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The Benefits of Long Term Partnering in the Australian Defence Environment: A Strategy for Enduring Relationships and Mutual Benefit

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Abstract

This paper makes a case for long term partnering, or 'partnering for the future', between the Department of Defence and the Australian defence industry. While the paper takes into account the potential risks that are inherent in longer term contracts, it argues that, in both theory and practice, there are numerous mutual benefits to be gleaned from taking a much longer term approach to defence contracting.

This paper is 20 pages long.

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Introduction

This paper explores the concept of long term partnering, or contracting for the future,¹ between the Australian defence industry and the Australian Department of Defence. For the purposes of this paper, long term refers to contracts that have at least 5-10 year initial durations, and potentially the same length extensions. Partnering does not necessarily involve long term contracts in every case. Therefore this paper uses the term 'long term partnering' with the specific meaning of being contracts being 5-10 years.

There are many potential benefits in long term partnering that are not seen in more traditional forms of contracting. In Australia, specifically within the defence environment, long term partnering is applied sparingly. Long term partnering is definitely not applicable in every circumstance. However the benefits of such partnering should be examined to see how it could be applied more often. Indeed, '[p]artnering is not a quick-fix remedy. The very foundation for partnering – a long-term relationship – necessitates trust, good planning, patience, and persistence.'²

Admittedly, the prospect of being locked into a long term partnership seems like a huge risk both for the supplier and customer. Common concerns are that the supplier could encounter a situation whereby delivery against commitment, for any number of reasons, could be compromised and thus lock them into a long term loss-making contract. The customer may be faced with a poor performing supplier who cannot deliver, and yet is still legally obliged to continue with the arrangement. Both could have requirements that may change, or the customer may decide the capability is no longer required. A short term contract for two years followed by annual extensions (for example) looks much less risky for all concerned. Yet to leave only one option open over such an extended period of time is not such a sensible idea either. The need to conform to the Department of Defence's desire to 'maintain a competitive environment and so get value for money'³ needs a broadminded approach to be successful.

These are among some of the arguments faced by those who are proponents of partnering. Admittedly, if a partnership is not clearly thought out, the possible scenarios mentioned above may well cause future regret. However, if a partnership is built on solid foundations, a long term agreement can deliver outstanding results in terms of value (long term savings) and quality (continuous improvements through the life of the contract). In an environment where there is a requirement for Defence to save over \$20 billion over ten years

¹ Scott T Baker, 'Partnering: Contracting for the Future', *Cost Engineering*, Vol. 32, No. 4, 1990, p. 7.

² Baker, 'Partnering', p.8.

³ Department of Defence, *Building Defence Capability: A Policy For A Smarter And More Agile Defence Industry Base*, Australian Government, Canberra, 2010, paragraph 2.33, p. 26.

as part of its Strategic Reform Program (SRP),⁴ any suggestions which generate significant savings as well as delivering quality outcomes, should be taken into account.

This paper explores the main arguments both for, and against, long term partnering. It considers the components of long term partnering, such as trust and incentives, and draw on examples from overseas. In particular, since the 1998 United Kingdom Strategic Defence Review, the UK government reversed its competition policy and now seeks to improve defence procurement relationships with industry through partnering which has shown, and continues to show, favourable results.⁵ Australia is in the initial stages of implementing its own review, the Strategic Reform Program, and if genuine savings are to be realised, such lessons from the UK may well be worth noting.

The paper will therefore assess some of the major benefits of a partnering relationship between the Australian Government and Australian defence industry. It will conclude with an overall position on whether partnering can be used more frequently in the context of Australian defence procurement.

Long Term Partnering, Personal Relationships and Trust

Partnering relies heavily on strong personal relationships and mutual trust. As Baker notes, '[t]he primary thrust behind partnering is the improvement in quality in our production of goods and services. Any mechanism that promotes trust and encourages communication over the long term will help create an environment for quality improvement.'⁶ More recently, and in direct reference to the Australian Defence Force (ADF), Robert Wylie states that the 'ADF's structural dependence on industry will increase'.⁷ The point for this paper is that, if indeed the government's dependence on industry increases, then long lasting relationships between government and industry must be pursued at every opportunity, and pursued for mutual benefit.

Long term partnering is essentially about a long term commitment between parties based on mutual trust to achieve common objectives. Many definitions exist. One business dictionary definition states that partnering is:

⁴ Department of Defence, 'The Strategic Reform Program 2009: Delivering Force 2030', Australian Government, Canberra, 2009, p. 3.

⁵ Andrew S Humphries and Richard Wilding, 'Partnerships in UK Defense Procurement', *International Journal of Logistics Management*, Vol. 12, No. 1, 2001, p.83.

⁶ Baker, 'Partnering', p.8.

⁷ Robert Wylie, 'Defence Industry Policy 2010: The Combet Iteration', *Security Challenges*, Vol. 6, No.3, Spring 2010, p. 60. Wylie argues there are two factors that make this so, the first being the difficulty for the ADF to attract and keep appropriate in-house personnel, the second is privatisation and contracting out.

Establishing a long term win-win relationship based on mutual trust and teamwork and on sharing of both risks and rewards...The objective is to focus on what each party does best, by sharing financial and other resources, and establishing specific roles for each participant.⁸

Even so, it can be a difficult concept to understand and implement.

While this paper finds partnering favourable, it is not necessarily universally applicable. It can be seen as new, and thus untried, and thus risky and dangerous in some quarters. It is risky because of the long term commitment required and the perception of being locked into an agreement over an extended period, and dangerous because of the extra effort required to ensure all necessary mechanisms (such as benefits, pain/gain share models and incentives are in place to drive the required behaviours.

Benefits

In order to explore the proposition of partnering over the long term, it is important that some of the benefits and implications of such arrangements are understood. Some, but certainly not all, of the benefits for both parties include:

- Improving the ability to innovate up front and extending the ability to continuously improve;
- Motivating industry to invest funds up front in facilities, assets and people, given the longer period of assured payback;
- Assuring delivery of capability over a longer term with budget certainty;
- Being more conducive to long term, enduring relationship building;
- Delivering long term customer, contractor and supply chain efficiencies;
- Allowing time to develop robust Key Performance Indicators and also to build in gain share / pain share mechanisms;
- Focussing on improving quality and thus on capability, (rather than just pure marketing and tender costs, for example); and
- Long term resource planning.

In order for long term partnering to succeed, it is essential that a long enough timeframe is allocated to enable enduring relationships to be built with all parties concerned. Building long term enduring relationships with both the customer (in this instance, Defence), and the supply chain, requires a long term commitment. This is compared to more traditional short term agreements where there could be seen to be little benefit in building a relationship as the process of winning, completing the job and walking away is comparatively

⁸ 'Partnering', The Business Dictionary, available at <http://www.businessdictionary.com/definition/partnering.html>, accessed 28 October 2010.

expeditious. Essentially, '[t]he value of a good relationship with your suppliers cannot be under estimated and most businesses work hard to ensure that they are truly effective from the outset.'⁹

Building Enduring Relationships

With a long term partnership in place, both parties allow themselves the time required to build a relationship. This will in turn encourage trust to develop between the parties. Each participant will have the incentive to build a workable relationship as they work together over a prolonged period of time towards a common outcome. Long term partnerships are of course not the only mechanism to drive effective relationship building. Customers and suppliers may necessarily have different arrangements in place such as a delivery with short timescales and this require shorter term agreements. This does not necessarily stop relationship building. However, these relationships are usually built over a prolonged period involving repeat business arrangements. The point here is to illustrate that long term partnering fosters relationship building. While both parties may not necessarily have a common goal, as the relationship matures, each can try to understand the other's goals and so help each other to deliver them. These enduring relationships should enable all parties to build trust over the long-term.

In 'Partnerships in UK Defense Procurement', the shift in relationships from a traditional contracting methodology to a partnering approach is identified as having the following components.

From traditional contracting typified by:

1. Suspicion and mistrust; each party wary of the other party's motives;
2. Each party geared to what is best for them;
3. Communication being structured and guarded;
4. Single project focus;
5. [Personal] Objectivity limited due to fear of reprisal;
6. Mistakes resulting in retribution;
7. Limited organizational access; structured procedures, self-preservation rather than performance optimization;
8. Involvement being limited to project personnel;
9. Blame and buck passing; and
10. Arm's-length, or at worst, an adversarial relationship.

⁹ Mike Robinson, 'So...You Think You Have Partnering Sorted?', *The British Journal of Administrative Management*, August/September 2005, p.18.

To partnering typified by:

1. Mutual trust forming the basis of a strong working relationship;
2. Shared goals and common objectives ensuring common direction;
3. Open communication avoiding misdirection and bolstering effective working relationships;
4. Long-term commitment providing the opportunity for continuous improvement;
5. Objective critiques geared to candid performance testing;
6. Creating an atmosphere where both parties initiate ideas and changes;
7. Organizational access and sharing resources;
8. Total involvement at all levels;
9. Team problem solving; and
10. Nurturing the relationship.¹⁰

This transformation from traditional behaviours to partnering behaviours identifies that moving from single project contracting to a long term partnership is one element of relationship building. The transformation also builds on the themes of trust and continuous improvement, all of which are surely desirable traits in all working relationships.

Without trust, it is apparent that time and time again when a contentious issue arises, parties turn to contractual documents and point the finger at each other instead of having forward-looking open conversations. Setbacks will arise in a complex project environment despite everyone's best efforts, but how they are dealt with largely depends on the nature and maturity of the relationship. A longer term relationship built on partnering behaviours is far more mature and trusting than a relationship built on more traditional, short-term, contracting behaviours.

As noted by Philip Copare:

In a partnering relationship, the parties seek to transform what is traditionally an adversarial relationship between the owner and contractor to a more collaborative and productive relationship.¹¹

¹⁰ Taken from Andrew S Humphries and Richard Wilding, 'Partnerships in UK Defense Procurement', *International Journal of Logistics Management*, Vol. 12, No. 1, 2001, Figure 6, p. 90.

¹¹ Philip B Copare, 'Partnering – A New Philosophy in Business', *Transactions of AACE International*, 1994, p. HF3.1.

The Australian Defence Context

The need for a mature and trusting relationship between the Department of Defence and industry is recognised by Australia's 2010 publication *Building Defence Capability*. This builds on previous policies. Notably in 2003, on the topic of stronger defence and industry relationships, Fran Bailey, then Parliamentary Secretary to the Minister for Defence, in an opening address to the 2003 Defence and Industry Study Course, said '[t]he Government has therefore implemented a more strategic approach to defence industry policy. This approach aims to foster long-term partnerships with industry as opposed to the project-by-project approach'.¹² Seven years later in the 2010 Industry Policy, it can be seen again that one of the four key elements emphasised is relationships:

The second element is a commitment to establish a stronger relationship between Defence and industry. The implementation of the Defence White Paper 2009, the achievement of Force 2030, and the successful completion of the Strategic Reform Program, will all require a strong relationship built upon more flexible approaches to defence procurement and contracting, where varying kinds and levels of risk are managed through the appropriate procurement and contractual vehicles. This has long been a key interest within industry.¹³

However, the message from Defence is not consistent. In the Defence Materiel Organisation (DMO) paper 'Incentive Contracting in Defence Procurement',¹⁴ there is no mention of the need to build long lasting mature relationships. The paper does not specifically set out to explain all aspects of contracting. It does however identify an alternative approach; Incentive Contracting. Incentives are indeed a key element of long term contracts, but a key omission in the DMO paper is the length of the contract award. Long term contracts are not the only way to build relationships, but they are one key way relationship building can be achieved. Industry therefore receives mixed and confusing messages where Defence policy states that relationships are important, but a DMO paper does not even mention the word 'relationships'.

Doing business in a long term partnering arrangement also provides industry with the assurance it needs in order to maintain a healthy, profitable business. This is because the longer period provides greater assurance in terms of revenue streams. In the UK, one of the six guiding principles of the 2005 UK Defence Industrial Strategy (DIS) was to look at long term arrangements. Keith Hartley notes that '[t]his new paradigm offers industry longer, more assured revenue streams based on long-term support and continued development

¹² Fran Bailey, 'Opening Address to the 2003 Defence and Industry Study Course', Puckapunyal Army Base, 31 March 2003, p. 3.

¹³ Department Of Defence, *Building Defence Capability*, p. 7.

¹⁴ Defence Materiel Organisation, 'Incentive Contracting in Defence Procurement: An Updated Approach Incorporating Performance-Based Measures', Discussion Paper, Australian Government, Canberra, 2009, paragraphs 33-38, pp. 8-9.

rather than a series of 'must win' procurements.'¹⁵ The US Government Accountability Office also noted that the 2005 DIS found that industry preferred long-term contracts.¹⁶ The 2005 DIS stated that companies are generally interested in using availability contracts (a form of long term contracting employed by the UK Ministry of Defence) not least because it provides commercial firms with 'greater returns over a longer period.'¹⁷ This is good news for industry because industry prefers to look at long term partnering wherever possible. These returns are coupled with the ability to generate long term savings in the support chain because the focus is on the availability of the platform.

The ability to have a long term plan for future capacity and resource issues is greatly enhanced by the stability provided by a long term contract. This is true for all parties involved on all sides of the supply chain. For industry, the benefit is that all parties involved are guaranteed to have a stable future capacity with respect to resource planning. For the government, the advantage is a stable, financially healthy industry able to deliver to the government's evolving requirements.

Long term partnerships also allow greater assurance in respect to delivery. With a long term contract or partnering arrangement, the budget for the outer years of a program is identified in the early stages. This gives the customer and contractor visibility of the funding required in the later years of a long term project. This frees up the contractor to concentrate on delivery of the required service or capability over a longer timeframe concentrating on capability quality and improvements in process, rather than purely focussing on the financial aspects. Essentially, it gives all concerned greater assurance of delivery over a longer term within a known budget. Contrast this with a short term contract with extensions; the funding in the outer years is unknown and can cause uncertainty.

Uncertainty should not be confused with risk, however; risks can be identified and managed and there are many risk management tools and processes in existence. Uncertainty in this context is about the inability to plan resources and budgets in the outer years of a contract.

¹⁵ Keith Hartley, 'The Economics of the UK Defence Industrial Strategy', *Security Challenges* Vol.3, No. 2, June 2007, p.23.

¹⁶ United States Government Accountability Office, *Defense Logistics Improved Analysis and Cost Data Needed to Evaluate the Cost-Effectiveness of Performance Based Logistics*, GAO-09-41, Report to the Subcommittee on Readiness, Committee on Armed Services, House of Representatives, December 2008, p.49.

¹⁷ Ministry of Defence, *Defence Industrial Strategy: Defence White Paper*, London, The Stationery Office, 2005, p. 64.

Improved Efficiencies

This paper has identified that improvements achievable over a longer period of time can deliver longer-term efficiencies to the customer, contractor and supply chain. This can be through the natural learning curve of knowledge being built over a prolonged period allowing for improvement, and/or the batching of procurements such as buying material in bulk. Both approaches force parties to think about savings and efficiencies over a longer period of time and not necessarily in the short term. In some instances there may be short term inefficiencies which may need to be accepted provided there is assurance of future improvements. In short, '[a]ccept short-term failings, provided there's long-term improvement for both parties'.¹⁸

Further, constructing a sensible incentive regime is critical in a long term partnering arrangement. Getting the performance measures (which will drive the incentives) correctly identified is vital to ensure that all parties are focussed on ongoing improvements and efficiencies. Typically, the incentives will be around performance based measures such as the percentage of time a platform is available for operations or the amount of time a particular system is operational. This involves identifying some objective parameters against which a company's performance can be assessed.

As noted above, the Australian Department of Defence has recognised the importance of incentive contracting and has stated some potential benefits. The DMO discussion paper of 2009 states:

Under an incentive contracting regime, Defence could achieve better value for money from the expenditure it directs to maintaining and enhancing functionality and availability of military equipment. It could also enjoy lower contract prices.¹⁹

There is also recognition of the benefits to industry in terms of better performing contractors getting better profit margins. The same paper states that 'Defence's better performing suppliers could benefit through higher rates of profitability as well as greater continuity of workload if a contract is accompanied by extensions to work based on so-called 'award terms'.'²⁰ While the recognition of incentives as a means for delivering value for all involved is understood by industry, the concept of extensions to increase the length of the contract does not provide the long term assurance required. Extensions to a contract are not recognised as part of the base award length – that is, the initial guaranteed period of the contract.

There is a perception that increased profit margins do not tally with the concept of savings. This is not necessarily the case. Reducing costs through improvements over a longer time period is one way industry is delivered

¹⁸ Mike Robinson, 'So... You Think You Have Partnering Sorted?', p.19.

¹⁹ Defence Materiel Organisation, 'Incentive Contracting in Defence Procurement', 2009, p. 2.

²⁰ Defence Materiel Organisation, 'Incentive Contracting in Defence Procurement', p. 2.

higher profit margins. Only the high performing companies will benefit from higher profits as the incentives in the contract are linked to performance, which in turn is linked to a more efficient delivery of a product or service. More efficient delivery means less is spent in the long run for that particular service. This reinforces the point that performance measures must be correctly identified from the onset.

Pain share / gain share are also mechanisms which play a part in long term contracting agreements. In broad terms, this kind of arrangement asks for contractor and customer to share losses if an overrun occurs - that is if spending is more than was planned - and allows parties to share the gains if a cost underrun occurs, that is if spending less than was planned. Industry therefore has an incentive to improve its efficiency which in turn will allow its profit to increase. The scope of these pains and gains is limited, as noted in the DMO discussion paper 2009; 'In practice, most incentive contracts place clear limits on the exposure of both industry and Government to risk arising from cost uncertainty by establishing price 'floors' and 'ceilings'.'²¹

Competition

Ultimately, a key element of the government's approach to dealing with industry is securing value for money, and one way of engendering this is competition.²² This is fair enough, because competition provides considerable benefits to the customer. The buyer remains in control, it forces industry to remain competitive in its responses to tenders, provides the buyer with multiple solutions and designs and should deliver best value for money in terms of contractual adherence to cost, schedule and quality. These are not unreasonable expectations when engaged in major materiel and sustainment services procurement.

Contrary to popular perceptions, industry welcomes competition and would encourage it where it is appropriate, especially if it is coupled with a long term positive outcome. There are, however, instances when sole source procurement is the only option,²³ and the buyer would need to proceed on that basis. This is given recognition within the Australian Department of Defence, but it would appear that the preference is not to go down this route wherever possible. Defence prefers that direct sourcing, or sole sourcing, be conducted only under specific conditions prescribed under the mandatory procurement procedures.²⁴

²¹ Defence Materiel Organisation, 'Incentive Contracting in Defence Procurement', p. 4.

²² Department of Defence, *Building Defence Capability*, paragraph 2.33, p.26.

²³ Where issues such as intellectual property, critical capabilities and rapid acquisition are drivers or when there are no effective alternatives.

²⁴ Department of Defence, 'DMO Acquisition and Sustainment Manual', Australian Government, 2007, paragraph 5.87, p.118.

Assuming therefore that the Australian defence industry is, and will remain, a competitive environment, what does this mean for long term partnerships and contracting? Generally, competition should not be a barrier to entering into long term partnerships based on availability contracts or other incentives. A competitive environment should not necessarily exclude long term contracting and there is no reason why the outcome of a competitive tender should not be a long term award. Industry simply generally favours long term contracts on the grounds of certainty. According to the 2010 Defence Industry Policy, 'competition encourages innovation, helps drive productivity and promotes efficiency.'²⁵ However, the nature of the competitive environment can drive behaviours not conducive to partnering and this impact on behaviours must be taken into account.

One potential drawback of a competitive environment is that it can often lead to adversarial contract structures. End goals of both buyer and contractor are often misaligned. The focus for both is to minimise risk and cost and thus increase profit and speed up delivery, usually at the expense of quality outcomes. Yet quality outcomes are of mutual benefit to all parties. In order to drive positive behaviours required in a partnership, the competitive environment needs to take these possible negative impacts on behaviours into account wherever possible. A competitive procurement strategy accompanied with long term base awards need not be a barrier to partnering.

Innovation

Innovation is also a key component of successful contracting. It is not simply about new, untried, high risk, leading edge solutions. Innovation can be applied to the way things get done. Over a longer period of time, it could be possible to apply different techniques to achieve the same goals. In the defence industry this is particularly relevant considering how long some of the platforms remain in service. If Defence intends to use platforms for extended periods, a long term enduring partnership must be something it considers in order to ensure that innovation throughout the contract can develop and mature.

Innovative Solutions

In a partnership, allowing the contractor to propose innovative solutions to add value has its benefits. Such benefits could be in the form of alternative solutions which still meet the desired capability, or alternative technology-based solutions that the customer may not have thought of. Solutions and innovations over the long term can be quite different to those in the short term. A long term assurance would allow investment in facilities which can, in some cases, take years to establish. Often, if it is known that the outcome of a bid will result in a two year contract with potential extensions, the focus is on how to

²⁵ Department of Defence, *Building Defence Capability*, paragraph 2.33, p.26.

win that bid, and how to ensure returns will not be jeopardised. In such cases, there is little incentive for industry to be innovative because the focus is on the financials of the deal rather than the delivery of capability.

An example of such innovation is the Hercules Integrated Operational Support (HIOS) 20 year contract. The former head of the UK's Hercules Integrated Project Team commented:

When HIOS was signed Marshall Aerospace was able to very quickly build a large office block to house the company executive and the overseas development team, thus freeing up accommodation for other parts of the organisation. I believe that one of the advantages of a 25 year contract is that it allows industry to get funding from the banks against the 'collateral' of a long-term contract. This is one of the advantages the MOD expected from entering into long-term partnering arrangement with industry.²⁶

Innovative behaviours and practices will not necessarily just develop out of a long term contract. When the correct incentives are added into a long term partnership, it will drive innovative behaviours. The 2009 DMO paper states:

Innovative behaviour is also facilitated through incentive contracts tending to rely on extensive pre-contract negotiations to better understand where more effective and efficient approaches to the delivery of capability might be made.²⁷

Innovation also brings with it an element of risk. If innovation is to be fully encouraged, then certain levels of risk should be allowed to exist and they should be owned and managed accordingly. According to the Australian National Audit Office:

Risk management is a fundamental feature of the innovation process...Elimination of risk is generally not a practical goal but risk can be managed and mitigated by various treatments. Good risk management is therefore fundamental to innovation.²⁸

Incentives for Investment Decisions

The contractor's ability to invest funds up front in a partnership or contract is dependent on the length of the contract or agreement. That is to say that the investment return will be planned over the same period as the contract award length. Investment capacity in facilities, assets, people and so on, is greater if there is a longer period of assured payback. Any investment decisions made by industry can only be based on the certainty of work tenure; or the base contract.

²⁶ Mark Hobbs, Former Hercules Integrated Project Team (IPT) Leader, Royal Air Force, Personal Communication to the Author, 4 November 2010.

²⁷ Defence Materiel Organisation, 'Incentive Contracting in Defence Procurement' paragraph 20, p.6.

²⁸ 'Innovation in the Public Sector: Enabling Better Performance, Driving New Directions, Better Practice Guide', Australian National Audit Office, Canberra, December 2009, paragraph 1.6, p. 4.

This also applies to the broader supply chain. There is little incentive for industry to commit for the long term - and so invest in improvements that take a long time to implement - when the implementation time is not the same as, or greater, than the length of the contract.

If industry is to invest in improvements and efficiencies, it can only be against the guaranteed period of the contract. If a piece of equipment is expected to be supported for 10 years for example, but the initial contract is for three years plus annual extensions, industry would only consider investments against the initial three year period. This has been recognised: 'For industry to sustain key capabilities, especially those that are less relevant to the civil market, it needs an environment conducive to securing positive returns on its long-term investment.'²⁹

In the UK, the Ministry of Defence uses long term performance-based contracts to good effect. It is important to note that the base award terms are for much longer periods than generally seen in Australia. Examples of such contracts are:

- Sea King Support – 10 years with Augusta Westland;
- Ministry Survey Ship – 23 year contract with VT Group;
- Tornado - 19 year contract with BAE Systems; and
- Merlin Helicopter support – 25 year contract with Augusta Westland.

The Sea King contract is in place for the first five years followed by five year increments. The Survey ship contract had renegotiation points at seven, 15 and 20 year points. The Tornado contract is in place for the first 10 years. The Merlin contract is in place for the first five years and the next five year period is being negotiated. In all these examples, a long term partnering approach has been agreed and interestingly, none have annual extensions but long term extensions.

Further, the Ministry of Defence (MoD) agreement for fast jet support is a good case in point, achieving both savings and improved availability. According to the National Audit Report 'Over the period 2001-2 to 2006-7, the Department has achieved cumulative savings on the support of Tornado and Harrier aircraft of £1.3 billion and £109 million respectively'.³⁰ Availability of the aircraft to the UK MoD in the same period also increased compared to when no partnering arrangement was in place. This clearly shows some of the benefits of partnering. It has allowed the focus to be shifted to the availability of the aircraft to the Royal Air Force instead of focusing on spares and repairs alone, which is often what consumes the shorter term contracts. It generated significant savings by allowing long term improvements and efficiencies to be built into the contract. The long term stability also allowed the MoD to rationalise personnel and bases across the UK. In all, this long term contract

²⁹ Fran Bailey, 'Opening Address to the 2003 Defence and Industry Study Course', p.3.

³⁰ National Audit Report, 'Transforming Logistics Support for Fast Jets', 2007, p.6.

allowed the UK MoD and the industry that supports it, to build a lasting relationship for mutual reward.

The Hercules Integrated Operational Support (HIOS) contract is another example of a successful long term UK partnering agreement. HIOS is a 20 year contract designed to ensure aircraft availability and performance at optimum levels for the life of the contract while saving around £260 million over the same period.³¹ Such success allowed the contract to move into its second phase ahead of schedule, and thus generated further savings. Industry concluded that '[t]his is a reflection of the excellent relationships that have been established between the industry and MOD partners.'³²

However, simply having a long term contract is not enough on its own. In conjunction with a long term award, the UK experience has been one of ensuring appropriate incentives and open book accounting are included in the agreements to ensure the benefits are realised.³³ A US report by the Government Accountability Office (GAO), which compared the US and UK experience of Performance Based Logistics arrangements notes:

Defence Equipment and Support officials said that they have found the long-term nature of availability contracts a key factor in reducing costs and that annual contracts cannot achieve the same benefits as the longer-term contracts do. According to officials, the long-term contracts for Tornado aircraft and helicopter fleets reduced costs because the contractors were able to stabilize their supply chain and obtain better prices from the supplier base.³⁴

The US experience was different as the award terms were much shorter and there were no incentives built in for industry. As a result, they did not experience the improvements shown in the UK. The focus on ensuring platform availability was a driver for industry to improve support chain costs. Essentially, the less time the platform spent in maintenance, the longer it is available for use. The long term contract allowed industry to obtain better prices from the supply base as it could guarantee the supply base long term work.

³¹ 'Hercules Contract Will Benefit Front Line Ahead of Time', available at <http://webarchive.nationalarchives.gov.uk/+http://www.mod.uk/DefenceInternet/DefenceNews/EquipmentAndLogistics/HerculesContractWillBenefitFrontLineAheadOfTime.htm>, accessed 28 October 2010.

³² Hercules Contract Will Benefit Front Line Ahead of Time.

³³ United States Government Accountability Office, Defense Logistics Improved Analysis and Cost Data Needed to Evaluate the Cost-Effectiveness of Performance Based Logistics', GAO-09-41, Report to the Subcommittee on Readiness, Committee on Armed Services, House of Representatives, December 2008, pp. 47-51.

³⁴ United States Government Accountability Office, Defense Logistics Improved Analysis and Cost Data Needed to Evaluate the Cost-Effectiveness of Performance Based Logistics', GAO-09-41, Report to the Subcommittee on Readiness, Committee on Armed Services, House of Representatives, December 2008, p. 49.

Conclusion

The need to build stronger more lasting relationships between Defence and the Australian defence industry has long been recognised through progressive Defence industry policies. Long-term partnering fosters relationship building, allowing parties to develop trust and move from adversarial to cooperative behaviours. Long term partnering drives innovation, generates savings over the long term and allows all parties to concentrate on delivering capability more efficiently. Continuous improvements and product and service innovation are most beneficial over the longer term in a partnering environment.

Both the Australian Government and industry recognise the need for industry to invest in the long term future to sustain a viable vibrant industry, as identified as a key principle in the 2010 Defence Industry Policy. Investment in the long term can only be made if the government follows through and provides long term assurances. Implementing more long term partnering will help the Australian defence industry to invest in the long term. The Department of Defence benefits as it secures long term access to a healthy defence industry; and industry benefits as it is motivated to improve efficiencies, reduce costs, thus also lifting profit margins, whilst efficiently delivering capability to its prime customer; the Australian Defence Force.

The savings demanded by the SRP also mean that partnering should not be overlooked.

In sum, the Australian Department of Defence should seriously consider embracing the concept of long term partnering; where appropriate and mutually beneficial.



