

Photo opposite: publicity poster for the Chief Finance Officer Group's 'Business Rules' initiative. The initiative is designed to provide a uniform understanding of the business rules that apply to everyday financial, contracting and budgeting tasks and procedures. The business rules complement the relevant government or departmental policies and legislation.

# CHAPTER SIX

## Management Reforms and Efficiencies

During 2003-04, Defence implemented a number of new processes to improve the way we do business and continued to develop those efficiencies already in place. In this chapter we report on our progress.



The Government's Defence Procurement Review recommended that the Defence Materiel Organisation become a prescribed agency for financial management purposes while still remaining part of the Defence Portfolio. This will be implemented on 1 July 2005

Another recommendation of the procurement review was the formation of the Capability Development Group to provide more robust capability proposals for consideration by the Government

A new portfolio-wide budgeting system was implemented in Defence

Defence achieved annual recurring administrative savings of over \$60 million against a target of \$50 million

A new travel management system was introduced, which is estimated to provide savings of up to \$21 million per year

## Progress on Financial Management Reform

Defence recognises that it must constantly seek to achieve best practice to ensure it is recognised by the Government and stakeholders as a respected financial manager. Defence is committed to addressing deficiencies and pursuing new opportunities in a more structured and coordinated way by implementing continuous improvement through financial transformation. Financial transformation will not only remediate business process deficiencies, but embed and sustain systemic reform to support more effective planning, management and reporting of Defence finances. Notable achievements in 2003-04 included:

- the full implementation of the Government's budget estimates framework for Defence budgeting and reporting requirements;
- the full implementation of a portfolio-wide budgeting system to meet reporting for internal or external use at the outcome, output and Group level;
- development, approval and release of a ten-year view of the Defence budget to Group Heads before the start of the 2004-05 financial year;
- the conduct of a rolling program of budget reviews, aimed at improving the overall quality and accuracy of Defence estimates and to eliminate large-scale unforecast variations;
- development and implementation of a force element and product cost capability complemented by improvements to the outcomes/outputs reporting framework;
- adaptation of the Defence business model to position Defence for the prescription of the Defence Materiel Organisation. A separate company code has been established to allow for separate reporting of all Defence Materiel Organisation financial transactions;
- substantial progress in reviewing and updating the Chief Executive Instructions and the Defence Accounting Manual. Solid progress was also made in improving the Defence delegations system and implementing a Regulation 10 reporting regime;
- improvements to the financial statements process and establishment of a Financial Statements Project Board;
- development of a financial systems strategy to progress the Resource and Output Management Accounting Network upgrade initiative and to provide a road map for ongoing improvements to Defence financial systems; and
- undertaking improvements in data quality, particularly debtor and cash management.

Further improvements to the budgetary process will focus on achieving a best practice budgeting system consistent with the Australian National Audit Office's guidelines.

Work to establish the Defence Materiel Organisation as a prescribed agency by 1 July 2005 provided a stimulus to accelerate change in financial management. A preliminary due diligence was completed to ensure all statutory requirements are met after the Defence Materiel Organisation separates from Defence. To complement this work, a new financial controls framework is to be implemented and remediation plans have been prepared to address major audit concerns. Work is also under way to introduce the new internal financial reporting framework.

Defence has worked to resolve a number of outstanding Australian National Audit Office findings. Under the direction of a newly formed project management board, an initiative titled Project Resolve has addressed audit issues and key aspects for the production of the 2003-04 financial statements. Defence acknowledges that more work remains to be done to address all outstanding issues.

A project to improve confidence in the accuracy of ADF leave records, has centred on the handling of leave applications by members and supervisors, systems changes to the Personnel Management Key Solution, remediation of records containing errors, and the introduction of Employee Self Service.

Work has been undertaken on Defence's key information systems platforms (the Resource and Output Management Accounting Network, the Personnel Management Key Solution and the Standard Defence Supply System) to advance interoperability, increase data quality, and enhance business processes. Defence has also completed a series of targeted programs that have upgraded existing enterprise resource platforms to better support Defence decision makers, as well as aiming to better meet the requirements of Government and other external stakeholders. Defence is now realising gains in areas such as data integrity, business efficiencies, and reporting accuracy. This work will continue in 2004-05.

Defence has also committed significant effort to improving the fundamentals supporting financial management such as data accuracy and business processes. In recognition of the central importance of data integrity, Defence continued a number of projects that examined and addressed shortcomings in information technology and business processes. The central role of training as the foundation for systemic change has also been recognised. A business skilling project was started in 2003-04 to identify Defence financial management proficiencies, leading to the development and presentation of targeted skills training across Defence.

## Defence Materiel Reform

The Defence Materiel Organisation supports the ADF by acquiring and sustaining leading edge military equipment.

The Senate Foreign Affairs, Defence and Trade References Committee tabled its report from the inquiry into materiel acquisition and management in Defence in March 2003. The Committee acknowledged the positive progress that had been made in the Defence Materiel Organisation reform program. The Government decided to implement a range of reforms to improve capability development and acquisition in Defence by further improvement of the capability definition process, providing the organisation with greater independence to better manage and deliver projects, and by progressing towards a more business-like approach in the organisation. These themes are consistent with the findings of the Senate Inquiry.

After the Government broadly accepted the findings of the Defence Procurement Review, the organisation's priorities were recast to reflect six key themes for materiel reform. Further detail on the themes is provided below.

### Defence Procurement Review

In September 2003, the Government announced that, as part of the ongoing reform of Defence procurement, it had agreed to broadly accept the recommendations of the Defence Procurement Review, led by Mr Malcolm Kinnaird. The review recommended the establishment of a new head of capability development at a senior level, strengthening the 'two pass' system for new acquisitions, establishing a high-level advisory board, considering the remuneration and tenure of project managers, and establishing the Defence Materiel Organisation as a prescribed agency. For more detail on the 'two pass' implementation process, refer to Chapter One – New Capability Development and Acquisition Process section.

Key to this reform was the appointment of a new Chief Executive Officer to the Defence Materiel Organisation to lead this reform program. Dr Stephen Gumley took up this appointment in February 2004.

The organisation is being assisted in its reform program by the Defence Procurement Advisory Board, established as a key recommendation of the Kinnaird review. The board comprises senior executives drawn from the public and private sectors, who bring with them a wealth of experience and knowledge. Chaired by Mr David Mortimer, the Board also includes Mr Malcolm Kinnaird, Dr John White and Mr Kevin McCann as the private sector members. General Peter Cosgrove (Chief of the Defence Force), Mr Richard Smith (Secretary of the Department of Defence), Dr Ian Watt (Secretary of the Department of Finance and Administration) and Dr Ken Henry (Secretary to the Treasury) are the public sector members of the board. The Board held its inaugural meeting in March 2004 and is now meeting monthly.

In June 2004, the Chief Executive Officer announced a reorganisation, consistent with adopting a more business-like approach as recommended by the Defence procurement review. The changes consolidated corporate planning and support in the organisation's headquarters, with the creation of new positions of Deputy Chief Executive Officer, Chief Operating Officer, General Counsel, New Ships – Amphibious and New Ships – Air Warfare Destroyer Divisions and a Director-General for Land Vehicle Systems.

## **Increased Professionalism**

In line with its aspiration to be the premier engineering and project management organisation in Australia, the Defence Materiel Organisation initiated a series of professional development and certification programs to improve recruitment, staff development and retention. The goal is to get the right people in the right positions at the right time. A professional certification framework for all program managers is being developed. The framework will be fully developed and implemented by the end of 2006.

In April 2004, a professional development program for engineers was implemented, and targets have been set for enrolment within the Engineers Australia professional development program. In March 2004, a survey of the qualifications of the organisation's workforce was undertaken, and targets have been established to improve the level of professional qualifications in other employment categories across the organisation.

The Project Manager's Development Program, a 12-month masters-level program run in conjunction with the University of South Australia, is in its sixth year with 15 staff participating in the current program. The program has seen 69 graduates awarded a Masters in Project Management over the past five years. The Quantum Program, a leadership development program for Executive Levels 1 and 2 and military equivalents in the Defence Materiel Organisation, continues into its third year with more than 164 staff participating in the program.

A new policy for the engagement of military personnel in the organisation was developed and will be implemented in 2004-05. This policy seeks to ensure that military staff have the necessary qualifications and tenure to meet the organisation's needs, while also meeting the ADF's needs for the development of its military personnel.

## **Standard Processes, Based on Business-Like Best Practice**

The Australian Defence contracting suite of tendering and contracting templates continued to mature, having adopted a more commercially-focused business philosophy. The organisation investigated further alternative contracting methodologies and, following a review of existing trial project alliancing contracts, removed the 'trial' status from that approach.

New principles underpinning the organisation's approach to contracting are being established. The basic philosophy of this approach is that industry has a right to a reasonable profit and some certainty of work, while Defence has a right to expect industry to deliver products on time, on budget and to the required capability. The Defence Materiel Organisation's performance in delivering major investment projects within budget and to the specified performance level has been steadily improving. A key goal of the organisation's Chief Executive Officer is to improve schedule performance, and this must include improved performance from industry. Underpinning this must be the development of a skilled workforce, in Defence and in industry, which can effectively deliver not only the current workload, but also the growth projected by the Government in the Defence Capability Plan.

As part of this reform program, ten materiel governance boards have been established to provide independent oversight and assurance of Defence's materiel projects. These boards review the technical, financial, contractual, risk and schedule performance of capital projects. The scope of the involvement of these governance boards in project assurance

was extended under the recent Kinnaird review to also consider the sustainment of ADF capability. The boards meet monthly and report regularly to the Chief Executive Officer.

During 2003-04, a new management information and reporting system, called the improve project scheduling and status reporting system, was introduced and has become the cornerstone of the standardised project reporting process. The organisation is also implementing a standardised project management methodology and tool-set across all projects. This process is supported by a corporate-level quality and environmental management system, which is being developed within the organisation to provide people with current information on policies, processes and practices.

A Project Risk Management Manual was released in June 2004 to provide direction on how risk is to be managed across the Defence capability life-cycle's 'needs', 'requirements', and 'acquisition' phases.

## **Improve Relationships With Industry**

In accordance with the Government's broad industry policy framework, Defence has developed a range of industry and procurement policies to support the delivery of ADF capability requirements and to facilitate greater alignment and partnership between Defence and industry. In February 2004, the Minister for Defence released the public version of the 2004-14 Defence Capability Plan. The plan provides industry with greater certainty about Defence's investment planning and had become Defence's key mechanism for informing industry of its major capital equipment investment intentions.

Following their endorsement by Government in June 2004, Defence is preparing an implementation schedule for the Electronic Systems and Aerospace Sector Plans, which will also include elements of the Naval Shipbuilding and Repair Sector Plan and, when completed, the Land and Weapons Sector Plans.

The seventh and eighth rounds of Company ScoreCards and the first formal round of 360-degree view ScoreCards were conducted in 2003-04. These ScoreCards enable the Defence Materiel Organisation and industry to discuss schedule, budget and project management performance in a constructive way.

## **Benchmark Against Both Public and Private Sector Organisations**

In 2004, the Defence Materiel Organisation initiated work to set productivity objectives consistent with industry benchmarks against both public and private sectors that also recognised the overheads associated with being a government agency. These benchmarks will be further developed in 2004-05 to gauge the organisation's project and platform management performance as well as its overheads.

## **Reprioritising Activity**

The Defence Materiel Organisation is clarifying its roles and responsibilities within Defence as a whole in order to reduce areas of overlap and free up resources to concentrate on high priority tasks.

Outsourcing of some activities will provide an opportunity for the organisation to reprioritise its activity. A major outsourcing contract for integrated storage and distribution was signed in December 2003 with Tenix Toll Defence Ltd. Contract

implementation commenced in March 2004 and is expected to be completed by December 2004.

## **Leading Reform in Defence**

The Defence Materiel Organisation has been at the forefront of Defence reform over recent years and, through its ongoing change program to achieve a more business-like focus, will continue to lead reform in Defence. In a number of areas, the success of reform in the Defence Materiel Organisation could create valuable precedents for change elsewhere in Defence.

## Corporate Services and Infrastructure Reforms

The Corporate Services and Infrastructure Group supports the working and living environments of Defence personnel.

### Results for 2003-04

Throughout 2003-04, the Corporate Services and Infrastructure Group continued to improve the quality of Defence's infrastructure and the services provided to its customers. It also continued to support Defence's reform agenda by focusing on delivering strategic objectives that provide assurance to its owner, customers and stakeholders. The strategic objectives for 2003-04 were to ensure that:

- customers were confident about the Group's products, service, performance and cost;
- customers understood what the Group provided and could easily access its services;
- the Group was recognised as a high-performing organisation that delivered best value-for-money and achieved planned performance; and
- the Group delivered sound stewardship of its resources in order to contribute to the sustainable delivery of Defence outcomes.

Results of the reform initiatives during 2003-04 are detailed below.

### Management of Defence Infrastructure

Infrastructure Division, within Corporate Services and Infrastructure Group, developed a new infrastructure asset development process which has been endorsed by the Government. The new process provides improved risk management measures and ensures the development of more robust cost estimates prior to bringing infrastructure proposals forward for departmental and Government approval.

This model has also been adapted for facilities operations and leasing proposals. The asset development model process is linked to broader Defence capability strategic planning by regular reports on the status of the overall infrastructure program to the Defence Capability Committee.

The development and implementation of the infrastructure asset development model has also enhanced the capital facilities planning process by addressing 'whole-of-life' costs, including operating costs and ecologically sustainable development aspects.

A new suite of construction contracts has also been developed and implemented. These contracts address whole-of-life aspects of design, construction and the ongoing operation and maintenance of facilities and infrastructure.

### Business Improvement

The Group focused on the implementation of a range of improvement activities designed to increase customer satisfaction and improve value for money in the provision of corporate services to Defence.

These improvement activities include:

- a new travel management system for business travel, including a new Defence travel card that will simplify travel arrangements, ensure prompt payments to suppliers and provide estimated savings of up to \$21m per annum;
- centralising arrangements for the payment of accounts through the purchase of data imaging and optical character recognition technology, which reduces the number of staff required to process these payments; and
- feasibility studies into management arrangements for ADF relocations, office requisites, administrative vehicles, hospitality and catering, logistics, occupational health and safety and corporate governance. These reviews will be completed in 2004-05.

The Group also implemented a new acquisition strategy for the provision of garrison support and facilities maintenance at Defence bases. The new contracts will have a strong emphasis on the provision of services by local industry providers. The first of the new contracts was signed for South Queensland in June 2004 and redirects an estimated \$17m per annum back into local businesses in South Queensland.

## **Information Systems**

Defence's information and communication technology capabilities have been restructured. By improving reliability, encouraging innovation and emphasising sound business principles, the Group has been able to meet current customer requirements while improving the effectiveness, and reducing the cost, of information and communication services.

A tender was released in November 2003 for the operation of a significant portion of Defence's information technology capability. This market-testing activity will ensure that Defence is obtaining value-for-money services. The selected service provider will be expected to assume responsibility for the designated portion of Defence's information technology capability during 2004-05.

As part of the upgrading of Defence computer systems throughout 2002-03 and 2003-04, over 40,000 redundant desktop computers were donated to the Australian Government's Computer Technologies for Schools Project. Defence also donated 80 surplus computers to the University of East Timor.

## **Industry Engagement**

A large proportion of the products and services for which the Corporate Services and Infrastructure Group is responsible are delivered by industry, with \$1.98 billion under contract in 2003-04. These contracts include the delivery of products and services in the areas shown in Table 6.1.

**Table 6.1 Expenditure on Corporate Services and Infrastructure Group-managed Contracts**

Service	Budget Estimate	Revised Estimate	Value
	\$m	\$m	\$m
Infrastructure investment <sup>(1)</sup>	376	382	364
Information technology and telecommunication services and products	352	320	347
Garrison support	335	345	346
Housing services	311	315	311
Facilities operations	233	278	260
Travel services	166	166	151
Property services	129	116	109
Utilities	95	93	93
<b>Total</b>	<b>1,997</b>	<b>2,015</b>	<b>1,981</b>

**Note**

1. Infrastructure investment contains the cost of training range upgrades, although it was reported separately in the 2003-04 budget and additional estimates statements.

## Commercial Support Program

The Commercial Support Program is Defence's primary mechanism for undertaking competitive tendering and contracting. The program, which began in 1991, aims to ensure that support services are provided to Defence in the most cost-effective manner. Services are contracted out when it is operationally feasible, a viable market exists and industry can demonstrate better value for money.

The *Defence Employees Certified Agreement 2004-2006* facilitates the application of the Commercial Support Program in Defence. The agreement covers all market testing and any other competitive tendering or equivalent processes that may result in the contracting out of a Defence civilian activity.

The Defence Integrated Distribution System market-testing activity was finalised during 2003-04 with the signing of a contract between Defence and TenixToll Defence Logistics on 18 December 2003. Requests for tender closed on 30 March 2004 for the Information Technology Infrastructure Support Services – Central Office market-testing activity. Evaluations are proceeding and an announcement is expected during 2004-05.

<b>Table 6.2 Commercial Support Program Progress Summary as at 30 June 2004</b>		
<b>CSP evaluation decisions made</b>	121	
Commercial contracts	80	(66%)
In-house options	32	(27%)
Status-quo retained	9	(7%)
<b>Number of positions tested <sup>(1)</sup></b>	15,935	
<b>Indicative total value of commercial contracts and in-house options <sup>(1) (2)</sup></b>	\$5,935.4m	

#### Notes

1. Values and positions tested are based on information provided at the time of decision announcement.
2. Indicative total value of contracts covers the full term of the contracts.

<b>Table 6.3 Activities in Progress or Under Consideration</b>	
<b>Activity Name</b>	<b>Status</b>
Information technology infrastructure support services	Request for tenders closed 30 March 2004. The evaluation is proceeding.
ADF rotary wing flying training – Army	Project scope under assessment.
Routine pathology services	Appropriate service delivery method to be determined.
Regional information communication technology market testing	Scope being finalised.
Personnel Services	Being rationalised and restructured under the Business Improvement Project.
Navy technical training services	Project scope is under assessment and business case is being finalised.

**Table 6.4** Activities Not Proceeding Under the Commercial Support Program

Activity Name	Reason
ADF rotary wing flying training – Navy	This activity has evolved into the Maritime Interim Rotary Training and Support System project. An operating lease is being sought to maintain relevant capabilities until definitive replacements are provided under later phases.
ADF Health Services – All regions	The preferred contractor for Victoria withdrew from negotiations. The Australian Capital Territory and southern New South Wales tender evaluation did not recommend a single tenderer. The lack of success with these two activities has led to alternative options being considered for all regional ADF Health Services activities. Future projects are likely to focus on specific bases and/or specialised health services.
Adelaide-class guided missile frigates and Anzac-class ships	Aggregation of existing contracts.

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