am. I said earlier that I would not normally see these things if they were below about one-star level but I do recall that case and I remember what we did about it. Mr Henderson is aware of it. We do not have any paperwork in front of us so we will be talking from memory.

Senator MARK BISHOP—The officer concerned was reported in the press to be employed whilst on leave by a company preparing a tender bid. The reporter quoted the officer as saying, ‘I have a signed approval from Defence to do this work.’ Do you have knowledge of this case, Mr Henderson?

Mr Henderson—Yes, I do. The tendering process related to the market testing of our regional IT support system, which is a possible outsourcing project with a scope of up to 400 or 500 civilian positions. There are six tenderers, one of which is an in-house option. The person you are talking about was employed by one of the tenderers to assist in the preparation of their tender documents. The case was examined, as you said, by the inspector general, as well as by the lawyer who was acting as the probity adviser for this market-testing process. The conclusion was reached that the person concerned had general familiarity with IT systems in the ADF but had absolutely no specific knowledge relating to this market-testing project and, in fact, had not even worked in the Corporate Services and Infrastructure Group that was managing this tender process. The probity adviser, as well as the inspector general, came to the conclusion that the firm that she was assisting had gained no advantage as result of her participation in preparing some of the documentation, and so I advised the other tenderers and the company concerned that their tender would be evaluated and the process would continue as planned.

Senator MARK BISHOP—You say that there was no conflict of interest between the officer’s duties and the work required in the tender company and that that was confirmed by the probity adviser, but that the officer was found to be in technical breach of defence regulations.

Mr Henderson—That related to the person’s employment in the particular service—it was Air Force, I think.

Senator MARK BISHOP—It was.

Mr Henderson—I am not across that. I have a vague recollection, but it would be better if somebody else answered that or we took it on notice. However, in relation to the tendering process, the question was: did that person’s experience give that company an unfair advantage vis-a-vis others? The answer was no.

Senator MARK BISHOP—I understand that a decision on this project was originally expected in May this year but it has now been pushed back to December of this year. Why is that?

Mr Henderson—In our preliminary judgments as to how long the evaluation process would take, we were assuming that we would have a similar number of compliant tenders to what we had for the market testing of the central network systems, which eventually was outsourced to a company called KAZ, which is a subsidiary of Telstra. In that case, there had been two private firms and an in-house option. In this case, as I said before, we have got five private tenderers and an in-house option. Because of the scope of the work and the number of

tenderers, it probably is going to be the end of this calendar year before we reach a final judgment on whether we are going to outsource it, give it to the in-house option, or in fact just continue with business as usual. So, basically, the number of tenders to evaluate was larger than we expected.

Senator MARK BISHOP—I must say that six tenderers does not strike me as being an excessively large number of tenderers to evaluate.

Mr Henderson—I mentioned the scope, in terms of the workforce involved, with somewhere between 400 and 500 civilian positions distributed right across the country, so this a substantial contract—

Senator MARK BISHOP—And it is a \$400 million contract—that is \$40 million each year for nine or 10 years, as I understand it—so it is significant contract. There would be a significant degree of industry interest. I am just making the point that I would not have thought that six tenderers would be either excessive or unanticipated on the part of your organisation.

Mr Henderson—I explained that it was double the number of people that expressed an interest in the previous recent market testing of IT support in Defence.

Senator MARK BISHOP—Is there an officer available who can tell me about the technical breach of regulations that the officer was engaged in? Is that person available?

Mr Smith—Are you aware of them, Peter?

Mr Sharp—No, I am sorry.

Mr Henderson—It may well be that if we just dig out our briefs for the February Senate estimates we might be able to get you the answer either tonight or tomorrow morning.

Mr Sharp—I can outline the policy for you.

Senator MARK BISHOP—Yes, thank you.

Mr Sharp—We have a policy in relation to employment and involuntary activities of ADF members in off-duty hours, which is a somewhat long way of saying that includes people who may be on leave and who wish to take employment. The context, of course, is that Defence seeks to facilitate transition of ADF members out of the ADF into employment and, indeed, in doing so we encourage people to consider their next career in one of the wider workforce components of Defence, if I might call them that—namely, the Defence public service and defence industry. However—and this is set out Defence Instruction (General) 25-2—prior to somebody going on leave and seeking and taking employment they are to seek approval as part of applying for leave. They are encouraged to discuss with their supervisor what employment they are contemplating and to include in the discussion any particular possibilities of conflict of interest.

This incident has highlighted perhaps that the policy is not being followed as punctiliously as we would like. We are currently looking to strengthen it somewhat so that we avoid the sort of circumstance that occurred here, where the approval came very late in the scene—that is, there was no prior discussion, as I understand it, of the matter until the end game.

Senator MARK BISHOP—When you say the end game, you mean that the officer was about to take it up employment with the company?

Mr Sharp—Yes. Supervisors' decisions are given in writing and kept on file.

Air Marshal Shepherd—I recall the brief from the previous Senate committee. We are chasing the brief up and it will be here before dinner, I hope, but certainly after dinner. I think the technical breach was that the officer in question had not sought written approval to conduct employment whilst on leave, but I will confirm that when the brief comes and read that into the transcript later on.

Senator MARK BISHOP—Was that the only technical breach that was found by the inspector general?

Air Marshal Shepherd—I do not want to trust my memory any further.

Senator MARK BISHOP—Okay. Perhaps we might adjourn that discussion until you have got the brief.

[5.59 pm]

CHAIR—We have moved from the overview and capability development and we will now be on outcomes. We will move to the Defence Materiel Organisation and outcome 1, and Adelaide class frigates, the FFG upgrade, is the topic of conversation.

Senator MARK BISHOP—At the last round of estimates I put some questions on notice and I have received a response. I thank the DMO for that. I will refer in particular to answers to questions W3 and W24 at this stage. In respect of the *Sydney*, you advised in the answer to paragraph (o) of question W3:

Contractor handback for HMAS *Sydney* is expected to be the end of April 2006. This will be with known deficiencies to contracted capability and a program to correct these leading up to December 2006, when Provisional Acceptance may be achieved.

What are those known deficiencies? Will they be corrected? If not, what is going to be the lost capability and what offsetting savings are being considered?

Rear Adm. Ruting—There is a long range of questions there. If I may, I will work progressively through them. Please remind me if I miss any of the latter ones.

CHAIR—Okay. Perhaps you can deal with known deficiencies first.

Rear Adm. Ruting—Yes. When *Sydney* was handed back on 28 April, a whole range of the systems were accepted as meeting the contracted requirements for performance, but we may not have had all of the logistics support documentation provided with them. However, that is in the process of being progressively delivered between now and the planned original acceptance period.

When it comes to the combat system areas, there are some identified deficiencies in some of the systems. For example, the underwater systems, the sonars, did not achieve all of the test requirements during the category 5 tests. People from ADI; its primary underwater systems subcontractor, Thales Underwater Systems; Defence Science and Technology Organisation; Navy; and DMO have been meeting over the month of May, looking at the improvements that are needed in that particular area and analysing the test results to look at what additional work

needs to be done on the underwater systems that affect the three sonars: whole mattered sonar, the patrol obstacle avoidance sonar and the towed array torpedo detection system.

Senator MARK BISHOP—Are they pretty important pieces of machinery?

Rear Adm. Ruting—All three of those are important to the capability of the FFG. In the case of what is called the electronic support measures system, which detects a wide variety of radio frequency transmissions, there are some known difficulties as well, so it does not meet the performance requirements as yet.

In the higher-frequency areas, it is more positive than in the low-frequency areas; many ES systems have difficulty in very low frequency areas. So that is another system that has not been fully proven as yet.

The combat management system, referred to under the acronym ADACS, has not achieved as yet all of the requirements of the contract. What must be recognised in the FFG contract overall, though, is that it allows ADI to progressively build up the total capability to achieve the contract. In fact, over at least the first three ships and therefore into the fourth ship, ADI had chosen—

Senator MARK BISHOP—I am sorry; can you say that again.

Rear Adm. Ruting—It allows ADI to progressively build up to the full contracted capability over the four ships. It would then retrofit to the first three delivered ships subsequent upgrades in the fourth ship. Final contract approval of the total four-ship package may not occur until after delivery of the fourth ship and the retrofitting of any final improvements in the three earlier ships. A lot of it is software based improvements in a number of systems; they can progressively deliver the various improvements.

ADI has chosen to do this over three baselines. Baseline build 1, which is what HMAS *Sydney* is to be delivered against, has to meet a requirement of the ship being no less capable than we started with—that is, before the contract, which is quite understandable.

Senator HOGG—That is a very good starting point—no less capable!

Rear Adm. Ruting—Then they can build up. What ADI have chosen to do over those three baseline build levels is deliver all of the basic capabilities there—

Senator MARK BISHOP—This is the refit we are talking about, isn't it?

Rear Adm. Ruting—This is the upgrade. This was in the original contract, signed in 1999. It allowed them to progressively deliver the capability. In baseline build 2 they will increase the software capabilities to also incorporate the evolved Seasparrow missile capability. And in baseline build 3 they plan to incorporate the full Link 16 combat datalink capability. Those are the two primary capability gaps that would be not delivered with HMAS *Sydney* in her initial arrangements.

Senator MARK BISHOP—So we could progressively accept refitted frigates over a period of years and use them in deployment, but the contract allows for the work on the systems that you identified not to be concluded until the final ship is accepted by Navy. Is that what you have just told me?

Rear Adm. Ruting—That is a fair summary of what the original contract in 1999 allows.

Senator MARK BISHOP—I am not greatly experienced in this area so I presume such a provision is kosher. Dr Gumley, if you were now tasked with negotiating the same refit of the frigates in 2006 or 2007 would you require such a delayed provision to be a part of the contract?

Dr Gumley—It would depend very much on the technology. What we have got here is a form of spiral development going on. It was clear that the previous combat system architecturally had run out of puff. It was not capable of further improvement. You then have to rip it out and put a new one in. So it is perhaps not unusual that it starts with no lesser capability than the old one, but at least this new one is capable of growth. What we have got here is three spiral developments of growth.

Senator MARK BISHOP—Yes, but when is the fourth ship coming?

Rear Adm. Ruting—Provisional acceptance of the fourth ship will now be in 2009.

Senator MARK BISHOP—So we will not have full capability until after 2009.

Rear Adm. Ruting—The contract amendment that has just been negotiated and completed, with the signing of the deed on Monday, envisages in fact that all of the capability will be delivered by 2009.

Senator HOGG—If I can just butt in for a moment, I am lost here in terms of process; I will not go to anything else. The first three ships that receive their upgrades will have to go back for a further refit?

Rear Adm. Ruting—No; in fact it is almost all software changes in those subsequent upgrades.

Senator HOGG—So it is downloading software. My next question then is: how long will the ships be taken out of service to allow the download of the upgraded software to take place?

Rear Adm. Ruting—I do not have that detail with me from the latest high-level contract master schedule information that was completed in negotiations.

Senator HOGG—Can you find that out for us. It would be interesting to know whether it is going to be a matter of weeks or months or even a year that they will take the ship out of action.

Rear Adm. Ruting—If I can generally cover that, in almost all of the cases that are being planned it is more a case of weeks that may run into perhaps two months, and it is planned that that will be conducted during routine maintenance availabilities of those ships.

Dr Gumley—And then, of course, the crew has got to work up and train on the new capability that has been added.

Rear Adm. Ruting—Yes.

Senator MARK BISHOP—Okay. These three contracted known deficiencies: is that the bulk of them, or are there others?

Rear Adm. Ruting—They are the main areas where the deficiencies are. There is a large number of systems on the ship that comprise the overall combat system as such and there are some logistics support and other deficiencies across—

Senator MARK BISHOP—But those are the main areas of deficiency?

Rear Adm. Ruting—They are the main areas of deficiency.

Senator MARK BISHOP—To this untutored civilian, the combat support systems in terms of underwater technology, the electronic support measures system and the combat management system strike me as being fundamental to force projection for these frigates. Is that right?

Rear Adm. Ruting—Certainly the combat management system is vital to its operational capabilities.

Senator MARK BISHOP—The sonar is pretty useful in getting to the place where you want to project the force from.

Rear Adm. Ruting—Sonar is one of a number of sensors systems, and certainly it is the only one that provides you with underwater information apart from the echo sounder, but it does not stop one from deploying to a geographic location.

Senator MARK BISHOP—No. The engine still works. We know that I am not talking about that. I am talking about, without effective sonar, the ship being taken out before it is able to project force. For those frigates to be effective force projection tools for the Navy, all of these contracted deficiencies have to be rectified, don't they?

Rear Adm. Ruting—That is correct. Before we gain the full capability that was envisaged and contracted, we do need to have all of those.

Senator MARK BISHOP—In fact, without a full degree of rectification of the combat system, the electronics system and the combat management system, we do not have an effective force projection platform in the FFGs, do we?

Rear Adm. Ruting—There is correct.

Vice Adm. Shalders—I might just correct that from an operator perspective. The *Sydney*—

Senator MARK BISHOP—Rear Admiral Ruting said it was right.

Vice Adm. Shalders—I am not sure that I heard the question correctly but let me reassure you that the *Sydney*, which was the ship that was accepted on 28 April, is at sea and she has quite a decent capability. There are deficiencies. Those deficiencies will be rectified. But the *Sydney* is actually operating now. She sailed on the Monday after she was accepted and she assisted in the work-up of HMAS *Kanimbla*. She has the same capability as the *Adelaide*, for example, which was sitting off Dili harbour five days ago. So I would not want you to have the impression that this is a ship that does not work. That is not correct.

Senator MARK BISHOP—I was not suggesting for one minute that the ship did not sail and it could not go into areas where there were no enemy activities. My concern is the use of the platforms in areas of conflict where the platforms themselves might be under attack. That is where they are unable to be used until the known contracted deficiencies are rectified. That is the point that Admiral Ruting was making.

Vice Adm. Shalders—I understand your point but, for example, in terms of its air warfare capability the ship has fired successfully, using the new combat management system, its current SM1 missile. It is capable.

Senator MARK BISHOP—Yes, it is capable to a degree, but it has not achieved the requirements to date of the contract.

Vice Adm. Shalders—Correct.

Senator MARK BISHOP—That is right. That is the point. Do those known deficiencies have to be rectified?

Rear Adm. Ruting—Those that are known deficiencies against the contracted capabilities, yes, will have to be rectified before we can take final acceptance of the four FFGs against the contract.

Senator HOGG—Can they be rectified? That is a quite different question.

Rear Adm. Ruting—That is a technical issue that I would not be able to give an absolute answer on. We are doing further work. In the underwater systems case, for example, the Defence Science and Technology Organisation, our own people, Navy, ADI and Thales Underwater Systems, who are the underwater subcontractor to ADI, are all working together on identifying the detailed results of the trials. From that ADI and TUS can then look at what improvements they need to make in those sonar systems, for example, to achieve the capability.

Senator HOGG—So it is a matter at this stage that the specific rectification necessary has not been identified. Is that correct?

Rear Adm. Ruting—In some of the systems, that is correct.

Senator HOGG—What sort of time within the contract is there for the identification of these system deficiencies?

Rear Adm. Ruting—In the case of HMAS *Sydney*'s capabilities, ADI have identified that they believe they can rectify what they need to to achieve what I call baseline build 1 standard by the end of 2006.

Senator MARK BISHOP—What about baseline 2 and 3?

Rear Adm. Ruting—They had planned that the second ship that is already in upgrade now, HMAS *Melbourne*, should be able to be delivered with baseline build 2 capability. It may be possible that in fact they can achieve that extra step to get from baseline build 1 to baseline build 2 prior to *Melbourne* completing all of her upgrade. In fact, that could be fitted into *Sydney* prior to that time, but they are contracted to achieve it progressively, as I say, up to baseline build 3 being delivered by the fourth ship.

Senator HOGG—What if they cannot? You have said there are some things that at this stage they do not have a specific solution for. Is there a problem that they might not be able to rectify?

Rear Adm. Ruting—There may be. I cannot postulate whether there is or there is not. At this point in time, we are progressively working through the delivery of very complex and very heavily software based solutions in a number of these systems. As the CEO commented,

it is a spiral development process, where you develop up to a certain baseline, do some pretty extensive testing on that and get further information—which you then use to develop the solutions up to the next step of complexity and capability of these very complex systems.

Senator MARK BISHOP—What is going to be the extra cost, if any, to us in rectifying the three known contract efficiencies?

Rear Adm. Ruting—There will be no extra cost to the Commonwealth. This is a fixed price contract. ADI is required to deliver that capability within that price.

Senator HOGG—What about the additional training that will be required? Who will meet the cost of that?

Rear Adm. Ruting—The additional training for each of those additional steps that are required in capability is covered under the contract. Some of the early training for the first two ship crews was covered under the contract, and DMO and Navy will then pick up training for additional crews after the first two crews. Some of it is covered under the contract and some of it, for additional crews, is actually being paid for.

Senator HOGG—I might not put this in the correct terminology but, as I understand it, by the time you get to ship 4, ships 1, 2 and 3 will be downloaded with the latest versions of the software—is that correct?

Rear Adm. Ruting—It may be, or ADI may have downloaded the very final version for the last ship and the last baseline into the first three ships.

Senator HOGG—All right. My question, though, is: will there be additional training needed at that stage and who will meet the cost of the additional training to be able to operate the enhanced software that is downloaded to ships 1, 2 and possibly 3?

Rear Adm. Ruting—I will have to take that detail on notice. I am not fully across all of the aspects of the training element of the contract.

Senator HOGG—I accept that. Is it a cost to the Commonwealth or is it a cost in the agreement with ADI? That is all I need to know, thank you.

Senator MARK BISHOP—I want to go back to the question W3 paragraph (1), which indicates the existence of powers of liquidated damages in the event of failure to deliver specifications. Will the known contract deficiencies to date trigger those damages?

Rear Adm. Ruting—Because we have just renegotiated the overall contract schedule for a four-ship program rather than, as previously, a six-ship program there are a new set of dates now for the delivery of the ships and there are a whole range of milestones for provisional acceptance of the ships and also for acceptance of the software because, as I mentioned, they could actually be delivered separately because of the spiral upgrade arrangements. Those new trigger dates will be the points at which we assess whether the capability has been met. And if it is delayed until after that, liquidated damages would accrue from those new milestone dates to when they were able to achieve the required capability.

Senator MARK BISHOP—So the new contract overrides the previous contracted liquidated damages provision?

Rear Adm. Ruting—Yes.

Senator MARK BISHOP—The old contract had a ceiling for liquidated damages of \$10 million, I think.

Rear Adm. Ruting—Correct.

Senator MARK BISHOP—What is the ceiling in the new contract?

Rear Adm. Ruting—The ceiling in the amended contract from the deed is still a total of \$10 million. However, the rate at which they accrue is a much steeper rate per day than it was previously, to provide additional incentive to complete on each of those milestone dates.

Senator MARK BISHOP—Is that figure of \$10 million liquidated damages for each contract violation separately or is that the total for all contract violations?

Rear Adm. Ruting—That is the total.

Senator MARK BISHOP—In that context, \$10 million is a fairly minimal amount of damages, isn't it? Why is it so minimal?

Rear Adm. Ruting—I do not know why it was originally set, back in 1999, at that fairly small figure of \$10 million total. But in renegotiating the package across the change from six ships down to four we were not able to get an overall increase in that amount. However, as a percentage of the profit that ADI would make on this overall contract it does become a much more significant element.

Senator MARK BISHOP—That just tells you their profit is minimal on this contract. That is what you just told me then. What has been the cost to DMO for the legal advice involved in this extensive contract renegotiation? The answer advised us that there had been 174 project change requests alone. What has been the cost of legal advice, both internal and external, involved in this contract renegotiation?

Rear Adm. Ruting—In this latest phase that has been going on over the last five months? I do not have the final bill for that. I would have to take that on notice. But as we are still in the process of executing the actual contract amendment—we have signed the deed as of Monday—there is still further action to go on, so it will not be closed probably for another month or so to be able to give you the final figure.

Senator MARK BISHOP—Can you give me a ballpark figure, Admiral?

Rear Adm. Ruting—I will obtain that information. I do not have it available at the present moment because it is ongoing.

Senator MARK BISHOP—Of those 174 project changes that you advised were requested in the answer to the question on notice, how many of those related to the issue of damages and contract failure?

Rear Adm. Ruting—I do not believe any of those particular contract amendments that have been executed to date were related to the imposition or invoking of liquidated damages for the late delivery or non-performance of equipment. They were all associated with other changes to the scope of the work or to correct minor anomalies in the contract.

Senator MARK BISHOP—How much has been paid to the contractors to date from the total funds available for this project?

Rear Adm. Ruting—To the end of April, which are the figures that I have here, we have paid \$950.56 million against the prime contract and \$54.25 million against other project expenditure.

Senator MARK BISHOP—How much is left outstanding—about \$400 million, is that right?

Rear Adm. Ruting—The total project approval is currently \$1,467 million.

Senator MARK BISHOP—So it is roughly \$467 million. When is that due to be paid? Firstly, is any portion of that \$467 million to be paid only at final Navy acceptance and approval of the fourth ship?

Rear Adm. Ruting—Yes. As a result of the major contract amendment we have just executed—at least as far as the deed for that on 29 May is concerned—we restructured almost all of the remaining payments to reduce the amount that was being paid by earned value and increase the amount being paid against milestones. We introduced a number of new milestones into that payment regime, and certainly there are milestones against software capability and also milestones against a final contract acceptance, as well those for each of the ships when they are delivered.

Senator MARK BISHOP—Do any of those milestones that you have introduced relate to rectification of the known contract deficiencies that we were discussing earlier?

Rear Adm. Ruting—They do for those milestones which set the times at which we will accept those various equipments, and so we do not pay for the final completion of some of those deficiencies until they are demonstrated by the appropriate tests, trials and documentation. At that point in time we would make, for example, a milestone payment that will—

Senator MARK BISHOP—How many more milestone payments are there now?

Rear Adm. Ruting—I will have to take that on notice as to how many remain.

Senator HOGG—Can you give us a chart that tells us when the milestones are due and what the payments due at those milestones are for?

Rear Adm. Ruting—That will be in one of the annexes of the about to be amended contract, and so when we have completed that particular annex—I think it is attached to the deed, one of the many attachments to the deed—it will have a list of all of the milestones.

Senator HOGG—But if it is in a complex and lengthy form—we are looking for it in a semi-simplified form to what you might otherwise have it in, Admiral.

Rear Adm. Ruting—Because the actual contract itself and all of the details inside it in that sense are commercial-in-confidence, I would not be able to identify all of the dollar payments against those milestones, but I can give you the list of what all of the milestones are.

Senator HOGG—You are not even able to give us a ballpark figure? Otherwise, we have no idea of how this is progressing. That is the difficulty. I understand that there are commercial sensitivities, and we cannot take things that are commercial-in-confidence at the estimates hearings. But if you can work out some way that lets us see what the progression is,

we can ask more pertinent questions next time around. Otherwise, we spend time hauling over this same ground. I do not know how you would do it, but I am sure there must be a way.

Dr Gumley—I think you are after some assurance that the ADI has got some skin in the game against performance. Is that correct?

Senator HOGG—Yes.

Rear Adm. Ruting—What I can indicate is that across this fairly comprehensive list of milestones the total amount, perhaps for all of those milestones, is more in the order of 60 per cent of the remaining payments due under the contract. It is in that order.

Senator HOGG—We are not after every minor milestone that you people are coming up to. We want to know what the significant ones are, so that we have some idea where we can place our questions.

Senator MARK BISHOP—I think the issue raised by Senator Hogg is fairly important in this context. This project has reduced ship numbers from six to four, it has blown out now in terms of delivery times by some three or four years, you have identified a series of fairly critical known contract deficiencies, and you have renegotiated the contracts and the payment dates for the outstanding three or four years. There has been a lot of discussion in the press—some justified; some not so justified—in recent times about some failures. I think it would be advisable if we could be assured that the ships we have contracted to purchase will only be paid for consistent with the new contract if and when they deliver the capability that projects the force that we have been regularly assured that we are getting in terms of this project. I make those comments in light of Senator Hogg's request for some sort of confirmation.

Mr Smith—Just to clarify one thing, this project did not reduce the number of ships from six to four. That was a government decision taken for reasons separate from the contract.

Proceedings suspended from 6.33 pm to 7.34 pm

CHAIR—We will continue with the DMO.

Senator MARK BISHOP—My question now probably goes to you, Mr Smith. With regard to the Seasprite matter under discussion in the last two or three weeks, Minister Nelson announced that he was going to request Defence to do a review and come to him with a number of recommendations. In that context, has there been any recommendation from Defence to Minister Nelson that there be a review of the refits for the Adelaide class frigates?

Mr Smith—Not that I am aware of. I am always cautious about belying what advice we have given to the minister, but I think that one is straightforward.

Senator MARK BISHOP—You would be aware of that?

Mr Smith—I would, yes.

Senator MARK BISHOP—So there has been no recommendation for a review?

Mr Smith—Not that I know of—we can check it with Dr Gumley.

Senator MARK BISHOP—Who is responsible for the renegotiation of the frigate refit contracts? Is that Dr Gumley?

Mr Smith—Yes.

CHAIR—Anzacs or Adelaides?

Senator MARK BISHOP—The Adelaides—the same subject we have been discussing. You have indicated a few times, Admiral, that the contract has been renegotiated, and my understanding is that it is now in the drafting stage and ready to be signed off on—is that correct?

Rear Adm. Ruting—On Monday, 29 May ADI senior principals and deputy CEO of DMO signed a deed of agreement that incorporated all the major agreements out of this renegotiation. That will then flow straight into the detailed contract amendments that will update the contract. Attached to that deed was a range of attachments which update the contract attachments, so to a large extent that has all been agreed in all the principles and now it is just the mechanics of the physical update of the contract itself and the signing of it.

Senator MARK BISHOP—Has that now become a job for the lawyers to do?

Rear Adm. Ruting—Yes.

Senator MARK BISHOP—Can you just advise the committee what are the changes of substance, the major changes, that have resulted in the amended contract?

Rear Adm. Ruting—The major issues being dealt with there were the reduction in the scope of the upgrade contract from six FFGs to four FFGs and the settlement of an excusable delay claim related to the conduct of the hull doubler plate work on HMAS *Sydney*. The hull doubler plates are plates that are on the outside of the FFG hulls to improve their strength. This work was not associated with the upgrade itself. It was other work that had to be done and, as a result of the extended period in dock to do that work, ADI was delayed on the upgrade work. As part of the settling of those two major issues, we have developed a new contract master schedule for all four ships. As I mentioned before, that involved the development of a new set of milestones, as well as new dates for those milestones, and included the conversion of some of the funds that were still due to be paid that would have been under the previous contract paid as earned value, moving those into milestone payments. So now a much higher proportion of the funds remaining will be paid against milestones rather than against earned value. I think they were all the major items that we incorporated in it.

We went into a lot of more detailed areas of clarification in this deed on the procedures to be used for test acceptance. We incorporated the concept of hand-back of the ship to allow Navy to have some operational use of the ship in the period prior to provisional acceptance. This was not a part of the previous contract, where the ship would have been effectively in ADI's control right up until they had completed all the documentation, software verification et cetera. This way Navy gets to use the ship and, as the Chief of Navy mentioned, in the case of HMAS *Sydney* he will get some four to five months of effective use of the ship prior to provisional acceptance. We also tidied up a number of other areas of the contract to make it more practical to execute.

Senator MARK BISHOP—Has the final contract price been altered in any way?

Rear Adm. Ruting—Yes, it has. In fact, we have reduced the final contract price as a result of settlement of all of those issues.

Senator MARK BISHOP—What is the reduction?

Rear Adm. Ruting—In base-date dollars for this contract—

Senator MARK BISHOP—In?

Rear Adm. Ruting—Base-date—1998—dollars, it is approximately \$40 million. In current currency of December 2006 price basis, that is approximately \$54 million.

Senator MARK BISHOP—So the contract price has gone from about 1440 to 1400?

Rear Adm. Ruting—No. The contract price was originally—

Mr Smith—\$1.009 billion.

Senator MARK BISHOP—From \$1.009 billion to—

Rear Adm. Ruting—To about 980—

Mr Smith—970 in base-date dollars.

Senator MARK BISHOP—In base dollars, the reduction was \$40 million,

Rear Adm. Ruting—Yes.

Senator MARK BISHOP—So \$1.009 billion, not—

Mr Smith—\$1.009 billion to \$969 million.

Senator MARK BISHOP—Okay. And in current dollars?

Rear Adm. Ruting—I am not sure that I have that immediately available. I will have to get the current date dollar value of that \$969 million.

Senator MARK BISHOP—Okay. It is not going to be much. We originally had six ships, in 1998 dollars, for \$1.09 billion and we now have four ships, in 1998 dollars, for \$969 million, with a net saving of \$40 million.

Rear Adm. Ruting—That is correct, but one needs to remember that we still get almost all of the equipment that would have been installed in ships 5 and 6 within that figure. There is something in the order of \$97 million, in base-date dollars, of equipment for ships 5 and 6 that we will still receive as part of the contract.

Senator HOGG—What will you do with that?

Rear Adm. Ruting—Most of it will be used as spares to support the other ships. As part of the difference between the project approval value and the contract value, we were originally going to have to buy quite a range of spares. We had not locked into exactly what all of those were when the original contract was signed, so quite a number of these items will be put to spares. We have already taken delivery of, for example, the vertical launcher that is not required now for the evolved Seasparrow missile. We are putting that into service in the ANZAC ship training centre over in WA on HMAS *Stirling*. That will be used for training the maintainers and operators for both FFG and ANZAC Class frigates.

Senator HOGG—Is there much of that \$97 million worth of equipment that will not be able to be used as spares that you will have to sell off, or is the vast majority able to be used for spares?

Rear Adm. Ruting—The vast majority will be able to be used for spares.

Senator MARK BISHOP—But the net of that is that we have 30 per cent, or two ships, less, for pretty much the same net outlay in 1998 dollars and 30 per cent less capability than if we had had the higher number of ships.

Rear Adm. Ruting—I would suggest that that is not a valid comparison to make, in that a very large component of the total cost of upgrading these sorts of ships is what we call ‘non-recurring expenditure’—all of the design and software development component. One might average the original price across six ships and come out at a particular figure by dividing the original contract by six and then, as you have done, divide the modified one by only four, and that suggests there is a 30 per cent reduction. In fact, a lot of that cost was, as I say, fixed costs regardless of the number of ships upgraded. If you had done only two ships, you would still have to pay a fair amount of that as a fixed cost. In fact, the cost for installation in ships 5 and 6 is the part that we have reduced the contract price by.

Senator MARK BISHOP—But we still have 30 per cent less capability because we have two less ships.

Rear Adm. Ruting—In an overall sense, yes; we have only four ships upgraded now.

Senator MARK BISHOP—And we have 30 per cent less capability.

Rear Adm. Ruting—Compared to where we started with the original contract, yes. However, it was a government decision—

Senator MARK BISHOP—I understand it was a government decision. I am just putting the dots on the i’s, which you have done. So that is fine.

Senator HOGG—Has the \$97 million appeared in the PBS at any stage as an expense or money expended?

Rear Adm. Ruting—That is correct.

Senator HOGG—And so it will now become an asset?

Rear Adm. Ruting—Yes. That will be rolled out as part of the assets under construction as those equipments are delivered. At the present moment, a large part of that is part of what has already been paid on the prime contract. As I have stated in a previous Senate estimates, some \$770 million—I think it is of that order—has already been invested in the Commonwealth, out of the \$950 million that I indicated we had already paid against the prime contract, using things like equipment.

Senator HOGG—How will that be shown in your balance sheet?

Rear Adm. Ruting—It will be rolled out as an asset.

Senator HOGG—And will you have some sort of notation there so that we are alerted to where it might be?

Rear Adm. Ruting—I would have to seek financial people’s advice on exactly how it would be entered.

Senator HOGG—It is just that sometimes these things get buried in the balance sheet.

Dr Williams—The normal arrangement would be that we would make a judgment on whether the amount spent was, essentially, increasing capability or whether it reflected money spent to overcome some deficiency in the previous work—something that was not effective. If it was the latter, we would need to write down the earlier amount, so the net may not be an increase in the asset value. However, if the money was a result of, perhaps, an underestimate initially and it was money that inevitably had to be spent then it would be reflected in the value of the asset as being a more valuable asset.

Senator HOGG—But in this case we have equipment that was going to be an essential element of, as I understand it, the frame of the ship; now it is going off to become spares.

Dr Williams—Again, providing it is still an item that has value long term, it would be reflected as an asset on the books.

Senator HOGG—Would you have bought the spares anyway?

Rear Adm. Ruting—Yes.

Senator HOGG—Was that allocation made anywhere in previous PBSs?

Rear Adm. Ruting—Yes. As part of the overall project expenditure that was planned for future years and identified in the PBS we would have identified that we had to spend money on spares. That would be part of future expenditures against this project out of the total project approval, which is why they would not be recorded as assets.

Senator MARK BISHOP—Would you, in any event, have purchased the spares that relate to the reduction in ships from six to four? If the answer to that is yes, where was it in the original contract?

Rear Adm. Ruting—We would not necessarily have purchased all the items but the vast majority of them, because in this upgrade, apart from some items like the vertical launcher and the diesel generator, many of the others were actually upgrades to existing equipment. The modification, for example, to take the Mark 92 radars and fire control systems up to the higher standard are in fact components, modules et cetera. So they are very usable directly as spares. So those will be able to be put into our stores system and held as spares which are able to be used to support the four ships to their end of life. In the original contract, we had a range of options. Because we could not identify exactly what the configuration of all the modules and equipments was going to be when the contract was signed—you do not know a lot of that until the design work is done and all the detailed equipment is selected—we had not included the purchase of those spares in the original contract in 1999. We were just getting to the stage of doing the logistic support analyses when the decision was made to reduce the number of ships from six to four. So, instead of spending additional funds and either buying those spares directly from some of the equipment providers or buying them through the prime contract, we will have them available through the prime contract.

Senator MARK BISHOP—That is okay. I do not have any further questions on this first issue, so I will turn to ordnance. Dr Gumley, the Auditor-General classified \$1.4 billion of ordnance in October 2005 as ‘other than serviceable’ and then went on to state that:

... one-third of the \$928 million in explosive ordnance that was classified as other than ‘serviceable’, could not be made serviceable.

What types of explosive ordnance have been deemed unusable?

Dr Gumley—I think it is better if I hand that over to the experts in bombs and bullets.

Ms McKinnie—The ANAO, in doing their audit report, in the way they presented that information made that somewhat misleading. As a result, the impression from that report is that the situation is much worse than it actually is. Probably the best way of going through the numbers is to talk about how we classify things as being other than serviceable and also give you the value of each of the three categories that fit into that. From there, you will get a better understanding of what the real understanding of the situation is.

Mr Smith—Let me just say that I do not think the ANAO was seeking to mislead; I think the point is that the way it presented could have had the effect of misleading people.

Senator MARK BISHOP—You mean the way the press reported it?

Mr Smith—Yes.

Senator MARK BISHOP—That is a matter for the press.

Mr Smith—I just would not want you to think that we are saying that the ANAO set out to mislead.

Senator MARK BISHOP—No, and I did not think was your position. My question, Ms McKinnie, was: what types of explosive ordnance have been deemed unusable?

Ms McKinnie—In the category of ‘other than serviceable’, there are three ways that we look at that. ‘Pending’ covers all of the EO and missile systems that are awaiting introduction into service. The type of thing that need to occur before it is introduced into service is that the integration into the platform systems has to be—

Senator MARK BISHOP—Ms McKinnie, I will have to interrupt you. We do not have time for a long defence or rejection of what ANAO did or did not say. I would ask you to answer my questions directly, because they derive directly from the findings of the ANAO report. If you think that the ANAO findings are suspect, capable of challenge or in error, I do not have any problem at all with you saying that, but I have very particular questions. I am asking exact questions, and I would ask you to answer the exact questions. My question is: what types of explosive ordnance have been deemed unusable?

Ms McKinnie—The category of what we call non-repairable includes a number of missile systems which have been withdrawn from service. They are things like Sparrow, Seasparrow and older SM1s. It also includes 105 millimetre artillery. They are some examples of what is included in the non-repairable category.

Senator MARK BISHOP—So Seasparrows, the SM1s—

Ms McKinnie—The older SM1s and Sparrows.

Senator MARK BISHOP—And the 105 millimetre artillery shells. Are there any others?

Cdre Law—They are the major components. There are a number of others that make up the remainder. I might just say that, of that total in ‘other than serviceable’, we are talking about a category of non-repairable of \$212 million—and I am talking October 2005 figures here, as quoted in the report—out of a total inventory of \$2.44 billion.

Senator MARK BISHOP—So a bit less than 10 per cent.

Cdre Law—Correct.

Senator MARK BISHOP—Do you have a program in place to review the remaining ordnance to determine its serviceability?

Cdre Law—Yes, we do. It is a dynamic process. The inventory management goes around and around. If I talk about some of the higher value items such as the missiles—

Senator MARK BISHOP—Yes.

Cdre Law—I will use the ESSM as an example. The ESSM has what is called a certification life of two years if it has been to sea in a frigate or, if it is sitting in a warehouse ashore in a climate controlled environment, of four years. So every four years or, at the worst case, every two years, the computer system that manages the inventory says, 'It's been out there for two years,' and it automatically goes from 'serviceable' to 'repairable'. That flags the inventory managers, who work for me, to then say, 'We have to put that missile over a test set and recertify it,' and then it goes back into the system as serviceable. Other items, such as small-arms ammunition, may have a nominal shelf life of, say, 10 years. The same system will say, after 10 years, that that will become basically repairable. The inventory managers look at it and say, 'Can we re-life that ammunition?' That is, can they give it an additional life? If the answer is yes, it goes back into 'serviceable'. If the answer is no, it goes into 'non-repairable' and will be disposed of.

Senator MARK BISHOP—You refer to that process as a dynamic review. Is that review part of standard operating procedure which has been in place for some time, or does it derive from the findings and recommendations of the ANAO?

Cdre Law—No, it has been in place ever since inventory came into being. It is just part of the through-life focus of my branch. Basically, we do the procurement and the through-life management through to disposal. That constant review and keeping the serviceability levels up is what it is all about. It is ongoing.

Senator MARK BISHOP—So there has not been any need on the part of Defence to change its review procedures or processes arising out of the ANAO report?

Cdre Law—Not in this area, no. We are looking at it. I would like to reduce the value of 'non-repairable' down, and I have a small team looking at the moment at how to do that. But again I have a finite work force. That finite work force does the higher priority tasks first. This is one of their day-to-day routine tasks that gets done. As I said, it is basically monitored by a computer system which flags when the ordnance itself goes in and out of serviceability.

Senator MARK BISHOP—You have identified \$212 million as non-repairable, and we have had that discussion. What were the other classifications apart from 'non-repairable'?

Cdre Law—I will be very brief. Pending is missiles and ordnance, which is being procured under the defence capability program yet has not been introduced into service. So it is not ready for use. That accounts in October 2005 for 25 per cent of the inventory. That is being worked on and brought into service.

Senator MARK BISHOP—The second classification?

Cdre Law—The second classification is repairable. As of October 2005 that represented 55 per cent of the inventory. That is components that are either in the supply chain being repaired or, in the case of small arms ammunition in particular, they have gone out of life. They then slip into repairable and may be re-lifed. It is that type of activity.

Senator MARK BISHOP—What is the final classification?

Cdre Law—That was it. So there is pending, repairable and nonrepairable.

Senator MARK BISHOP—And you say nonrepairable is \$212 million out of \$2.44 billion.

Cdre Law—Can I make a correction? I have just been reminded that repairable is actually 55 per cent of the other than serviceable, not of the total inventory. I misled you there. In fact the figure is \$575 million as at October 2005.

Senator MARK BISHOP—So it is 55 per cent of what?

Cdre Law—Of the other-than-serviceable category, which is made up of the pending, repairable and nonrepairable.

Senator MARK BISHOP—I am a bit confused here. We have three classifications: pending, repairable and nonrepairable. As percentage of total inventory, can you give me the figures of each?

Cdre Law—Of total inventory?

Senator MARK BISHOP—Yes.

Cdre Law—I do not have that figure breakdown in front of me. I can tell you that in October 2005, the other than serviceable, so the combined figure, was 43 per cent of inventory. Of that, a quarter of 43 per cent was pending, just over half of the 43 per cent was repairable and the remaining 20 per cent was nonrepairable.

Senator MARK BISHOP—This is getting a bit complicated. I thought we had three classifications of inventory: pending, repairable and nonrepairable.

Cdre Law—Yes.

Senator MARK BISHOP—The total value of inventory is something in the order of \$2.44 billion.

Mr Lewincamp—Senator, I might be able to help. The other category you are looking for is serviceable. You have had the three categories that are part of other than serviceable. Serviceable is the other 55 or so per cent.

Senator MARK BISHOP—Okay. So serviceable is 55 per cent of total inventory.

Mr Lewincamp—Something of that order.

Senator MARK BISHOP—Thank you. So the other three classifications account for 45 per cent.

Mr Lewincamp—According to Commodore Law it is 43 per cent.

Senator MARK BISHOP—Now we are cooking with gas. Of that 43 per cent, what are the figures for pending?

Cdre Law—About 11 per cent of the total inventory.

Mr Lewincamp—Of that 43 per cent is how you phrased the question.

Senator MARK BISHOP—We have four classifications of inventory: pending, repairable, nonrepairable and serviceable. We know serviceable is 55 per cent of total inventory. That leaves 45 per cent of total inventory to be allocated as a percentage. I want the percentage allocations of the other three groups of the 43 per cent as a percentage of total inventory so that we are talking in the same figures.

Mr Lewincamp—On a quick calculation, pending looks like it is around 11 or 12 per cent. Commodore Law said nonrepairable was somewhere around 10 per cent. On my calculation, that leaves about to 21 per cent for repairable.

Senator MARK BISHOP—So, of the order of 11 per cent pending, 21 per cent repairable, 10 per cent nonrepairable and 55 per cent serviceable—that is what we are talking about. In the context of that discussion, you assert that the dynamic review process that the department has had in operation for some years is adequate for ongoing assessment of the utility of ordnance.

Cdre Law—Yes.

Senator MARK BISHOP—And you are not caused in any way to have to change current practices or processes.

Cdre Law—No.

Senator MARK BISHOP—Apart from being satisfied with the utility of the existing system, did you do any examination that persuaded you that the existing system was satisfactory?

Cdre Law—We have looked at how our demand satisfaction rates are being met. That is, as the services demand ammunition, can we meet that demand? The answer to that is yes. At the moment we are fully supporting all the current operations and also all the service ‘raise, train, sustain’ activities that are conducted back home. As part of the ANAO audit—and we started this beforehand—we are looking with the services at how we can better define the upfront requirements for what we need to go and buy, and how we can program that into the procurement cycle better.

Senator MARK BISHOP—Is unusable explosive ordnance held at Orchard Hills in Penrith?

Cdre Law—Yes, there would be some there.

Senator MARK BISHOP—How much would be there?

Cdre Law—I do not have those figures. The actual storage and distribution of explosive ordnance does not belong to my branch in DMO; it is looked after by VCDF group, by Joint Logistics Command.

Senator MARK BISHOP—But there is some unusable explosive ordnance?

Cdre Law—Yes, there would be.

Senator MARK BISHOP—What do you intend to do that?

Cdre Law—With the small arms ammunition and the smaller calibre ammunition—in the past we have done a lot of this—we take it to Woomera and blow it up. That is becoming a little bit environmentally unfriendly these days, so—

Mr Smith—It was then, too.

Senator HOGG—I am glad to see you are environmentally friendly! We have not got any Greens here.

Cdre Law—These days we employ a company—an SME, or small to medium enterprise—that takes the ammunition, breaks it apart into its component pieces and puts those pieces back into circulation for other items such as scrap or whatever. It is a little bit more difficult with the missiles. At Orchard Hills at the moment we have some Sparrow and RIM-7P missiles. It is a little bit harder to break those down, but we are looking at how we might do that. In the case of the RIM-7P Seasparrow missiles, we may even be looking at transferring them to another user nation.

Senator MARK BISHOP—How many other sites are holding unusable explosive ordnance?

Cdre Law—I do not have exact figures, but I think the major sites of Orchard Hills and Myambat would be the main repositories.

Mr Smith—As you can see, Senator, there is some criticism about us holding a couple of hundred million—or whatever it is—of unrepairable stuff that people might think ought to be disposed of. But it is not that easy to dispose of; you do not just throw it out.

Senator MARK BISHOP—I accept that. If you did throw them out you would be the subject of criticism.

Mr Smith—Yes, all sorts of other problems.

Senator MARK BISHOP—Who does the inspection of ordnance within the DMO?

Cdre Law—It is done through Defence. The receipt inspections are done by ADI in most cases, as part of VCDF group through JLC. That is as stuff comes in to inventory, then when it is going through its through-life service ability regime, DSDO does some work for us, and my people do some work for us also.

Senator MARK BISHOP—How often do you carry out inspections at the major sites?

Cdre Law—We go through an audit process for the financial statements audits every year. ANAO audits the major sites on an annual basis.

Senator MARK BISHOP—What steps have been taken since the Auditor-General's report to ensure 'technical data necessary for the maintenance and storage of ordnance, both serviceable and other than serviceable,' is now attended to at each of these sites?

Cdre Law—We went back and had a look. One of the major issues we had was not having standard contracting templates across all activities that we controlled. As routine, we always seek technical information up front but, because we had different templates that might have been used in Washington or London or back in Australia, we carried out a review of those templates to ensure that the provisions for the required delivery of that information were

there. That is there and we have confirmed that. We have confirmed that the contracts require technical information to be delivered.

Senator MARK BISHOP—That is a template for the future, isn't it?

Cdre Law—No, we looked at past templates. We have now also standardised our templates.

Senator MARK BISHOP—Why was there a technical data deficiency?

Cdre Law—Even though you might have it as a contractual requirement as a deliverable, it may not always be available when you need it up front—and some examples of that are given in the report. Or, if you do receive it, it may not be adequate to do the thorough safety inspections and checks that you need to do to introduce that ordnance into the system. It is always there. We always seek it and if it is not available up front we go back and pursue it, but it depends on the operational urgency to get the ordnance into service. We do not cut corners; we still go through a very rigorous process. If we can get the information up front, that is great; if we cannot, then we will undertake some additional tests. We will take it down to the Land Engineering Agency and check it with the weapon. We will do checks at Graytown on the ordnance and that also gives you additional risk mitigation to introduce that ordnance into service. We always seek the technical information, but it is not always there when we need it up front.

Senator MARK BISHOP—Do we now have the required amount of technical data necessary for the maintenance and storage of that ordnance in those sites?

Cdre Law—Yes, we do. That is the first step in the introduction of the service process to make sure that you have got all the required information to allow you to both transport and store the item. Those are the key points we look at first. After that, you move to compatibility with the weapons platform and its overall safety for introduction into service.

Senator MARK BISHOP—I will turn to the role of the Guided Weapons and Explosives Ordnance Branch within DMO. The Auditor-General advised that following the 2003 Defence procurement review the GWEO was established in May of 2004. Can you provide a brief overview of the role of that branch in the purchase and maintenance of ordnance within Defence?

Cdre Law—My branch comprises about 400 people spread over Sydney and Canberra with elements in Perth. We are responsible for procuring all of the non-guided ammunition that comes into the ADF and a large majority of the guided weapons that come into the ADF ensuring that they are safely introduced into service. We are the inventory managers of all the items in the inventory. At the moment, there are about 3,000 items in the explosive ordnance inventory, and we are responsible from through-life, so through procurement to arranging for disposal of those items.

Senator MARK BISHOP—I gain the impression that your branch is now responsible for the purchase and maintenance through life of nearly all ordnance—is that correct?

Cdre Law—That is correct.

Senator MARK BISHOP—Is there any ordnance that you are not responsible for?

Cdre Law—Off the top of my head, no.

Senator MARK BISHOP—You have the lot.

Cdre Law—There are some major capital programs that my branch does not run, but those missiles or weapons are procured. For through-life activities they transfer to my branch. Once it is introduced into service, my branch is responsible for it, but I am not responsible for storage and transportation of the EO. That is an operational logistics activity that belongs to VCDF group.

Senator MARK BISHOP—Once it leaves your sites, it is the responsibility of those—

Cdre Law—In fact, the sites are run by ADI on behalf of VCDF group.

Senator MARK BISHOP—Since your branch was set up, have you established a series of protocols for the through-life support of future ordnance purchases?

Cdre Law—Those protocols already existed before the formation of my branch. If I go back a little in history, prior to 1998, the three services procured their own ordnance into the system. Back in 1998, the decision was taken to merge the three single service activities into a single activity and that was called the Joint Ammunition Logistics Organisation. That organisation established a common set of procedures and protocols that have been modified slightly through time, but they were already in place from about 1998 onwards.

Senator MARK BISHOP—Gotcher. I placed a question on notice in the Senate—question No. 171—in December 2004, in which I asked:

What steps have been taken by the ADF to reduce the theft or loss of weapons and/or ordnance ...

The response to that question was that the standard defence supply system would track movements of weapons by serial number and that all units were in the process of being connected to the system. Can you confirm that all ordnance sites are now connected to the SDSS?

Cdre Law—They are not connected to SDSS because we actually manage the explosive ordnance inventory and the general stores inventory separately. That is managed on SDSS. The explosive ordnance, because of its uniqueness, is managed on a separate system called COMSARM—the Computer System Armaments. My branch manages COMSARM. It knows the location, price and quantity of all the explosive ordnance within the Australian Defence Force.

Senator MARK BISHOP—All the explosive ordnance?

Cdre Law—Yes.

Senator MARK BISHOP—So you can identify and track all explosive ordnance?

Cdre Law—Yes.

Senator MARK BISHOP—But it is not part of the SDSS?

Cdre Law—It is a totally separate system. SDSS runs on the Defence restricted network. The COMSARM system runs on the Defence secret network. It is totally separate. You asked the question: ‘Are all sites on that system?’ The answer is: yes, bar two very small sites which are connected to the system via a side gateway called Telnet.

Senator MARK BISHOP—Can you confirm that a complete inventory of weapons and ordnance has been conducted?

Cdre Law—I can only answer on the ordnance. I cannot answer on weapons. They are managed by Defence. But certainly, as far as ordnance is concerned, every year the ANAO go through, validate the COMSARM system, do a series of stock checks on key sites and do ledger-to-floor and floor-to-ledger checks of all the ordnance. So every year we know where every bit of ordnance is and we know that none is missing.

Senator MARK BISHOP—Do they do a sample physical check to make sure it confirms the—

Cdre Law—Yes, they do.

Senator MARK BISHOP—Can we now turn to the prepayments issue that was also identified in the Auditor-General's report. The Auditor-General advised that prepayments totalling \$44.9 million out of a budget of \$50.1 million were made: in excess of 90 per cent. Which companies received these prepayments?

Cdre Law—It was Saab Bofors.

Senator MARK BISHOP—Just the one company?

Cdre Law—Yes.

Senator MARK BISHOP—What percentage of the contract did the prepayment represent at that time?

Cdre Law—It was 90 per cent.

Senator MARK BISHOP—So you made a prepayment to Saab of 90 per cent of the contract price?

Cdre Law—That is correct.

Senator MARK BISHOP—What types of ordnance were provided under this contract?

Cdre Law—There were two separate contracts but they both fall into the same basket. They are for a Bolide missile, which is a missile for the Army.

Senator MARK BISHOP—When did the delivery take place?

Cdre Law—The delivery from the first contract is taking place now, and I believe that the final deliveries of that first contract are due within the next month or so.

Senator MARK BISHOP—How many missiles?

Cdre Law—I will have to check.

Senator MARK BISHOP—We purchased a number of Bolide missiles from Saab and 90 per cent of the contract price was prepaid. That was almost \$45 million.

Cdre Law—Yes.

Senator MARK BISHOP—And, so far, only some of the missiles have been delivered pursuant to the first contract. Do you know a percentage?

Cdre Law—I am just checking to see how many have been delivered. I am sorry, I cannot find it. I will have to take it on notice.

Senator MARK BISHOP—What about the second contract?

Cdre Law—The missiles from the second contract have not yet been delivered.

Senator MARK BISHOP—Have we also made prepayments totalling 90 per cent?

Cdre Law—Yes, we have.

Senator MARK BISHOP—Off the top of your head do you know how many missiles were involved in the two contracts? Are we talking about 25 or 225?

Cdre Law—No. It is in the hundreds, but I cannot be specific.

Senator MARK BISHOP—So there are hundreds of missiles and only a small percentage has been delivered to date, notwithstanding the fact that 90 per cent of the contract price has been prepaid, pursuant to both contracts?

Cdre Law—Yes.

Senator MARK BISHOP—The Auditor-General has been critical about prepayments for a number of major capital projects in recent years. Why are we prepaying such a large number of contracts prior to actual delivery?

Ms McKinnie—The prepayments arose from the fact that that particular group was allocated a substantial amount of money fairly close to the end of the financial year and they sought to spend it before the end of the financial year.

Senator MARK BISHOP—It is a ‘spend in the financial year’ issue, is it?

Ms McKinnie—It was. It is not good practice.

Senator HOGG—I thought that practice was broken by Defence a number of years ago.

Ms McKinnie—Indeed. In the audit they found that, in the process of doing the prepayment, the business case that you would normally use to substantiate a prepayment was poorly documented. They also found that some of the parts to that business case did not eventuate. Although we did get some of the benefits from the prepayment, we did not get all of the benefits, including early delivery. What was recognised was that, in putting the case forward for the prepayment, we should have provided a more detailed risk assessment of the likelihood of being able to achieve all aspects of the business case. So we have now documented and made our processes quite clear: that the business case must be done within the GWEO Branch and not be split between GWEO Branch and London or the US, where the actual contracts might be negotiated.

Senator MARK BISHOP—Where was the fault in this instance—in the GWEO Branch or elsewhere?

Ms McKinnie—I think the fault pretty much lay with how we managed it between the GWEO Branch and London.

CHAIR—Was the business case a plausible case? The fact that we did not document it is a reason for the Auditor to go crook, but was there a decent business case for it?

Ms McKinnie—There was a reasonable business case and we achieved some elements of that business case, including additional missiles, but we did not achieve the whole business case. So it could be argued that the delegate, when signing off on the prepayment, should have been more acutely aware that some elements were at very high risk of not being achieved and, therefore, the business case was not as strong as it could have been.

Senator MARK BISHOP—In fact, the business case, with the wisdom of hindsight, was an extraordinarily poor business case on the basis that, even at today's date, the bulk of the missiles have not been delivered, notwithstanding the fact that Saab have 90 per cent of the cash up-front. Is that a fair comment?

Ms McKinnie—With 20/20 hindsight, you may very well say that.

Senator MARK BISHOP—Maybe it is 20/20 hindsight, but I recall that discussions of this exact nature have been held at this committee for at least the last five or six years and we were repeatedly assured that instances of abuse of prepayments was a feature of the past and was not going to be an occurrence in the future. I am being somewhat half-smart with hindsight wisdom, but it is on the basis of undertakings made here.

Ms McKinnie—We have strengthened the processes quite clearly for the GWEO Branch and, as a result of that, we have not spent as much money as was originally allocated to us for EO. That is because of a strict adherence to the processes that we have now put in place, with absolutely clear guidance for our people on how to do it.

Senator MARK BISHOP—In future. All right. The Auditor-General goes on to say that, under the SAMS agreement, in several instances 100 per cent prepayments were made. Can you confirm that prepayments of that magnitude under the SAMS agreement were received by ADI?

Cdre Law—They were.

Senator MARK BISHOP—Can you advise who authorised the prepayments?

Cdre Law—I will not name names, but the director of the particular business unit authorised those.

Senator MARK BISHOP—What is the particular business unit?

Cdre Law—It is the non-guided SPO, systems program office.

Senator MARK BISHOP—What was the basis of his authorisation?

Cdre Law—He had the appropriate delegations within the delegations framework at the time.

Senator MARK BISHOP—He had the right to make it?

Cdre Law—Yes.

Senator MARK BISHOP—He was the delegate; he had the right to make the call. Having the right, what persuaded him that it was an entirely proper thing to authorise?

Cdre Law—I believe those payments took place before I joined or took over the leadership of the branch, and I have not spoken to him about that. We would probably have to ask him if

that were the case. He made the right decision he thought at the time, given the information he had.

Senator MARK BISHOP—Is he here now?

Cdre Law—No, he is not.

Senator MARK BISHOP—Can you assist us, Dr Gumley?

Dr Gumley—No, I am not aware of it, either.

Senator MARK BISHOP—What benefit then, Commodore, was—

CHAIR—What was the business case?

Senator MARK BISHOP—They do not know what the business case is.

Cdre Law—If I can give a little bit of background—

Senator MARK BISHOP—Do you know what the business case was that supported it?

Cdre Law—If I could supply a little background, the global explosive ordnance unit manufacturing business expects a minimum of 30 per cent prepayments. That is to cover tooling up, materials et cetera. In this unique case, to my mind, there is no rational explanation as to why you would make 100 per cent payment of this kind. In fact, as Ms McKinnie has said, we have now tightened up the processes. I am now reviewing all the cases that go out of my branch, and 95 per cent of those say there are no prepayments at all. If there is going to be any requirement for a prepayment, that is fully justified with a business case. That business case is fully documented and it is signed off by an appropriate delegate, with the appropriate commercial—

Senator MARK BISHOP—I understand. In the SAMS case, was there any benefit derived from the prepayments at all?

Cdre Law—Not to my knowledge.

Senator MARK BISHOP—Have we got all the SAMS missiles?

Cdre Law—SAMS is a contract, not a missile.

CHAIR—Yes, it is a contract.

Cdre Law—SAMS is a 20-year contract we have with ADI for production of ordnance in Australia.

Senator MARK BISHOP—You are right. When was the Mulwala facility constructed?

Cdre Law—Mulwala dates back to the 1940s.

Senator MARK BISHOP—When was construction of the Benalla facility completed?

Cdre Law—I am not exactly sure, but it was in the late nineties.

Senator MARK BISHOP—That was constructed with Commonwealth moneys. What did that cost us?

Cdre Law—I am not sure. It was not done with Commonwealth moneys; it was actually paid for by ADI, as a very early form of PFI.

Senator MARK BISHOP—PFI?

Cdre Law—A private financing initiative.

Senator MARK BISHOP—Correct me if I am wrong, but my memory of the private financing is that the Commonwealth supplied the funds to ADI to build the site there. Is that correct?

Cdre Law—No. ADI funded up front, and we pay an annual capability payment to ADI. They are recovering the money that they paid to build the facility.

Senator MARK BISHOP—The cost of capital?

Ms McKinnie—That charge is part of the SAMS contract.

Senator MARK BISHOP—I am going to come to that. Why wasn't the Mulwala facility included in the sale of ADI?

Cdre Law—It is my understanding—and this is past history, which I am not fully across—because of the nature of the propellant high explosive chemical residues in the site that ADI were not prepared to take ownership of that site. The soil is spoiled.

Senator MARK BISHOP—The soil is spoiled; is that what you are telling me?

Cdre Law—That is my understanding.

Senator MARK BISHOP—As Senator Hogg says, there are huge remediation costs?

Cdre Law—Again, it is not part of my direct remit, and maybe CC can answer some of it, but I understand that \$63 million has been set aside for some remediation of that site.

Senator MARK BISHOP—When the government sold its shareholding in ADI Ltd in 1999, why did the contract provide for Defence to make a \$50 million annual payment to ADI for the Benalla facility?

Ms McKinnie—I was not involved in the sale, but as I understand it the arrangement was a part of the proposal whereby ADI developed the Benalla site and from there co-located production of a number of EO elements to that site. Rather than Defence paying up front for a manufacturing capability as a capital investment, it was taken over the period of the SAMS contract pretty much as a PFI type of arrangement.

Senator MARK BISHOP—Can you confirm that this \$50 million per annum is paid to ADI regardless of whether any ordnance purchases are made?

Ms McKinnie—That is correct.

Senator MARK BISHOP—Can you also advise why a condition of the sale included the provision for the return of the facility to Defence at the end of the SAMS agreement in 2015 for \$1?

Ms McKinnie—I think that is fairly standard for these sorts of long-term private financing arrangements.

Senator MARK BISHOP—Is this private financing initiative, PFI, the same sort of thing as private-public partnerships, PPPs?

Ms McKinnie—I am not an expert but I think it is similar.

Senator MARK BISHOP—Did somebody say it was exactly the same thing; who said that?

Senator HOGG—I think someone at the table should answer. For the purpose of the *Hansard* I think someone at the table should answer, other than the angels.

Air Cdre Plenty—They are akin in the same terminology.

Senator MARK BISHOP—So, in this case, ADI provide the capital and they get a payment on an annual basis of \$50 million to repay the capital they outlaid up front?

Air Cdre Plenty—I am not sure of the financial arrangements for that project.

Dr Gumley—I think the contract has two main components: one is a capital repayment, the industry payment component, and the other is, if you like, a standing army charge for the people and the basic facility. So the contract is structured such that, if we want ordnance out of it, we pay for the materials. I am sorry; I made a mistake on that contract. Ms McKinnie tells me that that \$50 million is all financial charge.

Ms McKinnie—That is around \$50 million per annum, and on top of that we pay the cost of the production of ammunition.

Senator MARK BISHOP—Right. So, from 1999 to 2015, we are paying \$50 million per annum for 16 years, which is something in the order of \$800 million, for the construction of that plant. In addition to that, we pay actual costs of production of ordnance at the site. Is that right?

Cdre Law—That is correct. But it is pure cost.

Senator HOGG—What do you mean by ‘pure cost’ of production?

Cdre Law—The cost that we pay for production is just the direct labour and the material costs. So what ADI is charged is what we pay, but the profit is in fact a component of the capability payment.

Senator MARK BISHOP—So over a 16-year period ADI are going to get \$800 million which they expended in about two years to build that plant? Is that right? Why was that done? What is the real deal here? Why was that done?

Mr Smith—This is the 1999 deal?

Senator MARK BISHOP—Yes. Why would we want to pay \$800 million over 16 years for an ordnance factory? What is the real deal here? Is that a backward way of slipping money into ADI for some other reason?

Mr Smith—You would need to go into the business case in some detail to work out whether that is a better way to do it than charging a profit on ammunition.

CHAIR—Secretary, why don’t we take this question on notice? Maybe in future days you could provide us with a brief historical background of what the business case was back then.

Mr Smith—We will probably have to go to Department of Finance and Administration to get at that.

CHAIR—I think this is a plausible and explainable situation. The numbers are big and it is not apparent to the committee exactly what the motivation was. I have no doubt that the motivation was a sound one.

Mr Smith—We will take it on notice.

Senator MARK BISHOP—That is fine. We know that we are paying \$50 million annual payment to ADI over 16 years for that site, and we know that we have to pay pure production costs for ordnance purchased, but DMO also pays an annual figure of \$25.8 million to ADI to keep the capability available to ADF, and a further \$5 million annually for repairs and maintenance. So we are paying \$30.8 million every year as well to keep the capacity available and for repairs and maintenance. Is that correct? Are they additional figures to that \$50 million we are talking about?

Cdre Law—They are good figures. The only clarification I would make is that, of the \$50 million for the capability payment we pay to ADI, about \$22 million of that every year flows through to the bond holders, so it does not stay with ADI. I just want to make that clarification.

Senator MARK BISHOP—Right.

CHAIR—The obvious reason for this is that this capability must be stand-alone and it must be ours. We cannot rely on some third party to provide this. We have got to have this ordnance. Am I right?

Mr Smith—That is the basis of it, as I understand it, yes.

CHAIR—This is very expensive business.

Mr Smith—And you pay a price for keeping it in Australia.

Dr Gumley—You also pay a price for the skills and technology, to keep them going and retrained.

Senator MARK BISHOP—I understand that is a strategic decision to have the two sites operational, capable and supplying ordnance. I do not argue with that. I suppose that is a debate the government held at the time: whether to have it done by ADI or to do it yourself.

CHAIR—I think that is the debate. Let us get the business case as best as we can, analyse it, and then come back next time and ask them more questions.

Senator MARK BISHOP—Is the Mulwala facility a defence property?

Cdre Law—Yes, it is.

Ms McKinnie—Yes.

Senator MARK BISHOP—What is the lease with ADI for that facility? What is the period of the lease?

Cdre Law—The period of the lease is similar to the Benalla arrangement.

Senator MARK BISHOP—So does it expire about 2016?

Cdre Law—Around 2015.

Senator MARK BISHOP—And then reverts to the Commonwealth?

Cdre Law—It is a Commonwealth property.

Senator MARK BISHOP—Does Defence receive any rent from ADI for the use of the facility?

Cdre Law—Not to my knowledge.

Dr Gumley—But if we did it would become a circular argument—they would just put the price of the propellant up again.

Ms McKinnie—We do receive part of the profits associated with the commercial sales that ADI makes, for explosives and the like.

CHAIR—Tell us about that. That is interesting.

Ms McKinnie—I think we share about 50 per cent. We share the profit they make on commercial sales 50-50.

CHAIR—Would the commercial sales be to the mining industry, for instance?

Cdre Law—Yes, and to small-arms ammunition in the US.

Ms McKinnie—And the medical industry.

CHAIR—Right. Very interesting.

Senator MARK BISHOP—In terms of that Mulwala site, can you advise on the details of the recent budget announcement for the \$300 million upgrade to the facility?

Dr Gumley—Yes, we can.

Senator MARK BISHOP—The press release put out on 11 May.

Dr Gumley—Yes.

Mr Veitch—As part of the budget, the government provided a further \$131 million towards the upgrade of the facility. All up, the project for the upgrade of the facility will cost in the order of \$300 million, with Defence making a contribution of about \$170 million.

Senator MARK BISHOP—So Defence provides \$170 million and the Commonwealth provides \$131 million.

Senator HOGG—Where will Defence get the \$170 million from?

Mr Veitch—We have been programming money for that over the last couple of years.

Senator HOGG—You have a sinking fund, in other words?

Mr Smith—No. We had programming money to pay a lease over a number of years. Instead of using it for that, we will now use it for the capital.

Senator HOGG—So this has been diverted from another project?

Mr Smith—No, this project. It is a reconfiguration.

Senator HOGG—So you are putting money in the tin to pay a lease on this?

Mr Veitch—We were making some provision for it as early as a couple of years ago, but we had not made a full provision for it. As part of this budget, we took a proposal to government and said, 'We can fund a certain proportion of it and we ask government to

consider a proposal to top that money up for the new project,' and that proposal was agreed to as part of the budget.

Senator HOGG—Prior to the announcement of the \$131 million, therefore, of the \$170 million how much do you have in the kitty and where will you find the balance from within your resources?

Mr Veitch—As part of each annual budget cycle we look at our priorities for the years ahead, and we have taken opportunities to move funds over those years to set aside whatever we could towards this requirement. Ideally, we would have liked to have been able to afford the whole \$300-odd million but, as it turned out, because of other priorities, we could only afford to kick in part of the total cost and that is why we took the proposal to government.

Senator HOGG—But you would not have had the whole \$170 million stashed away. How much of it did you have put away?

Mr Veitch—We had \$170 million or thereabouts. I do not want to go into the exact figure because of the commercial-in-confidence nature of the figure. I am just talking generalities.

Senator HOGG—I am quite prepared to talk in round figures. I am just trying to get a picture as to how you got the financing together. It means that you must have had an appropriation for this over two or three previous budgets?

Mr Veitch—We have been progressively looking at opportunities to put money aside for this project. We have done that over the last couple of cycles of our annual budget.

Senator HOGG—So for at least the last two budgets. And has that been an additional appropriation that you got on each of those occasions from the Commonwealth or have you made it out of savings? How have you done it?

Mr Veitch—First of all, we only get the appropriations in the year of the current budget. We have programmed for it in our forward estimates, as part of our annual update. What we have done is that we have progressively looked at opportunities as they have arisen to reprioritise the budget to find as much as we can towards the project.

Senator MARK BISHOP—So over the next couple of years we are going to be spending \$300 million to upgrade the facility up there. In due course, the facility will become more modern and presumably more valuable. Is there any consequent increase in the payments that have to be made to ADI to keep the capability available or for ongoing repairs and maintenance?

Mr Veitch—We are expecting—and, again, I am talking only in round figures—that the price of the product we buy from ADI could increase by about \$5 million or \$10 million a year after the upgraded facility comes online.

Senator MARK BISHOP—Is that because of higher quality product or extra product?

Mr Veitch—It would be a combination of both.

Senator MARK BISHOP—DMO pays an annual figure of \$25.8 million to ADI to keep the capability available. With the revamped site, is that figure of \$25.8 million going to increase at all or is that a fixed price?

Mr Veitch—I am sorry, but I do not have the figure. Shireane may be able to help.

Ms McKinnie—We do not know yet. We will have to renegotiate the Mulwala agreement, which would include any sort of annual payments that we would make.

Senator MARK BISHOP—So that figure is up for renegotiation?

Ms McKinnie—Yes.

Senator HOGG—Where will most of that \$300 million be spent? Will it be spent on infrastructure or software?

Ms McKinnie—The majority of it will be spent in terms of construction and also building the chemical plant.

Senator HOGG—Will any existing facilities close down as a result?

Ms McKinnie—We will close down the existing propellant plant and we will put the new propellant plant on a greenfields site within the Mulwala facility.

Senator HOGG—So part of the existing site will be closed and another part will be opened?

Ms McKinnie—Indeed.

Senator HOGG—And the time for this construction?

Ms McKinnie—We are negotiating a contract at the moment with Bovis Lend Lease. We are planning to go to government in about August this year for final project approval. We then have the Public Works Committee activity. With all of that occurring, we expect that the plant should be handed over for acceptance in about 2010.

Senator HOGG—By how long will that extend the life of the plant?

Ms McKinnie—It will be a new propellant plant.

Senator MARK BISHOP—I will now turn to AIR 87 and the Tiger project for some questions.

Senator Sandy Macdonald—Chair, with the indulgence of the committee, General Leahy has some opening comments to make on AIR 87 and the armed reconnaissance helicopter.

CHAIR—Please proceed, General.

Lt Gen. Leahy—Thank you, Chair. There was considerable comment in the media on the ARH Tiger following the tabling of the ANAO report on 2 May. It is the view of Defence that both the aircraft and the status of the project are far better than was described and it is our intention to provide you with some information to back this judgment. The ARH Tiger is a complex and highly sophisticated weapons system. It will provide Army with a military capability advance akin to that of the leap from the biplane to the jet fighter, and it is critical to the hardened and networked Army of the future. It is an extremely manoeuvrable helicopter that will contribute significantly to operations in the joint battle space. We see no reason to doubt that it will achieve full capability in a graduated and controlled manner.

Six ARH Tiger aircraft have been accepted. They have accrued 875 hours, of which 315 hours have been flown in Australia, since acceptance of the first two aircraft on 15 December 2004. We are very prepared to admit that the aircraft is not yet at the standard required in the contract. It was a conscious decision to accept the aircraft with known and quantified

shortfalls against the mature requirement, so that Australian based training could commence and Australian-specific flight testing could be conducted. It has also enabled the fitting and development of secure communications for the aircraft. The deficiencies are being closely managed under the ADF operational and technical airworthiness framework, and the contractor commenced the retrofit program at their expense on 17 May 2006.

I was recently at Australian Aerospace's facility in Brisbane. I discussed with them the fact that aircraft No. 1 was coming back the next week for many of those retrofits and improvements. I also observed the 20th aircraft on which assembly had commenced in their factory; there are 22 aircraft in total. Within a short period of time, the plant was constructed, an Australian workforce trained and aircraft assembly undertaken. It is a very impressive sight. Once in service, the 1st Aviation Regiment will operate Tiger. It is now based with our mechanised brigade in Darwin, and there has been a lot of work to prepare their facilities; they are ready now to accept the Tiger.

Once the crews complete their individual training by day, night and on the weapons, which we term the 'initial operational capability', Army will then conduct the collective and combined arms training and operational tests and evaluation for about eight months; that will mature the war-fighting skills of the 1st squadron so it is ready for operational deployment. Primarily due to delays in the Franco-German program on which the Australian program relies for aircraft certification, I understand that the current contractor training plan is about six months late and may be considerably more late—in the order of 18 to 24 months. But my staff are confident that DMO and the contractor will deliver the capability we are seeking and require for the complex war-fighting environment.

One example of why we have this confidence is the integration of the US Hellfire missile onto the aircraft. Whilst I understand that some work is still required for full certification, the seven missiles fired, including one at night, all struck the target at up to eight kilometres with lethal precision. That gives a different view to that given in the ANAO report, which suggests that the weapons do not work on the aircraft. I have some photographs with me, which I think are quite impressive, showing the Hellfire being fired out at the Woomera test range. If you would like, I can table those photographs.

CHAIR—We would be very pleased if you would.

Lt Gen. Leahy—The first photograph shows the Tiger aircraft firing the Hellfire missile. This is the first time that that missile has been integrated on an aircraft of this type, which is a very significant achievement for the world, for DMO and for the staff on this. They should be congratulated on this integration.

CHAIR—Is it a laser guided missile?

Brig. Patch—Semi-active laser.

Lt Gen. Leahy—In the next photograph, you will see the target of steel plates in front of containers. The third photograph shows, at six kilometres, a very impressive hit. The next photograph shows a larger target at eight kilometres; again, you can see a very impressive hit. Those pictures indicate to me that that weapon works pretty well. I would not like to be at the wrong end of it. I am confident that the issues facing the Tiger today are resolvable, that the project will address them and that we, in due course, will get a great helicopter.

Senator HOGG—You said that at this stage six have been accepted, and you mentioned 875 flying hours. Is that in total for the six aircraft?

Brig. Patch—Yes; all six aircraft have commenced flying. We accepted the sixth aircraft only a couple of weeks ago, but all six have contributed to those hours.

Senator HOGG—I think I heard that 315 of the 875 hours have been in Australia. Does that mean the rest were on aircraft that you have accepted that were constructed overseas?

Brig. Fraser—That is correct. The first four aircraft were assembled in France. They conducted considerable tests and development of the aircraft in France and some training. Then the aircraft were brought to Australia for the in-service date of 15 December 2004.

Brig. Patch—The first two aircraft were brought and the second two—3 and 4—were left in France to complete some residual testing. And as a result of delays in the Franco-German program we opted to leave those two aircraft there to provide an opportunity to conduct some early training of Australian aircrew and Australian flying instructors in France before the aircraft were brought home some four months late.

Senator HOGG—Regarding those six that have been accepted, is that a full acceptance or is that a provisional acceptance?

Brig. Patch—The contract is very clear on this. Even the ANAO report makes it clear in one of its footnotes, footnote 95, that it was never the DMO's intent to accept a fully complete aircraft at in-service date; the intention was to accept an interim aircraft at a configuration that was agreed by the DMO—in fact, by me as the project authority. That was what was delivered. The analogy we could use here is that of you purchasing a house. The builder says to you, 'I now have a certificate of occupation,' and you say to the builder: 'But the house is only partially complete. I won't move in,' which is an option you have. Or you can say to the builder: 'I will withhold a significant amount of the funds associated with the purchase of the house and I will move in to take advantage of what I have. I will get to use the house, I will get to work with you as we develop the house to its full capability.' That is what we have done.

Senator HOGG—Regarding the retrofit that I heard is going to start next week—or it might be this week—on aircraft No. 1—

Brig. Patch—It has already commenced, on 17 May.

Senator HOGG—So it has already commenced on aircraft No.1. Is there any additional costs associated with that retrofit and is that predominantly an upgrade of software or is it something more complex than that?

Brig. Patch—The retrofit of ARH1 has in fact three components. The ANAO comments on the fact that the retrofit will take nine months. That is not correct. It has three components to it. ARH1 was the first aircraft to fly. It is the first aircraft to reach a point in its life where it must undertake its first major servicing. That major servicing was conducted by Australian Aerospace technicians, who currently support the aircraft in Oakey in Queensland. The week before last it was flown to Brisbane, where it commences the second part of that, which is the retrofit of the aircraft.

Senator HOGG—As I asked, what is the retrofit designed to mainly do—upgrade software, or is it something to do with structural enhancements?

Brig. Patch—It is a combination of the two. The aircraft will be fitted with a full production sight, the software will be upgraded and there are other modifications that will be made to the aircraft.

Senator HOGG—Are there any additional costs associated with that?

Brig. Patch—No cost whatsoever to the Commonwealth. This was all agreed.

Senator HOGG—Is there any additional training for the crew?

Brig. Patch—No additional training is required. The final, third part of that retrofit is that ARH1 will become a fully instrumented aircraft. As the first aircraft it already had an instrumentation package built into the aircraft during its production. That instrumentation package will now be enhanced so that the aircraft can be used as a fully instrumented flying aircraft to undertake specific test and evaluation in absolute detail. It will be able to download that information to a ground station for the life of type of the ARH. This is a unique capability which we have built in to ensure that, through the life of this aircraft, we are always one step ahead in terms of its development.

Senator HOGG—How long will the retrofit take?

Brig. Patch—The retrofit element?

Senator HOGG—Yes.

Brig. Patch—It commenced last week and will be completed by—

Brig. Fraser—The retrofit program as started on ARH1 will be complete in November. That is when the instrumentation fit will also be initiated.

Senator HOGG—So that is roughly six months per aircraft.

Brig. Fraser—For the first aircraft it is, but the first aircraft and the second aircraft require more modification. Only those two will need to go into the factory facility. The remainder of the retrofits can be done during normal maintenance on those four aircraft.

Senator HOGG—Okay. So that will be some time down the track. When the retrofit is done, will there be a final acceptance on the part of Defence of the aircraft as they come off the retrofit line?

Brig. Fraser—Yes, there will. We still have commercial leverage to ensure they are completed, with a separate milestone for a final certification as well as a milestone at the end of the program with a significant payment.

Senator HOGG—Are there payments associated with those milestones?

Brig. Fraser—Yes.

Senator HOGG—What percentage of the contract?

Brig. Patch—In pure dollar terms, the final acceptance of all supplies is worth \$65 million, which is approximately five per cent of the value of the contract. The milestone which is yet

to be achieved in terms of final Australian military type certification is worth about \$5.7 million.

Proceedings suspended from 9.01 pm to 9.14 pm

Senator HOGG—With the retrofit and everything else, when will all of these aircraft be fully accepted into service?

Brig. Patch—The last aircraft, under our current plan, is due for acceptance in April 2008. We are currently slightly behind schedule for reasons which are internal to Defence in terms of our acceptance of the aircraft from the production line. So I expect that the last aircraft may be delayed slightly, but our intention at this stage is to drive forward for an April 2008 last delivery.

Senator HOGG—By then will they all be situated in Darwin, or will that occur some time—

Brig. Patch—The operational squadrons and regiment will be situated at a brand new greenfield site in Darwin, as the Chief of Army has already said. There will be a training capability at Oakey and an attrition fleet which will be divided between the two locations.

Senator MARK BISHOP—Thank you for that explanation, General Leahy. I just advise you that I had not intended to enter into any discussion with you as to the merits or utility of the particular platform. That is something that is certainly beyond my capability. The decision has been made and it is being implemented. You clearly have a different perspective to ANAO; so be it. It is not for me—

Lt Gen. Leahy—We are very proud of this platform, Senator. It is going to be a great capability for Australia.

Senator MARK BISHOP—That is right; that is what you wanted in the first place. But what I do want to talk about is the background, in particular the tendering process for the Tigers, going back some time ago. Can you advise me why it was fast-tracked from six months to six weeks?

Lt Gen. Leahy—I will ask Brigadier Patch, who is aware of the details of that.

Brig. Patch—AIR 87 was chosen as one of the vanguard projects for the Defence Materiel Organisation reform agenda. When the new undersecretary was appointed with a clear mandate for reform, he went looking for projects and we stuck our hand up. The end result was that we took a process of RFT release to contract signature from an average of about two years to 12 months. In that process we were required to come up with innovative ways of undertaking our analysis in order to compress the time frames. Rather than do it in series, we developed a process whereby we did it in parallel. In fact, there were six integrated product teams working simultaneously on different parts of the contract and the evaluation so that we could compress what would normally have been done in series into effectively a single time frame. That enabled us to do the work, which would normally have been done in some months, in a matter of weeks.

Senator MARK BISHOP—So the priority at that time was one of urgency, and that caused the entire planning process up to the tender stage to be compressed down to six weeks?

Brig. Patch—There were some other issues. We were literally five days away from releasing our tender when the government announced that a 2000 white paper would be released. So, when the 2000 white paper was released, all of the potential tenderers had their teams ready. That delayed the project release of the RFT by six months. In the end we did not release it until 18 December 2000—we were the first RFT released immediately after the white paper. And then, when the white paper was released, it brought forward our in-service date from 2005 to 2004. So the DMO was forced as part of its reform agenda to address that compression and we did that in the best way we knew how.

Senator MARK BISHOP—That is the first time I have heard that said. Why were you forced to compress the time line for what was such a major project, and had such significant developmental aspects, so that in the end the tender process was cut down from the norm of six months or more to just six weeks? What drove that urgency?

Brig. Patch—The evaluation process was cut to six weeks, not the tender process. The tender was released on 18 December 2000, and the contract was signed on 21 December 2001.

Senator MARK BISHOP—The ANAO report states:

The evaluation was initially planned to last for a period of six months (see Table 1.2), however, Defence compressed the review of tenders timetable to six weeks.

Brig. Patch—True, but we still had six months. The tenders closed on 30 April 2001 and we still had from that point to the end of the year to evaluate the tenders and then, having evaluated the tenders, to shortlist, if necessary—although the tender evaluation plan allowed us to shortlist to as few as one, which ended up being the result—and then to work with that company to develop their offer in such a way that we could sign a contract within 12 months.

Senator MARK BISHOP—How long in fact did the tender evaluation process take?

Brig. Patch—As I said, we released the tender on 18 December 2000 for three months and tenders closed 30 March 2001. We had from 30 March until 21 December in order to conduct a complete evaluation of all the tenders offered—there were four tenders—and then to shortlist those tenders through a series of processes and then to develop Australian Aerospace's offer, then Eurocopter International Pacific, such that we could sign a contract before the end of the year, within a 12-month period.

Senator MARK BISHOP—Was the tender evaluation process nine months—that is, March through to December?

Brig. Patch—The actual evaluation process was the six weeks the ANAO was talking about. Rather than distribute the tender document out across Defence, as was the normal fashion, we brought 80 personnel into our office in Canberra and, in a unique process in this team environment, we evaluated in six weeks what would have normally taken six months. The actual schedule is laid out in table 1.2 of the ANAO report.

Senator MARK BISHOP—Are you satisfied with the way that process was conducted in terms of the outcome to date?

Brig. Patch—As the author of the process, maybe you are talking to the wrong person, but I am completely satisfied with the outcome to date.

CHAIR—You carry the responsibility for the end product.

Brig. Patch—I certainly do.

CHAIR—So the question is a legitimate question. Are you satisfied with the process to this point?

Brig. Patch—I am perfectly satisfied with the process to this point.

Senator MARK BISHOP—I am confused on this: you said you had the ability from March through until December to do the tender evaluation, but then you said that you brought in a team of 80 personnel and you confirmed that the tender evaluation was done in a six-week period. Were nine months or six weeks involved in that tender evaluation process?

Brig. Patch—On 30 March we received four tenders. Within six weeks, we had evaluated those tenders and achieved a result of which we could advise government. We had two tenders at that point: one which was the preferred tenderer and one which was stood aside. We had the opportunity to take both of those, if necessary, but, in the end, we only took one through a full developmental process, which is now reflected in the standard processes that are used in capability development within the DMO.

Senator MARK BISHOP—At the end of May, you had reduced the four tenders to two, you had a preferred tenderer and you had a recommendation that was ready for sign off by government.

Brig. Patch—Yes.

Senator MARK BISHOP—So that is the six weeks that the ANAO is talking about.

Brig. Patch—Yes.

Senator MARK BISHOP—Since that time, are you telling me that that much truncated system has now become the norm within DMO for projects of this nature?

Brig. Patch—Six weeks is not necessarily the norm, but the process is now accepted. The process is longer. We were very fortunate in that we had more time allocated, but, because we were able to immediately reject one of the tenders because it was incomplete and soon thereafter reject a second tender because it was way overpriced, we were then able to go forward with the last two tenders. So we were very fortunate. We had planned to do it in a longer period of time, but circumstances enabled us to do it more quickly than we had anticipated.

Senator MARK BISHOP—Did you follow a tender evaluation plan for the Tigers?

Brig. Patch—Yes, absolutely. If there is one thing that the six-month delay due to the white paper gave us the opportunity to do it was to make sure that our planning, our contingency planning and our documentation were absolutely rock solid.

Senator MARK BISHOP—Did you detail to the unsuccessful tenderers at that time why they were unsuccessful in their bid?

Brig. Patch—We did.

Senator MARK BISHOP—More than just a one-page letter?

Brig. Patch—Far more than a one-page letter. We gave them each the opportunity to speak with us for as long as they wished to speak with us. We did a face-to-face debrief.

Senator MARK BISHOP—What were the reasons for choosing to award the tender to then Eurocopter International Pacific, now known as Australian Aerospace? I am hearing you say that there was a new Defence Capability Plan, that the government wanted and directed urgent decisions, that you as the responsible project officer within DMO volunteered for the Tigers project, that you had a different system of tender evaluation which brought a whole range of units together, that you compressed the time down from six months to six weeks and that you advised the unsuccessful tenderers forthwith, in detail, as to why they were unsuccessful. That is the story so far.

Brig. Patch—Yes.

Senator MARK BISHOP—I know government chose Aerospace, but what made them stand out in your mind so that you recommended their product to the National Security Committee?

Brig. Patch—Probably for some time before AIR 87, the acquisition side of contracts was given far more weighting than the through-life support elements of contracts. It tended to be the focus of tender evaluation.

Senator MARK BISHOP—Get the new product?

Brig. Patch—True. In AIR 87, we made sure that the through-life support aspects were given equal weight to the acquisition. We are not just buying an aeroplane; we are buying an entire system to deliver a materiel capability to Army so that they can turn it into an operational capability, and we are buying all the elements—training, ammunition, aircraft, test facilities, facilities themselves and so on—so we made a deliberate decision to evaluate through-life support and acquisition equally. When we put the tenders together, as the ANAO reports, the Tiger was not necessarily the most capable aircraft. It was, however, the only reconnaissance aircraft offered. All the others were attack aircraft, putting forward a proposal that if you bought an aircraft that was an attack aircraft it was possible to do reconnaissance with it because it had all the capability. The Tiger was the only truly reconnaissance aircraft, and it was a generation ahead of anything else that was offered.

CHAIR—What is the distinction between a reconnaissance aircraft and an attack aircraft, helicopter wise?

Brig. Patch—An attack aircraft basically is aimed at carrying a large ordnance load. A reconnaissance aircraft is aimed at being able to observe the enemy without being observed itself.

Senator MARK BISHOP—At height?

Brig. Patch—As an example, the Tiger has a radar cross-section, an aural signature and a visual signature considerably less than that of any of the other tenderers, because it is designed for reconnaissance; it is designed not to be seen. The truth is that it is amazing how close this aircraft can get to you before you even know it is there, and that is what it is designed to do. The reason it has such a low aural signature is that, as a carbon fibre aircraft, it is significantly lighter than a metal aircraft of the same dimension and, if you have

significantly lighter weight, you have significantly less demand on a rotor system and therefore lower pitch and therefore less noise. So, at the end of the day, this aircraft was designed from scratch to be a reconnaissance aeroplane, and we were looking for a reconnaissance aeroplane.

We were going to buy an armaments package with that reconnaissance aircraft, but that was secondary to the fact that we were buying a reconnaissance aircraft. It is not an armed helicopter that can do reconnaissance; this is a reconnaissance aircraft that has arms. That is all it is. What we now have is a reconnaissance aircraft which is without doubt the best of its type in the world, and we have a weapons package that goes with it which is close if not equal to the weapons package that is on any attack aircraft anywhere in the world. We have the best of both worlds.

Because it is designed to do reconnaissance, it cannot carry the massive load of weapons that some of its attack helicopter brethren can. But it is not intended to. The firepower mission and the ability of this aircraft to operate with and directly support the ground forces is a secondary role. What it does is go out well ahead of these forces and locate the enemy so that the ground forces, which it is an integral part of in the combined arms team, can prosecute that enemy. If the ground commander decides to use the capability of the Tiger to do the prosecution, so be it—it has that ability for a limited period with a limited ordnance load. It cannot do it in a protracted fashion; it is not an attack helicopter. But by then you would expect that, because it is working in an integrated fashion with its ground brethren, they would be able to carry out the prosecution and it would be able to withdraw and provide them with accurate reconnaissance information—it has that ability.

It has a sighting system which can look out and see well beyond the normal visual ranges of ground forces. It also has the ability to take still photography of that and deliver it via datalink back to the ground forces so that even though they cannot see the enemy they have a picture of them and know their exact location. It is not about this aircraft and its individual capabilities; it is about the fact that when you integrate it with the combined arms team it provides them with eyes in the sky. It packs a punch if it is called on to do so, but that is not its primary role.

Senator MARK BISHOP—Understood. We then go back to the original question. Even with all the kafuffle that has been in the press and the delayed delivery dates and cost issues and allegations of them not functioning adequately, do you still stand by your original decision? Was awarding the contract to Australian Aerospace the right call then and would it be the right call now?

Brig. Patch—Absolutely. I have no doubt. We bought the right helicopter—absolutely no doubt.

Senator MARK BISHOP—Thank you. Let us now turn to the more salacious aspects of this that have been picked up in the press. I do not think they are press allegations; they were reported by ANAO. The first allegation is that Defence accepted delivery of three Tiger craft that did not meet contractual specifications. The second is that the Tigers delivered could not fly long distances over water. The third is that they did not have the required spares and parts.

The fourth is that they lacked a suitable navigation system. The fifth is that they did not have an emergency locator beacon. Are those findings of fact by ANAO correct or wrong?

Brig. Patch—They are wrong.

Senator MARK BISHOP—Go through each of them.

Brig. Patch—Okay. With the first three aircraft, as I have already said, the contract provides for the Commonwealth and the company to agree to an in-service date configuration. The in-service date acceptance criteria state that the Commonwealth will accept two aircraft of an approved configuration, and that approved configuration was a configuration that I as the project authority approved. We agreed with Australian Aerospace that that configuration could not be exactly established at contract signature. But we agreed that 12 months before contract signature it could. So 24 months before contract signature we started talking about what that configuration would be and by February of 2004—a little bit later than we would have liked—we agreed to an in-service date configuration.

Senator MARK BISHOP—Right. So you agreed on an in-service state—

Brig. Patch—Date—an in-service date configuration.

Senator MARK BISHOP—Okay.

Mr Lewincamp—I could add clarification to the detail. I do not think the Audit Office actually said that we accepted the initial aircraft and that we had intended to accept them at that point as meeting the final contract configuration. The judgment that the Audit Office was making was about whether or not we had clearly specified the shortcomings of the aircraft at that point and whether there was a clear strategy in place for handling the shortcomings. There was agreement between us and the Audit Office that the aircraft at that point did not meet the final contractual specification. Their concern was more about whether that was a reasonable judgment at the time on our part. That was a judgment call on our part at that time, for the reasons that the Chief of Army mentioned in his introduction. So there is no disagreement between us and the Audit Office about the fact at that time. I think some of the later commentary had said that we had intended to accept a fully compliant aircraft at that time, but that is not what the Audit Office said.

Senator MARK BISHOP—Thank you. I accept the point you are making, but the issue is that, in February 2004, there was an in-service date configuration agreed between the parties. The product was then delivered pursuant to the timing in that contract and the product that was developed had those allegedly identified deficiencies: it did not fly long distances over water and it did not have the required spares and parts. The issue for resolution is whether Army's acceptance pursuant to that configuration contract was the right call. That is the issue that I am trying to deal with. The ANAO identified it and it was picked up by the press in purple prose. That is what I am trying to examine with the brigadier.

Brig. Patch—In February 2004 we agreed to an in-service date configuration. At the point that we agreed to that in-service date configuration, the Franco-German program told us that they were going to type-accept their aircraft soon thereafter, and in fact they did. They were the first to type-accept the aircraft and they did that in March-April 2004—some nine months before we type-accepted our first aircraft. So they type-accepted their aircraft. We had agreed

to the in-service date configuration on the basis that the Franco-German program, having slipped, would slip only at a rate of which we had been informed at that point in time, and so we went forward. It is true that in December 2004, when I accepted the first two aircraft, there were deficiencies, even to the in-service date configuration, and almost all of those were directly attributable to the fact that the Franco-German program had slipped even further and we were reliant on the Franco-German program.

Senator MARK BISHOP—The judgment call that you made as to the veracity of Franco-German acceptance, with hindsight again, turned out to be the wrong call and that caused a lot of problems for us in accepting an arguably deficient product?

Brig. Patch—That is true, in part. Yes, I misjudged the timing of the French acceptance of their first aircraft. We were basing that on their advice. Let me say up-front that we owe a great deal of debt to the French DGA. They did a fantastic job in assisting us in delivering our aircraft. The truth is that the French delayed the acceptance of their first aircraft in part because of the amount of effort that they were putting into helping us in the acceptance of our first aircraft. We owe them a great deal of thanks. They did a sensational job and, I might add, they continue to do a sensational job. The working relationship that we have with the DGA is just superb and at absolutely no cost to us.

Senator MARK BISHOP—That is fine and that is interesting. But the first two or three Tigers that were delivered could not fly the long distances over water, did not have the required spares and parts and lacked a suitable navigation system. Have those three deficiencies been fully remedied?

Brig. Patch—I will address each in turn.

Senator MARK BISHOP—Do flying over water first.

Brig. Patch—This aircraft is capable, in the ferry role, of flying over water for 1,000 kilometres. There is nothing stopping this aircraft, as we speak today, from flying over water but one thing. In our acceptance process, safety comes first in every respect. When we did our analysis of the French system—which, as far as the French and Germans are concerned, can fly over water to its heart's content—we determined that if the aircraft inadvertently ditched in water and the crew were required to fire off the explosive ribbon that jettisons the glass of the cockpit, that might cause compression of the crew to the point where they might be injured. So we are currently establishing a process whereby we will put a glass breaker in the cockpit.

There is one minor problem. The 30-millimetre turreted gun at the front of this aircraft is capable of rotating faster than the human neck. That is because it is head tracked by the helmet. Wherever the pilot who has that responsibility is looking, that is where the weapon is looking. That uses a magnetic field, which means that in this aircraft you cannot put anything metallic, other than what was in the original design, above waist level. We have to find somewhere in what is without doubt a very tight cockpit to put a glass breaker and it has to be crash worthy. We are currently going through that process. Once that process is complete, we will then allow Australian crews to fly over water in this aircraft. It is a safety issue and nothing more.

The second issue is spares. There were more than enough spares. We agreed to an in-service date spares purchase and those spares were available to us at in-service date to undertake the testing activities that we had intended to undertake. It was more than capable.

As for the emergency locator transmitter, Senator, you are right: we purchased an off-the-shelf aircraft. That came with an FAA—a civilian qualified emergency locator transmitter—that is only capable of operating to 55 degrees Celsius. It does not meet the 63 degrees Celsius requirement of the military standard. I bought an off-the-shelf aeroplane. When you buy an off-the-shelf aeroplane you do not necessarily get 100 per cent of everything you want, but you save a bucket of money in the process. There are certain things that I will accept as a permanent deviation to the specification, and that is probably one of them.

The last one was the nav system. I made a judgment call when we bought this aircraft. We stripped out of it the TACAN, which is another navigation aid often used by air forces but not often used by ground forces. We also stripped out the non-directional beacon, because at the time Australia had begun to replace all of the non-directional beacons around Australia with global positioning system approaches that do not need any ground aids. This aircraft has a GPS system which is accurate to within five metres. So we stripped out the NDB and the TACAN. It already had a GPS. We inserted an instrument landing system, because that is a standard instrument approach that many airfields in Australia have and the French aircraft did not have it.

So we have changed the navigation system. That means that that instrumentation package has to be given a waiver by CASA because the GPS is a military GPS, meant for landing out in the middle of nowhere and navigating in the middle of nowhere. It is not intended to navigate to a threshold on a brightly lit runway on a dark night. In order to do that, the CASA requirement is that it be RAIM compatible. That means it has certain characteristics that ours does not, but ours is far more accurate than is required. To get a CASA compliant GPS that is in any aircraft to fly into a hole in the trees out in the middle of nowhere is not possible unless you establish that CASA determines a particular approach to those trees. Our aircraft is designed to operate, as I said, as an integral part of the combined arms team. It has to be capable of operating in the middle of nowhere, and that is why we have a twin inertial navigation system and a GPS—so that it can accurately navigate to anywhere it needs to go.

Senator MARK BISHOP—So you say to the committee that those four shortcomings identified by the ANAO have either all been remedied in the first two or three craft and hence for future craft or are in the process of being remedied.

Brig. Patch—They are in the process of being remedied.

CHAIR—And they are highly technical.

Brig. Patch—It is a highly technical process. You cannot do it overnight.

Senator MARK BISHOP—That is okay. Earlier on, you said you went for this particular platform because it had a more useful balance between the acquisition price and the through-life costs for the life of the platform. It is reported that the contractor is now asking for an extra \$625 million for through-life costs for the Tigers. Are those reports accurate, and, if so, why is that?

Brig. Patch—It was our assessment that their claim was worth \$625 million, their assessment was somewhat less. We do tend to be pessimistic in these things. Yes, they have made a claim, or they originally made a claim almost a year ago now, for an increase in through-life support. Their argument was that they had misinterpreted the contract in terms of what was required to provide the through-life support for the Tiger, which they had agreed to provide under a fixed price contract. The Commonwealth's view at the time was that there was no case for the vast majority of what they had claimed.

There is a case for some of what they have claimed, because in order to increase the efficiency of the ARH system, we have agreed, over the time since contract signature, to change some of the work practices. For instance, the Commonwealth had intended to use military uniformed flying instructors as flying instructors on the simulator and to manage the simulator device and uniformed personnel to operate the instructor operator station. The contractor has since shown us that they can do that cost effectively, rather than using military uniformed personnel. So we have agreed to change the structure of the management of the flying training system so that they provide it to us virtually as a one-stop shop. That will cost us more money, and we are in the process of negotiating how much that will cost. That is Brigadier Fraser's responsibility now, not mine.

Senator MARK BISHOP—But in terms of the bulk of that \$625 million, where you say—

Brig. Patch—We rejected it because we do not believe it has foundation. We have directed that the contractor come back to us with the revised business cases so that we can do an accurate analysis of it. There will be increases; it is our expectation there will be increases. They will not be anywhere near the quantum that has been suggested.

Senator MARK BISHOP—The net of that is that you had two strong arguments for going for this reconnaissance platform—acquisition costs and through-life costs. You say that you had a clear understanding of the through-life costs that were involved in the contract. The contractor either has misunderstood or is wrongly interpreting his obligations under the through-life support, although that was the key feature that enabled the contractor to get the contract at first instance.

Brig. Patch—That is true.

Senator MARK BISHOP—How long do you think those negotiations will take to resolve?

Brig. Patch—They have been going for eight months now, they could go for a lot longer, but we continue to operate under a fixed price contract. From the Commonwealth's perspective, we can continue to operate this capability right through to the end of the 15-year contract at the current price. We have no concerns with doing that.

Senator MARK BISHOP—In a fixed life contract such as this, is there a place in the contract for arbitration of disputed clauses like that?

Brig. Patch—There is.

Senator MARK BISHOP—And you or the contractor has a right to avail themselves of that arbitrator?

Brig. Patch—They do.

Senator MARK BISHOP—But you are not choosing to go down that path as yet?

Brig. Patch—We are nowhere near that, Senator.

Senator MARK BISHOP—Thank you for that.

Brig. Fraser—If I may, the original submission that was given to us—contract change proposal for the increase in through-life support costs—was rejected. They have subsequently come back to us with part of that request, and we are in that process now. It is not as if we are at a complete stalemate. The contractor and the DMO are working together to try to come to a reasonable outcome here. I do expect there will be some increase.

Senator MARK BISHOP—I will pursue that in future estimates.

Senator Sandy Macdonald—Hopefully not.

Senator MARK BISHOP—The ANAO made some comments about the need to review intellectual property. I think the argument was that Army might not have had title to the intellectual property in the development side of the machine.

Brig. Patch—There is no question that we have exactly the intellectual property rights that we require. What the ANAO said was that the Defence Force needs to ensure that those intellectual property rights are at a satisfactory quality so that we can exercise them for the purpose for which the contractor expects, which is to operate, operationally maintain and sustain the ARH capability. What they said to us was, ‘In our view you ought to do an audit every so often.’ We have accepted that recommendation and we have already commenced that audit.

Senator MARK BISHOP—I understand also that tests are continuing on the engines for the Tigers, which failed, I also understand, to meet contractual specifications. Can you confirm that the option to replace these engines, according to the manufacturer, may exceed \$110 million?

Brig. Patch—I have prepared a small diagram. I want to explain what the deficiency is. The diagram refers to the most demanding requirement in the Tiger’s specification—that is, for the aircraft to be able to hover out of ground effect, above 50 metres, on a 36.7 degrees Celsius day at midday with clear skies, 29 per cent relative humidity, 23 kilometres visibility in the firepower configuration at Broken Hill, 381 metres above mean sea level, after it has transited 90 nautical miles from its point of take-off. The actual figure is not 100 per cent; it is less, but let us say 100 per cent is the power required to undertake that manoeuvre.

We said in the contract, ‘In addition to that 100 per cent you must be capable of providing a 10½ per cent margin on top of that for pilot error,’ in case the pilot accidentally pulls the collective a little hard. You do not want to overtorque a \$40 million aeroplane. The deficiency is that they can only provide 7½ per cent more than is required. The pink bit at the top of the diagram shows the deficiency. We are talking about me going to the Chief of Army and saying: ‘Chief, here’s the deficiency. Do you reckon that’s worth \$110 million? The contractor is willing, as the contract requires, to make that difference up at no cost to the Commonwealth.’

Senator MARK BISHOP—Are you saying it is a trial?

Brig. Patch—Going back to my point, the first course you do in project management is Pessimism 101 and the second course is Pessimism 102! We went to the contractor and said: ‘What happens if you can’t make up that three per cent or, as the ANAO has pointed out, if in making up that three per cent you reduce the range that the aircraft can fly?’—although I must admit in the contract we have already dealt with those issues—‘We want something better than that. You’ve got to give us something better.’ So we negotiated an agreement. That agreement is that, if they cannot make up the three per cent and at any time in the future of the Tiger at the Commonwealth’s choosing we wish to purchase the upgraded engine which is being developed for the Spanish and French versions of the ARH, we can do that at cost price. Cost price for the entire fleet is about \$110 million. The deal is that, in the very rare instance that this does not meet our requirements, we have that as a fall-back. That is all it is.

CHAIR—Is that an agreement in writing?

Brig. Patch—We have it in writing. So if at some stage in the future the Chief of Army decides that the Tiger needs to be able to carry eight Hellfires instead of four—the current engine cannot do it—we can say to the chief: ‘Not only can we deliver what you want but we can do it at cost price, for nominal saving, no profit and no margins—nothing. We can go forward with it.’ I would expect the Chief of Army at the time would consider that. But I do not expect General Leahy to consider it in the next few years.

CHAIR—This is the first international sale of this aircraft. Is that right?

Brig. Patch—It is. The Spanish were to follow us, but it is the first international sale.

CHAIR—It seems from what you have just said that the contractor is keen to impress.

Brig. Patch—The contractor was very keen to impress, yes.

CHAIR—And you are satisfied with the resolution of that issue such that all of those media reports have now been answered.

Brig. Patch—I do not think the media reports ever had any basis. There was clearly a misinterpretation.

Senator MARK BISHOP—Clearly. Let’s turn to the budgeted cost for the project Air 87. At June 2005 they showed approved costs for test and evaluation of \$22.7 million and actual expenditure of only \$300,000-odd—\$0.3 million. Why the discrepancy between actual and approved?

Brig. Patch—When we first agreed to purchase this aircraft, because Australians tend to be rather brash, one of the things we got Eurocopter to agree to in the contract is that, although there was a significant amount of testing yet to be done—at their expense—in order to deliver the capability, we wanted to insert into their test capability a number of qualified test pilots so that we could from the very outset be involved in the test program, get more understanding of the aircraft and even have an input into its design. We expect that after the acceptance of the aircraft, as the Chief of Army has already suggested, there will be an initial operational capability delivered, and up to and including that there will be production acceptance and some design acceptance, but beyond that there is operational test and evaluation.

I am responsible for that operational test and evaluation—for funding it and for paying for the training of all the people who participate in it so that the Army can do its trials of the aircraft in operational scenarios, not in the controlled airspace where we currently do development and production acceptance. So that \$22 million is the provision that I have in the contract to pay for Army to do troop trials and other such exercises so that they can undertake it and deliver an operational capability.

Senator MARK BISHOP—Are you saying that that money allocated for approved test and evaluation is to be spent at a later time?

Brig. Patch—It has not yet been spent. I have done all the test and evaluation that I require at this point, either at Eurocopter expense in France and in Australia before we accepted the aircraft or within project costs after it. Although the ANAO would not accept that it was the case, there are many milestones in this contract delivery schedule after the in-service date where we are progressively delivering increased capability.

Senator MARK BISHOP—Why don't ANAO buy that argument you have just put?

Brig. Patch—I have no idea. I spent 11 months trying to convince them of it.

Senator MARK BISHOP—Are they of the view that the test and evaluation funds should have been spent prior to accepting delivery of any of the platforms?

Brig. Patch—One of the other issues that the ANAO had with us was that we accepted the first aircraft and we have the lead aircraft worldwide. That is not the case. The French type-certified their aircraft some nine months before ours. What happened was that we had a very different acquisition strategy to the Franco-German program. They developed the helicopter. They had the money to put four or five prototype aircraft into service before they accepted their aircraft. We did not have that luxury. I did not have the money to go and buy a prototype aircraft, so I relied upon the French, with my test pilots assisting them, to do that test and evaluation on their prototypes, one of which they converted as close as possible to an ARH at their expense.

So we did our developmental test and evaluation on French aircraft, on the prototypes. Since then, as has already been said, one of the reasons we accepted an interim configuration was so that we could do test and evaluation of critical components. The chief mentioned a couple of them. Hellfire is clearly one. The other one is secure radio communications. The American radios, which we have installed in the aircraft to ensure interoperability with our US and other NATO allies, were not available to the French, so we had to wait until we got to Australia to be able to do the test and evaluation on them.

Senator MARK BISHOP—What do you say to the argument that there has been insufficient test and evaluation of the platforms accepted into this country and that the money—that figure of almost \$23 million—should have been spent on doing the T and E of those platforms?

Brig. Patch—There is no justification for such a statement.

Brig. Fraser—We will still conduct some test and evaluation—for example, to get our aircraft to be capable of flying on night vision devices. We are going to fly more aggressively that way than the Franco-German system allows. So for an Australian part—it is not unique

but it is an enhancement of the capability they have—we will conduct some test and evaluation. It is minor in the scheme of the life of the aircraft and the state of the aircraft, but we will be conducting some of that test and evaluation.

Senator MARK BISHOP—Why is the T and E of the French prototype—as near as possible to the eventual platform that was delivered here—adequate to satisfy you that the platforms that were delivered here do not need to be separately tested and evaluated?

Brig. Patch—We are doing production acceptance test and evaluation on each aircraft, but the developmental test and evaluation that led to the decision for us to go into production was all done on the French prototypes. The project did not have the funds to purchase a prototype ARH and then conduct developmental test and evaluation on that prototype.

Senator MARK BISHOP—So it would have been cost prohibitive to go down that path.

Brig. Patch—Absolutely.

Brig. Fraser—The issue about the Franco-German program being in front of us at the time that the ANAO wrote the report is that we had compressed that time and we had accepted more aircraft than the French or the Germans. Since the writing of the report we have accepted the same number of aircraft as the French and the Germans have, but they are well in front of us with the training of their crews. They were at the point of continuing with the full training of their crew personnel. I do not want you to take the wrong impression regarding our concerns about the ANAO report and the status of the Franco-German program versus ours.

Senator MARK BISHOP—I got the point. What is the total number of hours flown by Tiger aircraft since 1 January this year? Can we have those figures?

Brig. Fraser—I can give you the figures since 1 January. The figures that General Leahy gave you, the 875 total and the 315 in Australia, are for the complete program. We normally measure our hours over a financial year. We had originally forecast that that would be a higher figure than we are currently going to achieve. At the moment I envisage that we will achieve for the financial year 275. So, since 1 July last year—

Senator MARK BISHOP—That is 275 hours?

Brig. Fraser—That is correct, for the financial year.

Senator MARK BISHOP—For the 2006 financial year.

Brig. Fraser—For 2005-06, yes.

Senator MARK BISHOP—Under the contract schedule, how many Tiger pilots—

Brig. Patch—Do you want the figure from January?

Brig. Fraser—I will have to calculate it and get back to you.

Senator MARK BISHOP—Thank you. Under the contract schedule, how many Tiger pilots, not including test pilots, were scheduled to have been trained by the end of May 2006?

Brig. Fraser—I will do my calculation in a second. I will explain the training scenario, where we are at and how we might work our way forward. There are delays, clearly, in the training system. We would have liked to have had—and we had envisaged having—four instructors trained in France before we even started the Australian program. As the French and

German programs were delayed, that did not eventuate. We have had various strategies with the contractor and their parent companies to try and recover this training program. We have now trained one Australian instructor, who requires some consolidation but who has completed his training course, and we have qualified one test pilot as an instructor. It is our intention to have five instructors by the end of the year and to start training our pilots by the end of this year, first up into next year. We are also looking to have the simulator available in order to do that.

At the moment the contractor believes that the program is six months late in order to achieve this operational capability. There are a number of things that would be required to make that occur, and we consider that fairly high risk. Our assessment is that it will be somewhat longer than that. General Leahy indicated that it would be in the order of 18 months or so. What we would like to try and do is to work together to ensure that we achieve an operational capability, which is the individually training. We may be able to start training some of the collective work and meet some of the general's requirements of getting a troop level up even before all those individuals are trained.

Brig. Patch—To answer your question, Senator, by this time, May 2006, we would have expected to have completed the first course of six pilots and to be training the second course of six pilots at the same time as we converted a number of the pilots into battle captains—that is, aircraft captains.

Senator MARK BISHOP—Thank you, Brigadier. What is the time slippage in this contract, or do we regard it as being on schedule?

Brig. Patch—According to our own value management systems, the current slippage is approximately six months—with the exception, of course, of the training system. The delay to the production is due to an internal Commonwealth issue with the number of test and evaluation crews that we have available.

Senator MARK BISHOP—So, excluding the training issue, you say the time slippage in this contract is only of the order of six months—

Brig. Patch—Six to seven months.

Senator MARK BISHOP—When all of the platforms are delivered and warranted as satisfactory for operations in the context of the contract—that is, conform to contract specifications—what will the time slippage be then, do you think?

Brig. Patch—The contractor would have you believe it is six months; our estimate is more like 18 months.

Senator MARK BISHOP—Similar to the French.

Brig. Fraser—Yes, it is. We have compressed some of it. What we are trying to do is to ensure that, when we have our people trained, the aircraft will be fully operational and fully capable. In fact, we need it before that so that we can complete the training for them. Just to give you that figure, it was 67.5 hours for this calendar year, since 1 January.

Senator MARK BISHOP—Thank you for that. Could we now turn to the next set of helicopters: the MRH 90.

Senator HOGG—Does DMO consider the MRH 90 to be a developmental aircraft?

Brig. Patch—No.

Senator HOGG—Why not?

Brig. Patch—We are buying an aircraft which is being purchased at this stage by 14 other nations. We are buying the 51st aircraft off the production line as our first aircraft. We are buying an aircraft which is essentially, with only minor changes, the same configuration as the German TTH aircraft—the troop transport helicopter—which was qualified by the European certification agency in April 2006. It will be type certified on 21 June 2006 and accepted by the German defence force on 18 August this year. There are nine NH 90s which will be accepted this calendar year by five nations: Germany, Greece, Finland, Italy and Sweden. Twelve of the German aircraft, TTH variants, will have been delivered and will have been operational before our first aircraft is delivered in December 2007. By any measure, the aircraft is not developmental.

Senator HOGG—As originally announced by the government, are all 12 of the aircraft still to be delivered by 2008?

Brig. Patch—The first two aircraft will be delivered in December 2007. The final aircraft of the first 12 will be delivered by October 2009.

Senator HOGG—That is at variance with what was originally expected, is it?

Brig. Patch—No.

Senator HOGG—Has there been any change in the contract value that had been announced?

Brig. Patch—No. It is a fixed price contract.

Senator HOGG—Did the contract include all of the support systems and equipment needed to successfully train the crew and operate the aircraft?

Brig. Patch—The current contract includes an interim and transition phase training package. It does not include a mature or sustainment training package. That is to be developed and delivered as a part of phase 4.

Senator HOGG—You said ‘an interim and transitioned phase training package’. Are they two separate packages?

Brig. Patch—No. They will blend together but they are two quite significantly different training requirements. The first is to take the first crews and train them. The majority of that will be done in France. The second is the commencement of both air crew and ground crew training in Townsville.

Senator HOGG—When will that take place?

Brig. Patch—It will take place up to and including the middle of 2010.

Senator HOGG—When will the training start?

Brig. Patch—Training will begin in March 2007.

Senator HOGG—Will any of that training take place in Australia?

Brig. Patch—Yes.

Senator HOGG—Is that at the mature stage?

Brig. Patch—No. The transition stage training will be conducted in Australia: in Townsville for air crew and in Oakey for ground and maintenance crews.

Senator HOGG—Will there be something such as a simulator needed for that training and is that part of the package?

Brig. Patch—There will be. That is to be purchased under phase 4.

Senator HOGG—When will phase 4 operate?

Lt Leahy—Phase 4 is with the government at the moment.

Senator HOGG—Do we know when a decision is expected?

Lt Leahy—It will be when the government chooses to announce it.

Senator HOGG—I accept that, but there must be some sort of timetable that you people are operating under?

Mr Smith—It will be this year.

Senator HOGG—Is it imminent or is it months off?

Dr Gumley—It will be some time this year.

Senator HOGG—Given the technical performance issues that have been discussed about the Tiger, can DMO confirm that the Australian MRH 90 project will meet the initial specifications, including those announced by the government, such as seating 20 troops, electric blade fold and a 900-kilometre range?

Brig. Patch—The initial aircraft will not have a blade fold capability but it has 20 seats and it is capable of seating 20 personnel.

Senator HOGG—So it will meet that.

Brig. Patch—And it will have the range.

Senator HOGG—What about the electric blade fold?

Brig. Patch—No. The initial purchase will not have a blade fold.

Senator HOGG—Is that for later on?

Brig. Patch—It will be an option for later on and is certainly a consideration for other variants.

Senator HOGG—If it is an option for later on, will that be at an additional price?

Brig. Patch—In the phase 4 contract we will ensure the contractor provides us with both a price and a schedule for the delivery of the blade fold capability.

Senator HOGG—Have any technical performance changes been negotiated to date?

Brig. Patch—Could you define ‘technical’?

Senator HOGG—You are the technical person, from what I have heard.

Brig. Patch—The procurement of an off-the-shelf helicopter, as I have already said about ARH, may not necessarily meet 100 per cent of your initial requirements. There will be and there has been some negotiation of the Commonwealth's requirements. For instance, to be compatible with the United States we require a VMF datalink, which is different to the datalink in the European aircraft. So we will be providing a VMF datalink and we will be the initial procurer of that datalink.

One of the benefits of our time in ARH was that we learned that if you develop a certain element of a capability then you should be able to claim royalties from other countries that use that capability. For MRH, in every instance where we have done any development—minor as it is—on the aircraft, our contract allows for the payment of royalties to the Commonwealth by other nations. I did not mention it at the time but the same is true of the Hellfire capability on ARH. If other nations fit the Hellfire capability, we have the opportunity to earn royalties, as I noted in the ANAO report, which may be sufficient to completely cover all of our costs for the development of the Hellfire capability.

Senator HOGG—If there are delays in the project, are there any liquidated damages available?

Brig. Patch—There are substantial liquidated damages available under the contract.

Senator HOGG—Are those the same as have been negotiated by other countries?

Brig. Patch—No. The provisions under which we have negotiated our aircraft are far better than those of other nations. Up until this point, most of the nations have been a part of a developmental consortium and it is not in your best interest as a part of the developmental consortium to hit the company that you support with liquidated damages.

Senator HOGG—I understand that but, surely, there would be some that are not part of the consortia.

Brig. Patch—I am not privy to all the terms and conditions of the other nations.

Senator HOGG—Are you able to let us know what the liquidated damages are?

Brig. Patch—I can take that on notice. I do not know what they are off the top of my head. I should be able to get that fairly quickly.

Senator HOGG—What is the likelihood of any further changes to the contract that is in operation at this stage?

Brig. Patch—Our intention is that, when we have approval to negotiate the phase 4 and phase 6 contracts, the phase 2 contract which is currently in operation will be integrated completely into a single contract with those other two phases. The MRH contract package is a three-contract package. There is an overarching program agreement or strategic agreement, which has been developed under the auspices of the DMO aerospace sector plan, to establish a strategic relationship with the contractor. It gives us Australian industry capability provisions and options for future purchases. Those future purchase options are being used to secure significant discounts for future purchases under phases 4 and 6. It is our intention to ensure that a single MRH contract is the result of those negotiations, so, yes, there will be some changes.

Senator HOGG—And milestones.

Brig. Patch—As is the case with ARH, there are a series of milestones worth 60 per cent of the contract value, and 40 per cent of the contract value is to be paid under earned value management systems.

Senator MARK BISHOP—What are earned value management systems?

Brig. Patch—Earned value management is a process by which the work to be done in order to deliver a particular milestone is divided into small chunks, commonly known as work packages. As each of those work packages are opened or commenced and closed, the Commonwealth pays for that part of the work package, so there may be 200 or 300 work packages in delivering a particular milestone. The significant benefit to the Commonwealth is that it offers us insight into their management and pricing structure. In fact, under ARH, when I first started turning up at Eurocopter and describing their current contractual situation in terms of product to them, they were so concerned that I had that visibility that Eurocopter has now introduced an earned value management system across all contracts. It is a system whereby we can establish the cost of work packages and we pay incrementally for those work packages. On a monthly basis they report to us on how many of the work packages they have completed and we work with them to verify that and pay them on that basis.

Senator MARK BISHOP—It is ongoing progress payments—defined, achieved, specified work?

Brig. Patch—Yes.

Air Marshal Shepherd—Senator Bishop and Senator Hogg, I refer you to your questions earlier regarding people leaving the service and working for civilian employment. An Air Force officer was mentioned who had committed a breach. I will just run through a statement I have here. The Air Force member concerned had commenced long service leave prior to discharge on 23 September 2005. At the time, the member's intended discharge date was 17 January 2006. As you heard, from the inspector-general's investigation, the member's alleged improper involvement in the preparation of a tender response to the RICTMT request for tender, which is an IT outsourcing tender, found that this member had undertaken the work during a period of long service leave, without obtaining the necessary approvals. The member then put in a retrospective request for approval under DIG PERS 25-2. That was put in on 23 November and approved in short order on 24 November. Nevertheless, the member had failed to comply with the requirements of DIG PERS 25-2 by undertaking off-duty employment without approval. The member was issued with a notice to show cause why a censure should not be imposed as per DIG PERS 35-6, 'Formal warnings and censures in the Australian Defence Force', and the member was then placed on a unit formal warning for three months.

Senator MARK BISHOP—Because he did not apply at the right time?

Air Marshal Shepherd—Because that member had not applied for permission to work whilst still employed in the Defence Force, although the member was on leave preparatory to getting out. In a parallel activity that member's separation from the service had been delayed until June this year, due to a medical complaint that has nothing to do with this situation; the three months formal warning was served out and the member is currently undergoing transitional processes to civilian life.

Senator MARK BISHOP—That is the technical answer.

Air Marshal Shepherd—That is the answer.

Senator MARK BISHOP—Notwithstanding the fact that the particular officer was retained by the contractor to provide assistance in the drafting of its tender for the particular project, the bottom line is whether his knowledge derived from his work added no value to that particular process?

Air Marshal Shepherd—I understand that the member was moved from the tender process forthwith.

Senator MARK BISHOP—He was removed from the tender process?

Air Marshal Shepherd—I understand that is true. The inspector-general would probably be able to clarify that point. You can check it, but it is my understanding that the member was removed from the tender process.

Senator MARK BISHOP—Why was he removed from the tender process?

Mr Smith—But the company was not.

Air Marshal Shepherd—No, the company was not.

Senator MARK BISHOP—Why was the officer removed from the tender process when he resumed work if the knowledge he had gained from previous employment was of no value or not in conflict with the tender requirements of the company?

Air Marshal Shepherd—The member is still actually employed in the service now, but I think the member was removed from the tender process while the member was on leave.

Senator MARK BISHOP—And has not been involved in the tender process since?

Air Marshal Shepherd—That is my understanding. We will confirm that for you tomorrow.

Senator MARK BISHOP—Can you also confirm that his task whilst employed with the tender company did not in any way draw upon skills or knowledge derived from his time in service which would have given the tender company a commercial advantage over competitors in the tender process?

Air Marshal Shepherd—I will make a statement about that tomorrow.

Rear Adm. Ruting—I have information on Senator Bishop's two questions on the FFG upgrade. Firstly, the value of the total contract with ADI, as I mentioned, was \$969 million at the base date in 1998; in January 2006, the price basis is about \$1,164 million. With respect to training costs for the extra capability between baseline builds 1 and 2 and then 2 and 3, the original contract for the FFGs only covered the first two ship crews—for HMAS *Sydney* and HMAS *Melbourne*—being trained at contractor expense with the training for subsequent crews being at Defence's expense. The extra training would, in fact, be for anything after that capability is delivered with HMAS *Melbourne*; training for the second ship would be at Defence expense. However, cognisant of the fact that the capability delivery for those higher baselines has been delayed, the project director is in the process of negotiating with the prime

contractor for a proportion of attribution of those extra delta training elements between the contractor and the Commonwealth.

Senator MARK BISHOP—Thank you.

Mr Veitch—This morning Senator Bishop asked a question about the cost of the Al Muthanna deployment. I mentioned that overall the government had provided \$1.635 billion for all operations in Iraq. We estimate that the cost of the Al Muthanna component—the deployments to date and the new deployment for six months hence—will total \$376.7 million. You also asked for some clarification of the personnel numbers that were in the finance budget paper No. 1. I have been advised that the number used in the Treasury paper, 51,091, was a figure that we had advised on 20 April when the department of finance estimate system was closed off for the budget. The figure that we subsequently used, which was 51,253, was a later estimate that we had developed based on our consultations with the services, and we used the more up-to-date estimate in our documentation.

Senator MARK BISHOP—Can I conclude from that that the closing date for information from departments for PBS publication is different to the budget papers?

Mr Veitch—It should not be, and it is probably an oversight by us that we published an updated estimate. In hindsight, I would have preferred to publish the one that we had used at the earlier date. But I can confirm that the estimate that we published is our more recent and most current estimate.

Senator MARK BISHOP—So the budget paper had figures from around April 2006 and the PBS had figures from the middle of May 2006.

Mr Veitch—Yes. Because we did not send it to the printer until about 5 May, we used an updated figure.

Senator MARK BISHOP—That is interesting. Thank you.

Mr Veitch—There was one other point. You asked for some clarification on the non-capital investment by function in table 20. We have some verbal advice from finance and I think it is a little too complex to talk about tonight. What I would prefer to do, if you are agreeable, is to give you the answer in writing.

Senator MARK BISHOP—Yes.

Mr Veitch—It draws on quite a lot of numbers that are scattered through both the Defence and the DMO parts of the document.

Senator MARK BISHOP—Do that in writing and, if I have issues, I can come back to you next time.

Mr Prior—I have some information on some questions that Senator Payne asked. Regarding the 9,178 people we have trained in the 2005-06 year, the split between ADF and civilian personnel is 4,996 ADF participants and 4,182 civilian participants—not a bad split. You also asked about who the outsourced providers are. We are using six during the course of this year: Major Training Services Pty Ltd; Deakin Prime; CIT Solutions Pty Ltd—that is CIT's training arm—Achieve Training, Employment and Business Solutions; Impart; and, finally, Southern Cross University.

Senator PAYNE—Thank you for coming back.

CHAIR—I think we are into Super Seasprites. I see Dr Gumley is very keen to join in this.

Senator MARK BISHOP—During the life of the contract for the Seasprites, did the DMO review the contract at any time?

Cdre Campbell—Yes, on several occasions.

Senator MARK BISHOP—You reviewed the contract, after it was signed off on?

Cdre Campbell—Yes.

Senator MARK BISHOP—What advice was given to the minister at the conclusion of each of those reviews?

Cdre Campbell—The minister has been constantly updated on this program since it began. I do not have to hand the specific advice on what the minister was told about the contract reviews, but—

Mr Smith—And he would not, of course, go to the detail of that advice, but successive ministers have been successively updated.

Senator MARK BISHOP—There have been a series of reviews over the last 10 years on this contract; is that correct?

Cdre Campbell—Specifically in 2002 and 2004 there have been significant reviews.

Senator MARK BISHOP—There have been two reviews in 2002 and 2004, and each time the relevant minister was provided advice as to the review?

Cdre Campbell—Yes.

Dr Gumley—I think it would be fair to say this contract has been under constant review, certainly since I have been in DMO. It is monitored every three to six months to see how it is progressing. We certainly have not gone to sleep on it; it has been a very difficult one to manage.

Senator MARK BISHOP—Why has it been a difficult one to manage?

Dr Gumley—Firstly, the project was clearly late. Secondly, the specifications were 1996 specifications and the specification environment has moved on a bit since then. Thirdly, and probably most importantly, contractor performance has not been adequate by our version of what we expected. And it has always been a challenge to ensure that a contractor, who probably is not making any money on a fixed price contract, adds sufficient resources to a contract to get you over the finishing line. There is not a lot of motivation for a contractor in those sorts of situations to keep on working.

Senator MARK BISHOP—Was advice given to the minister in either 2002 or 2004 to try to find an escape clause from the contract?

Dr Gumley—Again, we cannot comment on advice that we have given our minister.

Senator MARK BISHOP—All right. In the last round of estimates in February, Air Vice Marshal Rossiter stated:

All going well, with not too much rework out of that, we would hope that, by the middle of the year, we would be looking at getting our first fully mission capable aircraft.

Subsequent to that advice, on what advice did Dr Nelson announce his review of the Seasprite project?

Cdre Campbell—Air Vice Marshal Rossiter made those comments to the best of his knowledge at that time. We then had an incident in early March where we had quite a benign malfunction in the aircraft's automatic flight control system. That raised concerns about the reliability and the design of the automatic flight control system, such that the Navy's operational airworthiness authority suspended flying and then Dr Nelson ordered his review.

Senator MARK BISHOP—What exactly has Dr Nelson ordered a review of? Is there a publicly available document, apart from his press release advising of the terms of review?

Mr Smith—That is the only public document.

Senator MARK BISHOP—The press release?

Mr Smith—Yes. He has made some comments to the press.

Senator MARK BISHOP—There was a press release and there were some comments to a conference here in Canberra that was reported in the press. So what exactly has Dr Nelson instructed the department, or the DMO, to review?

Dr Gumley—There was an intermediate step. We had a three-star review down at Nowra comprising the Chief of Navy, Chief of Air Force, Chief of Capability Development and myself. We had a program review of what had happened and what some of the options and alternatives might be. Then we reported that back to our minister.

Senator MARK BISHOP—Okay, so you had essentially a chiefs of services meeting with yourself, Dr Gumley, to identify the problems reported on your views to the minister. Arising out of that report did he determine then to go forward with a full review?

Dr Gumley—The minister announced that there is to be a further review of some alternatives. The chief of the capability group might talk about what they might be.

Senator MARK BISHOP—What does that mean?

Lt-General Hurley—The minister had directed us to look at the options we have for achieving the capability that was required under the Super Seasprite project—that is, to provide that naval combat capability off our frigates. In doing so, we are going to look at three options. One is to continue with the Super Seasprite project, where that might get us to. Secondly, we will go out to look at two other helicopters—the Sikorsky 60R Seahawk and the Eurocopter Agusta NH 90 maritime or naval combat aircraft. So we will be looking at those two options over the next couple of months in addition to the Kaman option and we will take the three options back to the minister.

Senator MARK BISHOP—Has the minister given you a time frame for that review?

Lt-General Hurley—No, he hasn't given us a time frame. He has asked us to come back to advise him of what the plan for the way ahead would be.

Senator MARK BISHOP—The plan for the way ahead of the review?

Lt-General Hurley—How long it will take us to work out these options. So we have to contact the management of the international companies, go and do the visits, find out what is available, do the cost assessments and build business cases essentially for each one. The long pole in the tent is probably the Kaman response, how long it might take them to get the aircraft at an acceptable level. Once we know that, it will give us a time frame to do the whole package. So I am looking at about three months.

Senator MARK BISHOP—So the sequence is this. The heads of two services and Dr Gumley and General Hurley had a meeting after a major problem was identified.

Lt-General Hurley—Those in attendance were Dr Gumley—from DMO's perspective he ran the Seasprite project; the Chief of Air Force from the airworthiness technical side of the house, the Chief of Navy as the capability manager and me because if we are going to look for other options I would be the person going out looking at the capability options available.

Senator MARK BISHOP—So the four of you had the meeting. You reported back to the minister. Arising out of that he gave instructions for a review to occur and you have been tasked with developing the framework of that review. You are in the process of doing that and you think it will be concluded in three months.

Lt-General Hurley—That is my estimate at the present time. I am still waiting for my staff to come back because they are contacting local members of the firms here. We are writing off to the senior management of Sikorsky and so forth saying 'This is what we need.' We have a team leaving for the United States and Europe I think in the second week of June to visit those companies, get the data, and at the same time DMO is in discussions with Kaman about what they might be able to do.

Senator MARK BISHOP—And that review is designed to achieve the same level of capability that the Seasprites were proposed to bring to the frigates.

Lt General Hurley—To provide that naval combat capability that we seek for the frigates, yes.

Senator HOGG—That is not to actually make a decision on which are the alternatives.

Lt General Hurley—No, it is to provide a way ahead.

Senator HOGG—It is just to say, 'These may well be the alternatives and we suggest you should look at this.' Meanwhile, what happens to the Seasprite project? Is it at a standstill?

Dr Gumley—It is progressing.

Senator HOGG—It is still proceeding.

Dr Gumley—Yes, recalling that it is a fixed price contract, and the contractor still has an obligation to deliver—the contractor just cannot down tools. It is a fixed price contract.

Senator HOGG—That's fair enough.

Senator MARK BISHOP—The fact that you have grounded the aircraft has no bearing on the contractor's—

Dr Gumley—The difficulty is that some software changes are going to have to be made. While they make these software changes it does not really matter whether the aircraft is flying or not.

Senator MARK BISHOP—General Hurley, that is a very short time frame in which to do a detailed review of the other two options for delivering the same level of capability, is it not?

Lt-General Hurley—It will have us on our toes, but I have asked Chief of Navy for additional personnel to help me to do it and to put together some specific teams that will work their way through this. It will not be the first-pass quality that we would normally expect, but we will be able to go to government and say, ‘This is when you could get helicopters if you decided to change horse; these are the risks you would take on because the Sikorsky helicopter that is coming off the line now is different to our Seahawk.’ Do we then make decisions about bringing them to a uniform standard? What is the risk in doing so? The European helicopter is a developmental helicopter in the sense that it does not have a lot of the characteristics and capabilities we need; what is the risk in our travelling down the route? So we have got to bring those up. There is no easy solution here, because each of the options has its own attendant risk in terms of cost capability and schedule.

Senator MARK BISHOP—Does the US Navy use Seahawks as platforms off their ships?

Lt-General Hurley—Yes.

Senator MARK BISHOP—Are you considering them as an option in this review?

Lt-General Hurley—That is the Sikorsky MH-60R, which is the Seahawk equivalent.

Senator MARK BISHOP—Yes, the Seahawk equivalent.

Lt-General Hurley—But it is different from our current version of the Seahawk.

Senator MARK BISHOP—Is it the more advanced version?

Lt-General Hurley—Yes.

Senator MARK BISHOP—Is it several generations ahead?

Lt-General Hurley—It is one generation ahead. There are two versions of the Seahawk. There is an international version and the 60R version. We will look at both of those, but the 60R is the one with the greater production numbers and so forth.

Senator MARK BISHOP—So you have this ongoing review of the current Seasprites, plus two alternatives. That is going to take three months, and additional resources have been allocated and you have additional teams. Meanwhile, work under the existing contract continues to be required and is being done.

Lt-General Hurley—Yes.

Senator MARK BISHOP—What about the issue that caused the platforms to be grounded? Was it the automatic pilot?

Cdre Campbell—It was the automatic flight control system.

Senator MARK BISHOP—Tell me about the automatic flight control system.

Cdre Campbell—In English, Senator?

Senator MARK BISHOP—Yes.

Cdre Campbell—There is a small computer card, that is effectively the size of a credit card, that fits inside the automatic flight control system. It became loose and then sent erroneous data into the automatic flight control system, which caused the helicopter to drive in one particular direction.

Senator MARK BISHOP—Is this a major problem? I appreciate that it is a serious problem. Is it a problem that can be rectified in a two- or three-month period? It is essentially a software problem, isn't it?

Cdre Campbell—It is a software problem that needs fixing, but because this is a safety-critical system—an automatic flight control system—it is not an area that you just play around with. The software experts tell me that it is at least a six-month job.

Dr Gumley—And then there would be tests and evaluation to prove that it works.

Senator MARK BISHOP—That would be what, another three months on top of that?

Dr Gumley—Probably six months on top of that.

Senator MARK BISHOP—So at best guess, it is likely to be at least 12 months before you will be able to—

Cdre Campbell—Somewhere between six and 12 months is our current estimate, but there is a lot of work going on right now on that exact topic.

CHAIR—Who is paying for this?

Cdre Campbell—The Commonwealth position is that the command has not yet delivered us an aircraft in accordance with the contract, and we believe it is their nickel.

CHAIR—So the prime contractor is liable to find and access a subcontractor who can rectify this problem?

Cdre Campbell—They are doing a lot of work themselves. They have already found the problem with the card that I described earlier, but they have to do some other additional work with the software to rectify the problem. They can do that in house.

CHAIR—The flight control system is not just about flight control; it is part of an integrated system that has to be interfaced generally with the command and control system on this helicopter—is that right?

Cdre Campbell—That is correct.

CHAIR—In other words, it is very complex?

Cdre Campbell—It is, but it is a small, well-defined part of the actual overall system. It is only 5,000 lines of code in a huge mission computer. So this 5,000 lines of code inside the automatic flight control system is something that is easily defined and got at.

CHAIR—Who is the architect of the command and control system?

Cdre Campbell—Kaman itself, but its two subcontractors are Northrop Grumman and CSC Australia.

CHAIR—Are they both still involved in this project?

Cdre Campbell—They are.

Senator MARK BISHOP—So it will be at least 12 months before Dr Gumley, or whoever the responsible officer is, will be able to authorise the Sprites back in the air?

Cdre Campbell—It is somewhere between six and 12 months, and it is actually a call of the Navy.

Senator MARK BISHOP—But it could be up to 12 months?

Cdre Campbell—Yes.

Senator MARK BISHOP—If the government determines to stay with the existing contract and existing platforms, is there any extra cost involved?

Cdre Campbell—Potentially. We are working through that with the contractor at present.

Senator MARK BISHOP—What sort of magnitude are we talking about?

Cdre Campbell—I would not like to put a figure on it at present because, as I said, a lot of engineering design and analysis work is going on right at the moment. I would not like to hazard a guess.

Senator MARK BISHOP—Have we paid up to \$1 billion so far to the—

Cdre Campbell—No, we have paid about \$890 million to 30 April.

Senator MARK BISHOP—How much is outstanding?

Cdre Campbell—About \$40 million is outstanding.

Senator MARK BISHOP—So it is 95 per cent paid already?

Cdre Campbell—Correct.

Senator MARK BISHOP—There was press speculation—and I do not know whether it came from Defence or otherwise; I cannot recall—at one stage that we would need something in the order of another \$150 million to get the Sprites flight worthy. Can you comment on that?

Cdre Campbell—It is pure speculation.

Senator MARK BISHOP—That figure did not come from Defence?

Cdre Campbell—No.

CHAIR—How much is the contractor committed to it? Are we aware of the contractor making any payments to do some of this rectification work?

Cdre Campbell—They have started some work already, yes.

CHAIR—At their expense?

Cdre Campbell—At their expense.

CHAIR—Do we know how much they have committed in terms of dollars at this point?

Cdre Campbell—It would not be much. They have committed something. This problem is only a couple weeks old, and they would have committed to a couple of weeks work by a couple of design engineers. It is not a large figure.

CHAIR—It has been suggested to me that the overall contract has cost them a considerable amount of money.

Cdre Campbell—That is correct.

CHAIR—What do you understand to be the amount that it has cost this contractor?

Cdre Campbell—It has cost them a considerable amount of money.

CHAIR—I have heard \$100 million.

Cdre Campbell—They have reported about that figure.

CHAIR—And they are a publicly listed company in the United States?

Cdre Campbell—Yes.

CHAIR—So they have had to report to the stock exchange in the United States?

Cdre Campbell—That is correct.

CHAIR—And they have reported that they themselves have committed \$100 million to this project.

Cdre Campbell—It is not quite \$100 million, but it is getting up towards that figure.

Senator MARK BISHOP—Did any of these Seasprites serve in Vietnam?

Cdre Campbell—These actual airframes? Before I answer that, Mr Chairman, I would just like to point out that the company is still very committed and working hard on this.

CHAIR—That is what I was given to understand. That is why I was asking the questions.

Cdre Campbell—They have put a big financial commitment into this. To answer your question, Senator Bishop, I believe one or two of the airframes—and I would have to check this—saw service in the Vietnam War.

Senator MARK BISHOP—What is the total we are purchasing?

Cdre Campbell—Eleven airframes.

Senator MARK BISHOP—So one or two of them did see service in Vietnam?

Cdre Campbell—Yes.

Senator MARK BISHOP—Of the other nine or 10, have they seen service anywhere?

Cdre Campbell—I think several of them saw service in the Gulf during the Iran-Iraq war in the late eighties. That would be a fairly reasonable guess, I suspect.

Senator MARK BISHOP—The *Australian* reported on 25 May that Defence's preferred option was to continue with the Seasprite project. Is that correct?

Cdre Campbell—I think we have said enough about that already. Several options are being looked at, but we are continuing with the program at present.

Senator MARK BISHOP—I understand that you are continuing. We have had that discussion. Do you have a view on the three alternatives?

CHAIR—I do not think you can ask for an opinion.

Lt Gen. Hurley—No, we do not. As Dr Gumley has said, the contract is still active. The company still has to deliver against it. We need to see what they will be saying about their ability to deliver against the contract and the level of capability we will achieve. In the meantime, we will go off and look at these other options, and we will come back and provide that advice to government.

Senator MARK BISHOP—Has a new time frame been given by Kaman aerospace for the first fully operational Seasprite?

Cdre Campbell—Not yet, no. They are still in shock as to what the Commonwealth's actions over the past few weeks are.

Senator MARK BISHOP—Are they? They are in negotiations with you?

Cdre Campbell—Yes.

Senator MARK BISHOP—What are they seeking in general terms?

Dr Gumley—They are seeking for us to pay for the remediation from here on in.

Senator MARK BISHOP—Deriving from the flight control system?

Dr Gumley—Yes.

Senator MARK BISHOP—Had they costed that?

Dr Gumley—We do not have a cost yet from them, do we?

Cdre Campbell—Not yet, no.

Senator MARK BISHOP—Are they talking ballpark figures?

Cdre Campbell—Not yet, no.

Senator MARK BISHOP—They are just saying that they want the Commonwealth to pay for the remediation?

Cdre Campbell—Yes.

Senator MARK BISHOP—What is their argument for the Commonwealth paying for the remediation?

Cdre Campbell—They believe they had met the contract.

Senator MARK BISHOP—How did the coding system and the card go bad if they had met the contract specification?

Cdre Campbell—They have done extensive work with their subcontractor. Their subcontractor has worked the last two weekends on it. They are just about to deliver a report to us to basically say: 'This is what happened. We believe that fixes the problem that the Commonwealth has and we believe we have met the contract. We should move on.' The Commonwealth has a separate view.

Senator MARK BISHOP—I understand. So in the event that work continues, you cannot yet give me an indicative price of the remediation work?

Cdre Campbell—Not yet.

Senator HOGG—Are there any air crews that have been trained on the likelihood that these might fly?

Cdre Campbell—Yes, we have trained a couple of crews on the aircraft. They are obviously not all the way through their training but they have received initial training.

Senator HOGG—Now that these aircraft are grounded, what are these air crew doing to maintain their flying hours and also to upgrade their experience levels?

Cdre Campbell—I think Chief of Navy might like to answer that question, but I will start by saying that Navy has developed a plan to wind down operations at 805 Squadron while we work this problem.

Senator HOGG—Wind down? All right.

Vice Adm. Shalders—805 Squadron has been stood up for some years and has been flying the aircraft in squadron service, mostly in a training role. Since the aircraft was grounded on 29 March we have had a look at the manning status of the squadron. We have a reduction plan in train at the moment to wind the squadron back from around 90 people to what we think will be a base level of about 40 people while this problem is resolved. Those 40 will be largely maintainers rather than air crew.

Senator HOGG—I was coming to those in a moment. My recollection from I do not know how many estimates ago now is that the first thing you had were the maintainers to start the squadron off, if that is correct. The planes were not ready and I think it was part of the preparatory stage. What are those maintainers doing, given that I do not think any of the aircraft have been formally handed over?

Vice Adm. Shalders—The maintainers have been maintaining the aircraft. We have been flying them in squadron service. With the aircraft in the state they are in at the moment the maintainers will continue to maintain the aircraft. They cannot just be left to sit there. There will be ongoing maintenance required whilst these other problems are resolved; hence, we will leave about 40 doing that task. The others—

Senator HOGG—What will happen to them? Are they mainly pilots?

Vice Adm. Shalders—No, they are mainly maintainers.

Senator HOGG—They are the other 50?

Vice Adm. Shalders—Yes. Those people will be posted to other squadrons where we do have some shortfalls and we will requalify them from whence they came, if I can put it that way. For example, if they were in 817 Squadron looking after Sea Kings before they transferred to this squadron, we will requalify them on Sea Kings and use them in that fashion until we can ramp the squadron up again.

Senator MARK BISHOP—I would like to go back to this whole review process. What I understand, from what you have told us tonight, is that up until March the advice that Air Vice Marshal Rossiter provided us in February stood. But a problem was identified in late March.

Mr Smith—On 14 March there was an incident.

Senator MARK BISHOP—That caused Dr Gumley and relevant heads to become involved. A decision was made on safety grounds to ground the craft. A review was done by

various senior people and a report was made to the minister. We have paid 95 per cent of the contract price, we are of the view that the contract adequately covers the problem that has emerged and it is the prime contractor's responsibility to fix, yet the minister is determined to have a review that considers going on with the current Seasprites or looking at two off-the-shelf alternatives. There is a whole range of implications with that. Why are we having this review? Would you just explain that to me?

Gen. Hurley—Because if we get to the point where Kaman cannot convince us that they can deliver a helicopter that is safe to fly and can perform at the level of capability that we require, we may make a decision that we do not want that helicopter.

Senator MARK BISHOP—That is a similar-facts situation to the problem we had with the subs some time ago, when there were critical problems with certain aspects. We got access to alternative technology from the Americans which fixed the problem, with additional product, and we now have some very capable submarines. What I am hearing you say is that, having spent the best part of \$1 billion on state-of-the-art platforms for Navy because a problem with the flight control system has emerged, we should junk the whole goddamned lot. I do not understand how that decision can be considered at this late stage. What is driving this?

Cdre Campbell—There are other concerns that we have that we are addressing and believe can be addressed. As to whether they can be addressed inside the current contract and inside a reasonable time frame, we are still working on that. This automatic flight control system issue is the one which is obviously of most concern to us though.

Senator MARK BISHOP—It is legitimately of concern. We have heard from Dr Gumley that, in the worst case, it might take up to 12 months to fix. He is not saying it cannot be fixed; he is just saying it is going to take a lot of time to fix.

Dr Gumley—The flight control system is one of a number of things we have got to do to bring the helicopter up to full specification.

CHAIR—What are the others?

Cdre Campbell—There are some other issues that impact on the automatic flight control system. You might recall that the problem that this contract has had for several years has been software development. Software testing started today, which is great, and we look like having a very good mission system. I think you heard earlier tonight that part of project management is to study Pessimism 101. I have done 101, 102 and 103 and I am just not sure that this amount of software is going to work as well as we would all like it to.

CHAIR—So there is a confidence element starting to come through in this project?

Cdre Campbell—It is about the level of risk, I think. The level of risk is moderate at present that we are not going to get to deliver all of Navy's requirements.

Dr Gumley—So the 12-month figure is to fix the immediate trigger of this incident.

Senator MARK BISHOP—This is the trigger that caused you to ground them?

Dr Gumley—Yes. There are likely to be other issues related to the software that are going to take extra time as well. That is what we are also trying to work out at the moment.

Cdre Campbell—Until this testing is done, we are not going to know.

Senator MARK BISHOP—Right.

CHAIR—In other words, this is a typical project where very many lines of code and the developmental stage are causing us to bog down in this phase.

Cdre Campbell—We have hundreds of thousands of lines of code—

CHAIR—This is about number four or five on the list of most complex projects. Is that about right?

Cdre Campbell—It is very complex.

Senator MARK BISHOP—If we decide to junk the sprites, we have lost \$1 billion, we have lost x number of years and we have not got the capability. How long is it going to take to get the capability in place if we go down the path of one of the other two platforms?

Lt Gen. Hurley—That is exactly why we are going to speak to the companies to try to determine the answers to those questions. They are very relevant questions. We will be bringing that back to say: if we decide not to continue with the Seasprites, here are the options. This is the time frame to get this capability into play, this is the level of capability you will take on and, depending on whether you go the European way or the American way, there are technical risks going either way that you take on as well.

Senator MARK BISHOP—Yes.

Lt Gen. Hurley—We will be cautious and sceptical about what we are told.

Senator MARK BISHOP—I bet you will. If you have to junk the sprites, you will have to go down the path of one of these other two alternatives. What do we do in terms of capability until one of the two alternatives is purchased and put into Navy?

Vice Adm. Shalders—We will manage with what we have right now. That is a point. That puts a lot of pressure on our existing assets to get the number of air frames we need to sea.

Senator MARK BISHOP—There is an additional cost in maintaining them, as well, isn't there?

Vice Adm. Shalders—It is a loss of capability. We do not have the Seasprite capability at the moment, of course. It is a capability we do not have but the fact that we do not have the air frames means that we are putting more pressure on the air frames that we do have.

Senator HOGG—But it does not deliver the capability that you had hoped to deliver. That is the real problem.

Vice Adm. Shalders—Yes. For example, we do not have the capability to fire the Penguin missile, which is something we would like.

CHAIR—But you have harpoons and evolved Seasparrows. The gap is not exactly a huge black hole.

Vice Adm. Shalders—Correct.

Mr Smith—We have done without it for quite a long time.

Senator MARK BISHOP—We were looking forward to having this new capability worth \$1 billion coming online sometime in the next two years, weren't we?

Vice Adm. Shalders—We all were.

CHAIR—We will adjourn until 9 am tomorrow morning, when we can continue this discussion.

Committee adjourned at 11.04 pm