



First Principles Review

CREATING ONE DEFENCE



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FOREWORD

I am pleased to present the Report of the First Principles Review Team.

In August 2014, the previous Minister for Defence appointed the team to undertake the First Principles Review of Defence. I was asked to chair the review team comprised of Professor Robert Hill, Professor Peter Leahy, Mr Jim McDowell and Mr Lindsay Tanner. The membership of the review team brought together a range of perspectives and a wealth of experience and expertise.

We were ably supported by Roxanne Kelley, Major General Paul Symon and their secretariat¹ as well as the Boston Consulting Group. The Secretary, Dennis Richardson and the Chief of the Defence Force, Mark Binskin are to be commended for their openness, professionalism and cooperation during the course of the review. I am extremely pleased that a quality outcome has been delivered in a tight timeframe.

We were tasked with ensuring that Defence is fit for purpose and is able to deliver against its strategy with the minimum resources necessary. Using a structured framework, we have conducted an end-to-end holistic review based on the outcomes required of Defence and founded on the first principles agreed by the review team. Simply put we sought to answer the question, what is the most effective and efficient organisation that will enable Defence to deliver the outcomes required of it?

Defence is an organisation with a long and deservedly proud history. Its evolutionary journey from separate single Service agencies into the Australian Defence Force and further into an increasingly integrated Defence Organisation commenced in the 1970s. This report, in our opinion, sets out the next phase of change for Defence.

Our work has been forward looking. We believe the review positions Defence to best meet the future demands on it. We present a sustainable and enduring business model, one that allows Defence to protect the nation and its interests whilst also delivering best public value.

The recommendations are not revelations and many carry a familiarity with those coming from previous reviews. However, our review and its supporting analysis have led us to recommend transformational change to an organisation which has drifted from contemporary best practice. In combination the recommendations will change the structure, governance arrangements, accountabilities, processes and systems of Defence. They are designed to operate as a whole and will need to be implemented as such in order to be most effective.

The combined effect is a more unified and integrated organisation that is more consistently linked to its strategy and clearly led by its centre. We have called this, the **One Defence** approach. It has four key features:

- A stronger and more strategic centre able to provide clear direction, contestability of decision-making, along with enhanced organisational control of resources and monitoring of organisational performance;
- An end-to-end approach for capability development with Capability Managers having clear authority and accountability as sponsors for the delivery of capability outcomes to time and budget, supported by an integrated capability delivery function and subject to stronger direction setting and contestability from the centre;

¹ Members of the Secretariat are listed at Annex H.

- Enablers that are integrated and customer-centric with greater use of cross-functional processes, particularly in regional locations; and
- A planned and professional workforce with a strong performance management culture at its core.

Effective implementation is essential to achieving the **One Defence** model and to generating the efficiencies the review has identified. A high level implementation plan has also been developed. Successful delivery of the review's intent will require a unified leadership team willing to drive change and a behavioural shift; a sense of urgency and a willingness to push the pace of change; and sufficient planning, oversight and commitment to delivering the full intent of recommendations. As the Secretary and the Chief of the Defence Force are recently appointed to their roles, this provides a good starting point for the implementation of our recommendations.

The **One Defence** transformation is an opportunity for Defence to establish better relationships with the Government, Ministers, external stakeholders, central agencies, its own leadership and workforce. It is an opportunity for Defence to reset its reputation and re-position itself as a truly integrated agency that consistently produces the best public value, and is able to meet the current and future demands on it. Most importantly, it will allow Defence to effectively deliver on its primary focus: to protect and advance Australia's strategic interests through the provision of appropriately prepared and equipped armed forces.



David Peever

Chair
First Principles Review of Defence

KEY RECOMMENDATIONS

This review of Defence from first principles has shown that a holistic, fully integrated **One Defence** system is essential if Defence is to deliver on its mission in the most effective and efficient way.

In order to create **One Defence** and give effect to our first principles, we recommend Defence:

1. Establish a strong, strategic centre to strengthen accountability and top level decision-making
2. Establish a single end-to-end capability development function within the Department to maximise the efficient, effective and professional delivery of military capability
3. Fully implement an enterprise approach to the delivery of corporate and military enabling services to maximise their effectiveness and efficiency
4. Ensure committed people with the right skills are in appropriate jobs to create the **One Defence** workforce
5. Manage staff resources to deliver optimal use of funds and maximise efficiencies
6. Commence implementation immediately with the changes required to deliver **One Defence** in place within two years

We have also outlined 70 specific recommendations which detail the actions required to deliver these key recommendations.

FIRST PRINCIPLES REVIEW RECOMMENDATIONS

1. ESTABLISH A STRONG STRATEGIC CENTRE TO STRENGTHEN ACCOUNTABILITY AND TOP LEVEL DECISION-MAKING	2. ESTABLISH A SINGLE END-TO-END CAPABILITY DEVELOPMENT FUNCTION WITHIN THE DEPARTMENT TO MAXIMISE THE EFFICIENT, EFFECTIVE AND PROFESSIONAL DELIVERY OF MILITARY CAPABILITY	3. FULLY IMPLEMENT AN ENTERPRISE APPROACH TO THE DELIVERY OF CORPORATE AND MILITARY ENABLING SERVICES TO MAXIMISE THEIR EFFECTIVENESS AND EFFICIENCY
<p>We recommend:</p> <div><div>1.1</div><div>this review be adopted as the road map for Defence reform for the next five years</div></div> <div><div>1.2</div><div>a new One Defence business model</div></div> <div><div>1.3</div><div>the diarchy is retained</div></div> <div><div>1.4</div><div>the individual and shared accountabilities of the Secretary and the Chief of the Defence Force be clarified, formally documented and promulgated through the organisation</div></div> <div><div>1.5</div><div>a streamlined top level management structure for the Department that is aligned with the One Defence business model</div></div> <div><div>1.6</div><div>the strategic centre include the Associate Secretary and Vice Chief of the Defence Force as the integrators for the Defence enterprise and the future force and joint capabilities respectively</div></div> <div><div>1.7</div><div>the Vice Chief of the Defence Force's decision rights be greatly strengthened, including the right to stop projects proceeding through the approval process until joint force integration is proven</div></div> <div><div>1.8</div><div>legislative changes to formally recognise the authority of the Chief of the Defence and the Vice Chief of the Defence Force, including removing the statutory authority of the Service Chiefs</div></div> <div><div>1.9</div><div>that policy advice be strengthened by bringing all policy functions into one organisational unit in order to improve the quality of advice provided to Government</div></div> <div><div>1.10</div><div>a strong and credible internal contestability function be built and led by the Deputy Secretary Policy and Intelligence with responsibility for strategic contestability, scope, technical and cost contestability</div></div> <div><div>1.11</div><div>that the policy and intelligence functions be combined under a Deputy Secretary Policy and Intelligence, who will have responsibility for providing policy advice and intelligence assessments to the Secretary and the Chief of the Defence Force</div></div> <div><div>1.12</div><div>the Defence Security Authority be repositioned under the Associate Secretary</div></div> <div><div>1.13</div><div>the Defence Committee be re-positioned as the primary decision making committee of Defence and the heart of the strategic centre with two supporting committees – Enterprise Business Committee and Investment Committee</div></div> <div><div>1.14</div><div>that all other enterprise-wide committees be reviewed for their relevance and alignment with the One Defence business model with the aim of a substantial reduction in the number of committees</div></div> <div><div>1.15</div><div>that the organisational structure reporting to the Vice Chief of the Defence Force be simplified through the incorporation of a two-star Head of Joint Enablers role</div></div> <div><div>1.16</div><div>a strengthened centre-led, enterprise-wide planning and performance monitoring process be adopted</div></div> <div><div>1.17</div><div>that the Associate Secretary be the central authority to deliver enterprise planning and performance monitoring processes, in line with the requirements of the <i>Public Governance, Performance and Accountability Act 2013</i></div></div> <div><div>1.18</div><div>that the Minister for Defence meet with the Defence Committee twice yearly to consider a formal strategic assessment of the alignment between Defence's strategy, funding and capability</div></div> <div><div>1.19</div><div>Defence conduct regular reviews of the capital program in consultation with the Minister and central agencies</div></div>	<p>We recommend:</p> <div><div>2.1</div><div>disbanding the Capability Development Group and dispersing its functions to more appropriate areas</div></div> <div><div>2.2</div><div>disbanding the Defence Materiel Organisation and transferring its core responsibilities in relation to capability delivery to a new Capability Acquisition and Sustainment Group</div></div> <div><div>2.3</div><div>developing a new organisational design and structure as part of the implementation process for the Capability Acquisition and Sustainment Group with reduced management layers</div></div> <div><div>2.4</div><div>examining each System Program Office to determine where each fits within the smart buyer function, the most appropriate procurement model and achieving value for money</div></div> <div><div>2.5</div><div>the Capability Managers specify the Fundamental Inputs to Capability requirements with the Capability Acquisition and Sustainment Group having responsibility for developing and delivering an integrated project plan</div></div> <div><div>2.6</div><div>the accountability for requirements setting and management be transferred to the Vice Chief of the Defence Force and the Service Chiefs with strategic, financial and technical contestability being located with Deputy Secretary Policy and Intelligence</div></div> <div><div>2.7</div><div>that the Independent Project Performance Office and the Capability Investment and Resources Division be relocated to Deputy Secretary Policy and Intelligence, significantly enhanced and strengthened to provide such contest</div></div> <div><div>2.8</div><div>revising the Defence investment approval process for all large or complex capability projects</div></div> <div><div>2.9</div><div>introducing a new formal gate into the process at entry point - Gate Zero: Investment Portfolio entry</div></div> <div><div>2.10</div><div>Government increase approval thresholds for capability development projects, with ministerial approval required only for projects above \$20 million, two ministers above \$100 million and Cabinet above \$250 million</div></div> <div><div>2.11</div><div>significant investment to develop an operational framework which comprehensively explains how the organisation operates and the roles and responsibilities within it; detailing the life cycle management processes which provide project and engineering discipline to manage complex materiel procurement from initiation to disposal; and reviewing architecture to reinforce accountability at all levels and bringing together information upon which good management decisions can be made</div></div> <div><div>2.12</div><div>the Deputy Secretary Capability Acquisition and Sustainment must sign off and assure the Secretary of the operational output of each of his/her divisions every quarter and on major contracts on a monthly basis</div></div> <div><div>2.13</div><div>the use of net personnel operating costs process cease immediately</div></div> <div><div>2.14</div><div>developing a Defence Investment Plan which would include all capital and related investments (such as materiel, estate and facilities, workforce and information and communications technology)</div></div> <div><div>2.15</div><div>that, on Government approval, the entire project acquisition budget is allocated to the Capability Acquisition and Sustainment Group to ensure expenditure is in accordance with the project delivery plan</div></div> <div><div>2.16</div><div>the Defence Science and Technology Organisation be required to clearly articulate its value proposition. This would include examples and actual amounts of value created</div></div> <div><div>2.17</div><div>the Defence Science and Technology Organisation become part of the Capability Acquisition and Sustainment Group</div></div> <div><div>2.18</div><div>the Defence Science and Technology Organisation senior leadership be rationalised</div></div> <div><div>2.19</div><div>the Defence Science and Technology Organisation strengthen partnerships with academic and research institutions to leverage knowledge and create pathways with academia and industry</div></div> <div><div>2.20</div><div>disbanding the Defence Science and Technology Organisation advisory board</div></div> <div><div>2.21</div><div>Defence, in partnership with academia and industry, review its research priorities, their alignment with future force requirements and capacity to leverage allied partners to promote innovation</div></div>	<p>We recommend:</p> <div><div>3.1</div><div>Defence define the estate need as determined by future force requirements and Government agree to dispose of all unnecessary estate holdings starting with the 17 bases identified in the 2012 Future Defence Estate Report</div></div> <div><div>3.2</div><div>Defence strengthen its capability to present options to Government for estate disposal including obtaining expert external advice as required</div></div> <div><div>3.3</div><div>the Government amend the <i>Public Works Act 1969</i> to set a \$75 million threshold for referring proposed works to the Public Works Committee, and re-consider recent adjustments to the 2015-16 Budget operational rules that run counter to more efficiently managing investment spending</div></div> <div><div>3.4</div><div>the Associate Secretary be directed and resourced to implement enterprise information management that provides Defence with trusted information to inform decision-making and military interoperability, with the Vice Chief of the Defence Force as the design authority for the next generation of Command, Control, Communications, Intelligence, Surveillance and Reconnaissance</div></div> <div><div>3.5</div><div>the information management agenda be governed at the Band 3/3 Star level by the Enterprise Business Committee to set overall direction and priorities, including the management of trade-offs and conflicts</div></div> <div><div>3.6</div><div>supporting the Chief Information Officer to meet these responsibilities by formally recognising the Chief Technology Officer as the technical authority with appropriate 'red card' decision rights</div></div> <div><div>3.7</div><div>Defence establish enterprise-wide frameworks for architecture standards and master data management</div></div> <div><div>3.8</div><div>Defence embark on a pragmatic implementation road map to standardise business and information processes and their supporting applications</div></div> <div><div>3.9</div><div>Defence ensure adequate resourcing and funding for information management reform is prioritised as part of the fully costed 2015 Defence White Paper</div></div> <div><div>3.10</div><div>geospatial information functions be consolidated into the Australian Geospatial-Intelligence Organisation following improved resourcing and connectivity</div></div> <div><div>3.11</div><div>the service delivery reform program, including full integration of the current Defence Materiel Organisation corporate functions, be completed</div></div> <div><div>3.12</div><div>all corporate services (with the exception of finance but including the Defence Security Authority) be consolidated under the Associate Secretary</div></div> <div><div>3.13</div><div>all military enabling services (Joint Logistics Command Policy, Joint Health Command, Australian Defence College, Australian Civil-Military Centre) be consolidated under a Two-Star officer who reports to the Vice Chief of the Defence Force</div></div>
4. ENSURE COMMITTED PEOPLE WITH THE RIGHT SKILLS ARE IN APPROPRIATE JOBS TO CREATE THE ONE DEFENCE WORKFORCE	5. MANAGE STAFF RESOURCES TO DELIVER OPTIMAL USE OF FUNDS AND MAXIMISE EFFICIENCIES	6. COMMENCE IMPLEMENTATION IMMEDIATELY WITH THE CHANGES REQUIRED TO DELIVER ONE DEFENCE IN PLACE WITHIN TWO YEARS
<p>We recommend:</p> <div><div>4.1</div><div>that as part of the budget and planning process, Defence build a strategic workforce plan for the enabling functions, and incorporate workforce plans for each job family in order to drive recruitment, learning and development, performance and talent management</div></div> <div><div>4.2</div><div>Defence employ Australian Defence Force personnel in non-Service roles only when it is critical to achieving capability and for a minimum of three years to achieve best value-for-money from the premium paid</div></div> <div><div>4.3</div><div>as many functions as possible be performed by public servants or outsourced if they are transactional in nature</div></div> <div><div>4.4</div><div>Defence review the entirety of its enabling and military corporate workforce to ensure that it supports the Australian Defence Force with the minimum of overlap and redundancy, and with the greatest overall economy, efficiency and effectiveness</div></div> <div><div>4.5</div><div>Defence reduce organisational layers; increase the spans of control of managers; align workforce standards in accord with the requirements of the Australian Public Service Commission; and engage external assistance to facilitate this work as required</div></div> <div><div>4.6</div><div>Defence implement a transparent performance management system that is consistently applied, recognises and rewards high performance and introduces consequences for underperformance and failure to deal with it</div></div> <div><div>4.7</div><div>as part of the performance management system, Defence take steps to create a culture where leadership, professionalism and corporate behaviour are valued and rewarded</div></div>	<p>We recommend:</p> <div><div>5.1</div><div>the use of the measures such as the teeth-to-tail ratio and the one third budget split should cease</div></div> <div><div>5.2</div><div>appropriate efficiency measures are developed which link to the delivery of agreed outcomes</div></div> <div><div>5.3</div><div>the focus on public service reductions as the primary efficiency mechanism for Defence cease</div></div> <div><div>5.4</div><div>Defence manage its workforce numbers in line with good resource management practice where Defence is held to account for delivering on required outcomes within available resourcing</div></div> <div><div>5.5</div><div>as part of the implementation process, Defence examine the headquarters functions for opportunities to achieve more effective and efficient arrangements</div></div>	<p>We recommend:</p> <div><div>6.1</div><div>no additional reviews on the organisational issues covered by this Review are imposed on Defence, particularly within the early years of implementation</div></div> <div><div>6.2</div><div>past reviews and current reform initiatives should be assessed for currency and alignment to the One Defence model</div></div> <div><div>6.3</div><div>establishing an Oversight Board to provide close external scrutiny, advice on implementation progress and regular reports to the Minister</div></div> <div><div>6.4</div><div>the Minister, with input from the Department and the Oversight Board, report progress on implementation to the Government in March 2016 and March 2017</div></div> <div><div>6.5</div><div>stability in the key leadership positions, particularly over the next two years to provide consistency of direction and ownership of the change</div></div>

1

One Defence Case for Change



The First Principles Review of Defence was commissioned by the then Minister for Defence in August 2014 following the Government's 2013 election commitment. We were tasked with ensuring that Defence is fit for purpose and is able to deliver against its strategy with the minimum resources necessary. The Terms of Reference for the review are at **Annex A**.²

Approach

We have taken a total systems approach based on evidence and analysis, sound principles and root causes rather than symptoms.

Our framework for the review (see **Annex B**) ensured we addressed the Terms of Reference in a manner which focused on the entire Defence system, interacting with the broader government, business and community systems. We have conducted an end-to-end holistic review based on the outcomes required of Defence and founded on the first principles agreed by the review team (see Diagram 1).

Diagram 1: First Principles

DEFENCE OUTCOME	FIRST PRINCIPLES
Protect and advance Australia's strategic interests through the provision of appropriately prepared and equipped armed forces. To achieve this, Defence prepares for and conducts military operations and other tasks as directed by the Government. ³	<ul style="list-style-type: none"> ☛ Clear authorities and accountabilities that align with resources <ul style="list-style-type: none"> ➤ Decision-makers are empowered and held responsible for delivering on strategies and plans within agreed resourcing ☛ Outcome orientation <ul style="list-style-type: none"> ➤ Delivering what is required with processes, systems and tools being the 'means not the end' ☛ Simplicity <ul style="list-style-type: none"> ➤ Eliminating complicated and unnecessary structures, processes, systems and tools ☛ Focus on core business <ul style="list-style-type: none"> ➤ Defence doing only for itself what no one else can do more effectively and efficiently ☛ Professionalism <ul style="list-style-type: none"> ➤ Committed people with the right skills in appropriate jobs ☛ Timely, contestable advice <ul style="list-style-type: none"> ➤ Using internal and external expertise to provide the best advice so that the outcome is delivered in the most cost-effective and efficient manner ☛ Transparency <ul style="list-style-type: none"> ➤ Honest and open behaviour which enables others to know exactly what Defence is doing and why

We considered the enduring tasks of Defence whilst recognising the changing future context that Defence will need to operate within. Then through the lens of the first principles we considered what is required to fulfil these responsibilities. We have focused specifically on the areas of: direction setting and control; provision of policy advice and intelligence; capability development, acquisition and sustainment; and the key enablers (information management, estate, service delivery and the workforce). We have conducted wide-ranging interviews with stakeholders and have been supported by the Boston Consulting Group and a small departmental secretariat.

² Annex A also includes the review recommendations aligned with the Terms of Reference and National Commission of Audit Defence recommendations.

³ Department of Defence, *Portfolio Budget Statements 2014 - 15*, Budget Related Paper no. 1.4A, 2014, p. 15, available at <www.defence.gov.au/budget/14-15/PBS.asp>.

Why another review?

Since the 1973 Tange Review, there have been over 35 significant reviews and many more supplementary reviews of Defence (see **Annex C**).⁴ The sheer frequency of reviews over the past decade has meant that many were short-lived or simply overtaken by the next review. Often the recommended changes were not allowed to bed in before another review began.

Despite this, Defence has implemented significant changes and improvements since the 1990s, for example, recommendations associated with the Kinnaird, Mortimer, Coles and Rizzo reviews along with the Pathway to Change initiatives. Compared to a decade ago, Defence has better governance and greater transparency. It has delivered on some difficult efficiency targets and has a more capable Australian Defence Force and Defence system generally.

Defence has a long history of effectively delivering militarily for Australia but faces great challenges over the next ten to twenty years. It must deliver a significant capability modernisation program against a backdrop of strategic uncertainty including, but not limited to: rapid technological change; budget uncertainty; substantial economic growth in our region; and increasing demand for military responses to various regional and expeditionary crises.

Notwithstanding previous reviews and reforms, both the Government and senior leaders in Defence recognise that the organisation needs to work much more effectively and that Defence in its current form is not best organised to meet these challenges. This is the focus of our review.

The problem

There is general agreement about the nature of the problem.⁵ The current organisational model and processes are complicated, slow and inefficient in an environment which requires simplicity, greater agility and timely delivery. Waste, inefficiency and rework are palpable.

Defence is suffering from a proliferation of structures, processes and systems with unclear accountabilities. These in turn cause institutionalised waste, delayed decisions, flawed execution, duplication, a change-resistant bureaucracy, over-escalation of issues for decision and low engagement levels amongst employees.

Previous reviews and interviews with stakeholders indicate Defence operates as a loose federation where the individual parts from the highest levels, then down and across the organisation, are strongly protective of their turf and see themselves meriting more favour than other parts of the department. The centre is weak and not sufficiently strategic.

The problem is illustrated by the following examples:

- The number of senior leaders has nearly doubled, growing from 201 in 1998 to 374 in 2014 (an 86 per cent increase), while the total number of other staff has risen from around 73,000 to 78,000 (an increase of seven per cent - see **Annex D**);
- There are around 200 active committees in the organisation;
- There are up to twelve layers in some parts of the organisational structure against good practice of around seven;⁶
- Eighty per cent of managers supervise less than five staff with sixty per cent of these supervising either one or two staff members. Good practice would see managers supervising between five and eight staff;⁷

⁴ The significant reviews are listed in Annex C, along with a summary of recurring themes in capability development and a timeline of reviews since 1973.

⁵ We formed our views following interviews with stakeholders and consideration of a range of recent reports to Parliament by its Committees and by the Australian National Audit Office.

⁶ From briefing material provided by the Australian Public Service Commission to the Secretaries' Board, October 2014, and the Boston Consulting Group, augmented with analysis of Defence personnel data.

⁷ *ibid*.

- Capability development is a series of hand-off points between different parts of the organisation involving around 7000 Defence staff spread across seven organisational units: the three Services, the Vice Chief of the Defence Force, Defence Science and Technology Organisation, Capability Development Group and Defence Materiel Organisation;
- The setting of needs and requirements is poor with priority given to single Service needs over joint projects. While 16 per cent of major capital equipment funding has been allocated to joint projects, actual expenditure is between four and nine per cent demonstrating that less priority is given to joint projects;⁸
- Costing methodology does not account for all of the inputs to capability, at acquisition and over project life, and the true total cost of ownership is opaque;⁹
- Project approval processes are lengthy and expensive. The average government submission is 70 pages long, takes 16 weeks to move through the Cabinet preparation process and an average of 46 months to progress from first pass initiation through to second pass approval;¹⁰
- Acquisition teams must comply with over 10,000 Defence Materiel Organisation specific policies and procedures which includes 35 policy and procedure artefacts totalling around 12,500 pages on procurement processes and controls;¹¹
- There is a 'one size fits all' approach to procurement strategy that inhibits strategic engagement with industry;¹²
- Defence has a larger estate footprint than it needs because of significant internal and external blockages to removing redundant parts of the estate; and
- Duplicated systems and processes reflect entrenched resistance to implementing businesslike approaches such as shared corporate services and the empowerment of single accountable officers in areas such as information management. According to the Chief Information Officer, Defence has over 2500 information and communication management applications including 300 financial applications.

Previous review themes

Previous reviews, more frequent since 1997, have resulted in only incremental change. Whilst these reviews have been specific rather than holistic or have occurred in response to specific events, they have nevertheless identified some consistent and recurring themes:¹³

- Requirement for greater clarity in the roles and responsibilities of the Secretary of Defence, the Chief of the Defence Force, the Service Chiefs and the organisation;
- Ongoing issues with the relationship between the Services and the supporting/enabling elements of the Defence organisation;
- Recurring issues with a lack of accountability, ill-defined authority, unclear allocation of responsibility and great difficulty measuring and monitoring real performance;
- Difficulty in balancing in-house service provision with industry support and services purchased externally;
- The requirement for fundamental and sustained changes in attitude and culture across all arms of the organisation; and
- The persistence of fundamental problems in the Defence capability system, from capability planning to acquisition, delivery and finally sustainment.

8 Advice from Chief of Capability Development Group based on programming analysis over 40 years.

9 Australian National Audit Office, *Major Projects Report 2013–14*, p. 17; Australian National Audit Office, Audit Report no.6 2013–14, *Capability Development Reform*, October 2013, pp 177-197. These reports are available at < <http://www.anao.gov.au/Publications/Audit-Reports> >.

10 Analysis of project approval data provided by Capability Investment and Resources Division.

11 The suites of documentation include inventory procurement policy, risk environment assessment policies, and Defence Materiel Organisation guidance.

12 Advice from industry and government stakeholders.

13 The significant reviews are listed in Annex C along with a summary of recurring themes in capability development and a timeline of reviews since 1973.

These concerns have also been widely acknowledged by external observers and commentators, including the Parliament, the Australian National Audit Office and the broader academic and professional community. They were echoed throughout our extensive engagement with individuals and organisations as part of the review process.

Resistance to change

These recurring themes and the continuing need for external review are symptomatic of an organisational culture within Defence that is risk-averse and resistant to change.

Reform of the capability development process is a pertinent example. The persistent message is that reform intent is subsumed by box-ticking and process tinkering. The Senate Foreign Affairs, Defence and Trade References Committee in its report on procurement procedures in Defence observed:

Defence's responses to the evident failings in their procurement projects have tended to focus on process. The committee is concerned, however, that such measures merely promote form over substance and it remains to be convinced that in practice they are effective. In the Committee's view, Defence have been tinkering at the margins of the problem, giving the impression that by improving process, the desired change in behaviour will follow. The Committee believes that such an approach only serves to mask fundamental weakness in the overall management structure of Defence and its major acquisition programs.¹⁴

Defence reported to Parliament that major reforms to buying military equipment proposed by David Mortimer in 2008 had been implemented. In 2013 the Auditor-General found that many of these recommended reforms had been implemented by 'process' rather than 'outcome', with Parliament none the wiser.¹⁵ Defence had added veneers of process, papered over the concerns of reviewers and the findings of auditors, and avoided fixing the underlying problems.

Concerns expressed by a number of external stakeholders to the review team consistently portrayed Defence as inward-looking, complicated and difficult to manage. A number of previous ministers and heads of central agencies also commented on Defence's lack of transparency, propensity for obfuscation and willingness to 'game the system' for its own advantage.

Playing the reform game, rather than delivering on the intent, has meant that Defence is not seen as transparent by central agencies, creating a lack of trust in decision-making. This in turn leads these agencies to engage at a more tactical level to constrain Defence. Unfortunately, these agencies often do not have a sufficiently detailed understanding of Defence, which means their attempts to defray risk result in additional processes which add to inefficiency and waste.

Root Causes

We acknowledge the complex and difficult tasks expected of Defence, particularly in making investment decisions with a 30 to 40 year tail. Yet we were puzzled as to why Defence has been unable to reform itself. Organisations need to be periodically reset and reshaped by their leadership. Substantive change appears to have been too difficult for Defence leaders because of the root causes listed over the page.

14 Senate Foreign Affairs, Defence and Trade References Committee, *Procurement procedures for Defence capital projects: Final Report*, August 2012, pp. 250–251, available at <www.aph.gov.au/Parliamentary_Business/Committees/Senate/Foreign_Affairs_Defence_and_Trade/completed-inquiries/2010-13/procurement/index>.

15 Australian National Audit Office, Performance Audit Report no. 6 2013–14, *Capability Development Reform*, October 2013, pp. 273–287, available at <www.anao.gov.au/Publications/Audit-Reports>.

In seeking to determine what has prevented Defence from changing, we noted three root causes which over the past decade have created complacency and inertia:

- The high operational tempo and increasing national security demands over the past decade have demanded high levels of the senior leadership's time and attention;
- Budget uncertainty with \$18.2 billion removed from the Defence budget from 2009–10 onwards which has led to reactive planning, deferred military capability and a hollowing out of enablers such as estate and information and communications technology; and
- Leadership churn from 1998 to the present resulting in nine ministers with an average tenure of two years, six Secretaries with an average tenure of two and a half years and five Chiefs of the Defence Force with an average tenure of four years.

We note the Government has acknowledged the budget uncertainty issue and that it aspires to increase Defence spending to two per cent of Gross Domestic Product. We also note that the life of this review extends beyond the current economic cycle. It is therefore prudent to assume that Defence expenditure may again come under pressure. In any event, the current waste and inefficiency will continue if Defence remains in its current form, as it is neither equipped nor organised to make efficient use of whatever funding levels are available to it.

Leadership churn and budget uncertainty are the critical root causes of the organisation's complacency. The frequent turnover in Ministers and Secretaries, in particular, does not enable effective leadership of change. The state of the organisation is symptomatic of one that has not been materially reshaped for over a decade and has been allowed to drift.

Delivering value

Defence is obliged to produce the military capability required to achieve its mission in a transparent, accountable and efficient manner. In so doing, it is also obliged to deliver the highest levels of public value.¹⁶

Ongoing drift and complacency, with or without increased funding, creates risk and opportunity costs for Defence and the Government. Defence capability will not be optimally delivered and wastage will mean less funding available for other priorities.

Defence cannot continue as it is. The time is right to clear the decks and liberate the organisation for the future. It must transform itself in order to deliver the required public value.

Direction

This is the third holistic, end-to-end review of Defence since Tange in 1973 and the Defence Efficiency Review in 1997.¹⁷ We have reviewed Defence's structures, systems and processes and concluded that it is imperative that Defence evolves into a single, integrated system.

Defence must become one end-to-end organisation, not a federation of separate parts, if it is to effectively and efficiently deliver the required outcomes. Joint capability — the ability to coordinate across land, air, sea, intelligence and other domains to deliver joint effects — is increasingly important to the war fighter. It is essential to prioritise investment in corporate and military enablers (such as information and communications technology) and professionalise the workforce.

We are recommending transformational change which will reshape the way Defence does business.

Our proposed end-to-end changes will enable Defence to operate as one integrated system to meet the challenges

¹⁶ Mark H. Moore, *Creating Public Value — Strategic Management in Government*, Harvard University Press, Harvard, 2002.

¹⁷ Sir Arthur Tange, *Australian Defence: Report on the Reorganisation of the Defence Group of Departments*, (hereafter the Tange Review), Department of Defence, Canberra, 1973; and Department of Defence, *Defence Efficiency Review*, Canberra, 1997.

of the future and deliver on its outcome in a more effective and efficient manner. We have termed this the **One Defence** approach.

Our recommendations for creating **One Defence** are a package which should be implemented in their entirety rather than cherry-picked and selectively modified. They represent transformational change because they entail organisation-wide structural, system and process changes combined with a requirement for a significant shift in business culture (mindset and behaviours) and discernible shifts in power.¹⁸

We recommend that this review be adopted as the road map for Defence reform for the next five years.

First class implementation is critical to the success of these reforms. It will require substantial drive, determination, endurance, focus from leadership and in some cases significant investment.

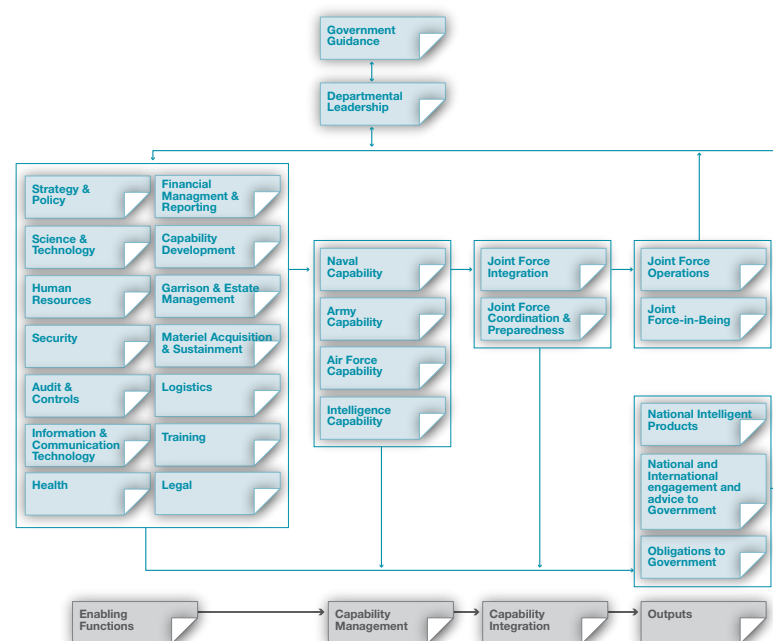
We have therefore recommended not just ‘what’ should change but also ‘how’ the change should be implemented. Success will only happen with strong, clear, wise and uncompromising leadership from the top (both public service and military) supported by an energetic, committed and able senior leadership team. Given the history of reform in Defence we also feel that this process will benefit from external scrutiny for an extended period of time.

One Defence Business Model

Implementing the **One Defence** approach will require changes to accountabilities, structures, systems and processes. More importantly, it will require changes to behavioural mindsets with clearly understood expectations that in delivering Defence outputs, leaders are focused on the corporate good and what is best for Defence overall. It will involve power and authority changes with the centre becoming much stronger than the individual parts but with an organisation more empowered to execute the direction set by the centre. It will also have stronger ‘checks and balances’ to ensure leaders are delivering on their commitments within agreed timeframes and budgets.

Defence’s current business model is a mixture of functions and structures.

Diagram 2: Defence’s current business model



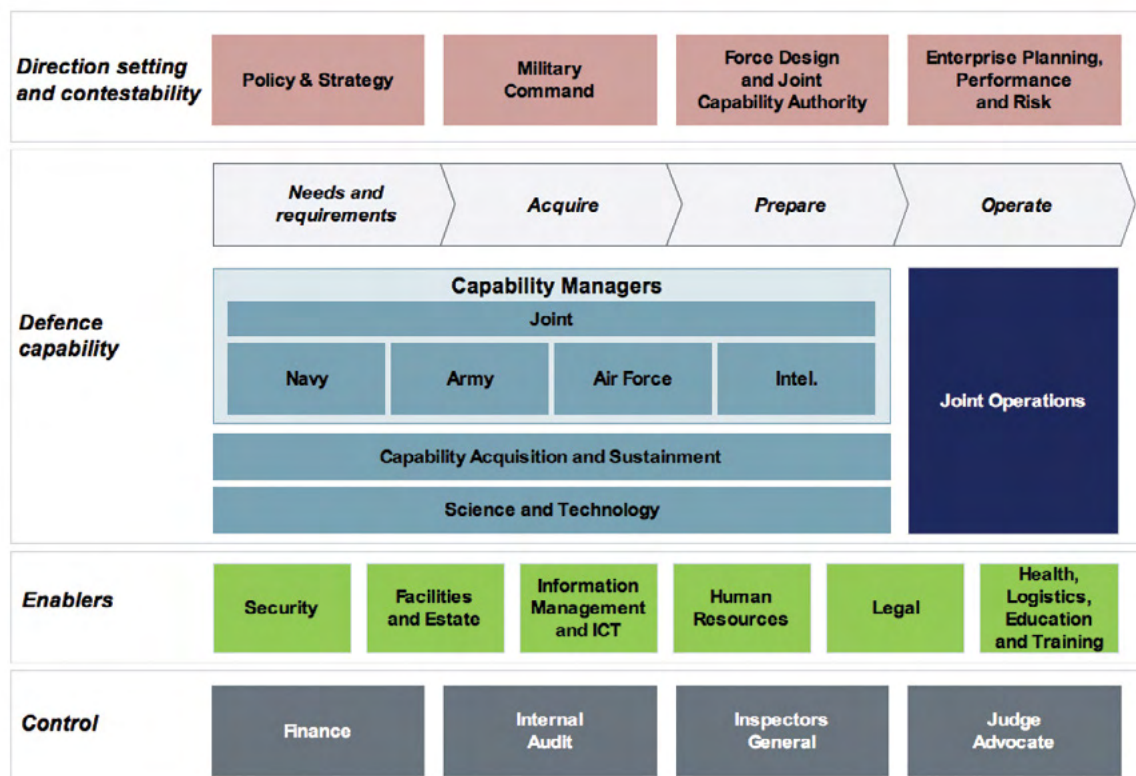
18 David Miller, ‘Delivering Transformational Change’, *The European Business Review*, March 2012.

In accordance with our first principles of simplicity and focus on core business, we have simplified the business model and designed the new model based on the functions required in the **One Defence** approach. It has three key features:

- **A stronger and more strategic centre** able to provide clear direction, contestability of decision-making, as well as enhanced control of resources and monitoring of organisational performance (refer Chapter 2);
- **An end-to-end approach for capability development with Capability Managers assigned clear authority and accountability** as sponsors for the delivery of capability outcomes to schedule and budget, supported by an integrated capability delivery function and subject to stronger direction setting and contestability from the centre (refer Chapter 3); and
- **Enablers that are integrated and customer-centric** with greater use of cross-functional processes, particularly in regional locations (refer Chapter 4).

We recommend a new One Defence business model:

Diagram 3: Proposed One Defence business model





2

One Defence
A Strong, Strategic Centre

Key Recommendation 1

Establish a strong, strategic centre to strengthen accountability and top level decision-making

The size and complexity of the Defence task requires a degree of decentralisation and autonomy within the three Services and other large organisational units. However the current organisation has too many voices to be effective. It lacks clear, single points of accountability for outcomes, is more focused on detail than alignment with policy or strategy, and rewards federated rather than enterprise behaviour.

Our recommendations for establishing the strong, strategic centre outline the roles and responsibilities of the diarchy¹⁹ and the top decision-making team. They also describe the committee structure required for effective decision-making and the planning and performance framework required to embed transparent and accountable corporate behaviour.

The strong strategic centre

Establishing a strong, strategic centre to set direction, provide contestability and ensure organisational control is consistent with our first principles and underpins **One Defence**. Current power and authority will shift to achieve more effective joint outcomes with empowered responsibility and activity in the service delivery and enabling functions.

The strategic centre will comprise the Secretary, Chief of the Defence Force, Associate Secretary, Vice Chief of the Defence Force, a new position of Deputy Secretary Policy and Intelligence, and the Chief Finance Officer. This group will form the new Defence Committee. The current Defence Committee of seventeen members is too large and unwieldy to function as an effective strategic centre.

The Diarchy

The diarchy is an unusual leadership construct that does not necessarily align with our first principles of clear authorities, accountabilities and simplicity. However, given the dual nature of the Defence organisation, which requires both military and public sector expertise, **we recommend the diarchy be retained**.

The diarchy maximises the value of public sector and military culture, skills and experience. It also provides the contestability of advice to Government which is required given Defence's two key outputs of joint warfighting and policy advice.

The current division of accountabilities between the Secretary and the Chief of the Defence Force has not been updated since the Ministerial Directive of 2007. We have noted the Commission of Audit's recommendation regarding the responsibilities of the diarchy.²⁰ We also received feedback from internal stakeholders about duplication of effort between the public service and military functions of Defence and consequent opacity around accountability at all levels in the organisation.

19 The diarchy is the term used to describe the dual leadership of the Australian Defence Organisation by the Secretary of the Department of Defence and the Chief of the Defence Force, enacted through legislation and subject to ministerial direction.

20 See recommendation 24(d) in National Commission of Audit, *Towards Responsible Government — The Report of the National Commission of Audit: Phase One*, February 2014, p. xlvi, available at <www.ncoa.gov.au>.

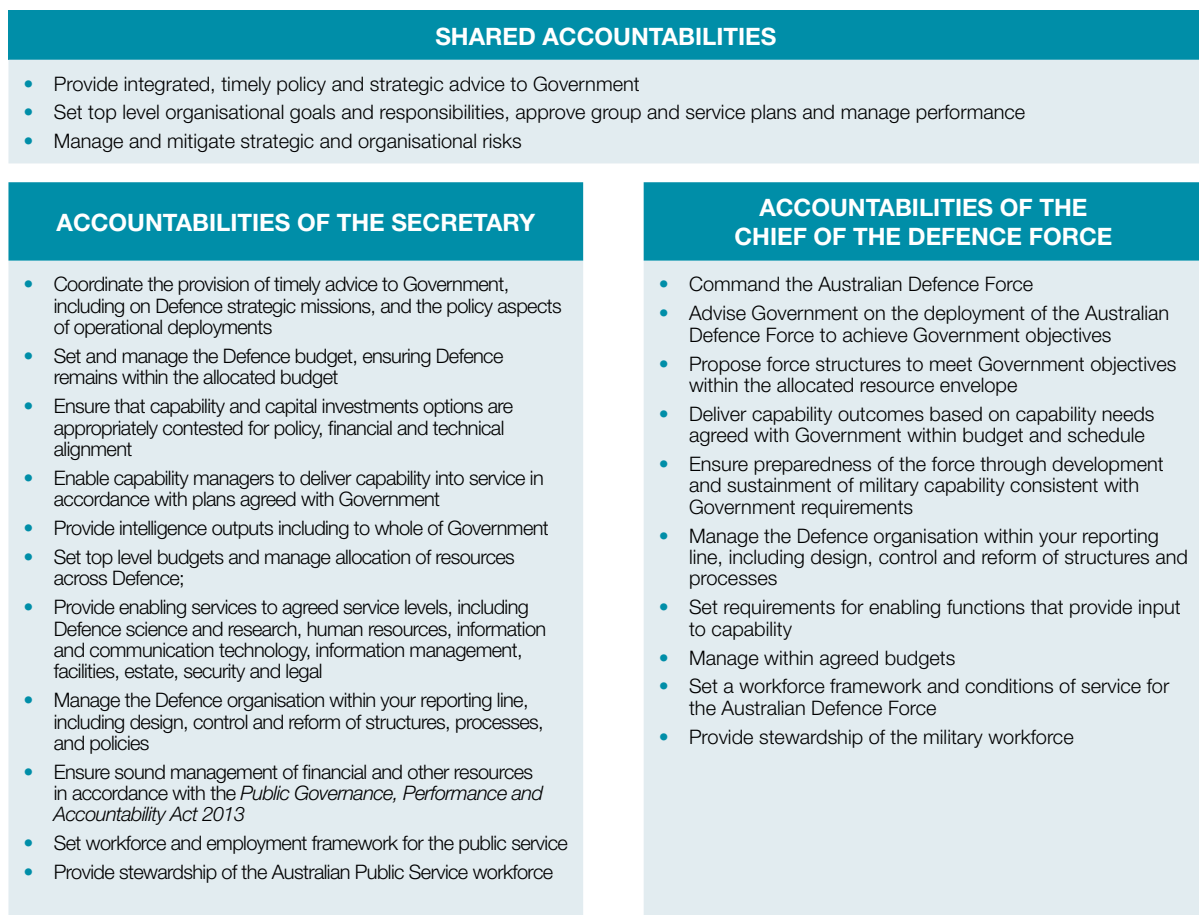
To increase effectiveness, minimise duplication and simplify reporting lines, **we recommend that the individual and shared accountabilities of the Secretary and Chief of the Defence Force be clarified, formally documented and promulgated throughout the organisation.**

More specifically, the shared accountabilities of the Secretary and the Chief of the Defence Force should be reduced to the highest level functions of the Department with individual accountabilities as follows:

- The Chief of the Defence Force commands the Australian Defence Force and is responsible for advising the Government on the deployment of the Australian Defence Force to achieve the Government's objectives. The Secretary has primary accountability for the provision of advice to Government, including for the policy aspects of operational deployments;
- The Secretary is responsible for managing the portfolio budget and plans to meet Government objectives, building on the force structure options developed by the Chief of the Defence Force;
- The Chief of the Defence Force is responsible for delivering capability and preparedness outcomes within schedule and budget, while the Secretary is responsible for providing the enablers; and
- The Secretary has ultimate responsibility for ensuring the sound management of financial and other resources, including setting and managing organisational budgets and overall investment management.

Maintaining the diarchy and the inevitable sharing of some accountabilities is not an excuse, however, for failing to ensure that the organisation operates as a integrated entity, nor should it weaken the individual accountabilities set out in Diagram 4.

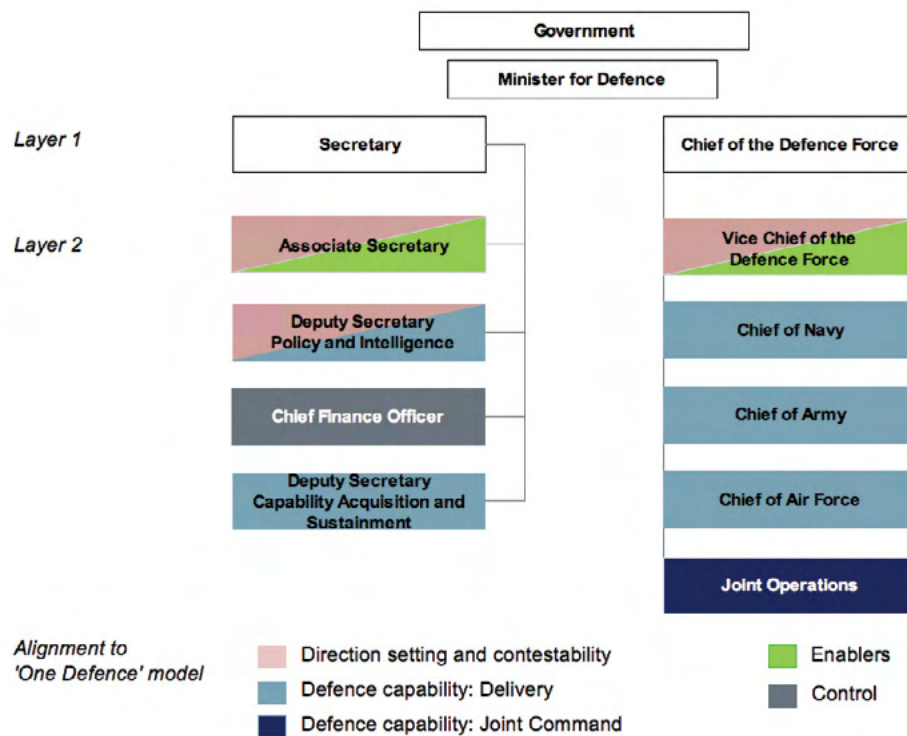
Diagram 4: Diarchy accountabilities



One Defence Senior Leadership

Delivering **One Defence** requires a senior leadership structure that is able to harness distinct military and public sector culture and skills. **We recommend a streamlined top level management structure for the Department that is aligned with the One Defence business model** (see Diagram 5).

Diagram 5: Proposed Layer 1 and 2 Organisational Chart



In the new structure the Secretary has four direct reports at Senior Executive Service Band 3 level:

- An **Associate Secretary** responsible for enterprise planning, performance and risk management and the integration of corporate enabling services;
- A new **Deputy Secretary Policy and Intelligence** responsible for policy, contestability and intelligence. This position incorporates the strategy, policy and contestability functions of Strategy Group, Capability Development Group and the Defence Materiel Organisation as well as the three Defence intelligence agencies;
- The **Chief Finance Officer** responsible for financial control and assurance; and
- A new **Deputy Secretary Capability Acquisition and Sustainment** role responsible for smart procurement of Defence capability and being the delivery agent for the Capability Managers. It incorporates functions from Capability Development Group, Defence Materiel Organisation, logistics service delivery, non-materiel procurement and the Defence Science and Technology Organisation. The Chief Defence Scientist role would be retained as a Band 3 reporting to the Deputy Secretary Capability Acquisition and Sustainment.

The Chief of the Defence Force has five direct military reports at the 3 star level:

- **Vice Chief of the Defence Force** as the joint capability authority with responsibility to champion joint capabilities and future force design (including preparedness settings and military strategy) and integrator of military enabling services (such as joint logistics policy, joint health, joint education);
- **Service Chiefs for Navy, Army and Air Force** retain their existing responsibility to raise, train and sustain capability as Capability Managers. As the Capability Development Group would be abolished, the service specific capability needs and requirements functions would transfer to the individual Services²¹ to support a stronger capability sponsor role. The Capability Acquisition and Sustainment Group would become responsible for delivering on their requirements; and
- The **Chief of Joint Operations** would retain responsibility for the conduct of joint operations.

Roles in the Strategic Centre

Integrators: Associate Secretary and Vice Chief of the Defence Force

Given the important roles the Secretary and the Chief of the Defence Force have in managing the external environment (upwards and outwards), it is important for the organisation to have integrators who bring others together, make trade-offs and drive cooperation to create joint outputs.²²

Integration is a central issue for the **One Defence** business model as it seeks to deliver the joint and future force more effectively as well as drive greater integration of the enabling functions. This will require prioritisation and trade-off decisions particularly across different capability areas.

In line with the Black Review of 2011,²³ the review team considers that integrators, at the second level of the organisation, supporting both the Secretary and the Chief of the Defence Force, are required for effective management in a diarchal organisation and to implement the **One Defence** system.

We recommend that the strategic centre include the Associate Secretary and Vice Chief of the Defence Force as the integrators for the Defence enterprise and the future force and joint capabilities respectively.

The **Associate Secretary** is the Secretary's deputy and the key integrator for the single Defence enterprise. The Associate Secretary is responsible for Defence enterprise planning, performance and risk management functions and is the integrator for all non-military enabling services (facilities and estate, security, information and communications technology, information management, human resources, legal and audit).

The **Vice Chief of the Defence Force** is the Chief of the Defence Force's deputy and is responsible for joint force integration, interoperability and designing the future force. In addition, the Vice Chief of the Defence Force is responsible for preparedness settings, military strategy and is the integrator for all military enabling services (Joint Logistics Command policy, Joint Health Command, Australian Defence College, Cadets and Reserves, and the Civil Military Centre).

21 Joint capability needs and requirements functions transfer to the Vice Chief of the Defence Force so that he can acquit his responsibilities as joint capability authority.

22 Y. Morieux and P. Tollman, *Six Simple Rules — How to Manage Complexity without Getting Complicated*, Harvard Business Review Press, Cambridge MA, 2014.

23 Black, Rufus, *Review of the Defence Accountability Framework*, (hereafter the Black Review), Canberra, January 2011.

Establishing a permanent future force design function means the Vice Chief of the Defence Force will be able to clearly set out requirements, including joint requirements. It will also provide capacity to evaluate capability development proposals from Capability Managers and review them on a continual basis for alignment with the strategic requirements of the Defence mission and investment program. The function should consider individual Service (maritime, land, air) and joint capability as well as enabling infrastructure requirements (such as the estate and information and communications technology required to support the force posture).

Although the Vice Chief of the Defence Force is currently identified as the Joint Capability Authority, the role has limited power to ensure that interoperability requirements are delivered. Currently, the Vice Chief of the Defence Force is but one voice among many and has to prove integration issues for consideration. **We recommend that the Vice Chief of the Defence Force's decision rights be greatly strengthened, including the right to stop projects proceeding through the approval process until joint force integration is proven.**

The system of command in the current legislation, the *Defence Act 1903* (Defence Act), is not congruent with the way the Australian Defence Force currently operates and our recommendations regarding **One Defence**. There is a risk of creating uncertainty in relation to command arrangements.

The Defence Act does not recognise the Australian Defence Force as an entity in its own right; rather it encourages a view that the Australian Defence Force is no more than a 'federation' of the three Services.

Subsection 9(2) does not, on its face, give the Chief of the Defence Force full command over the Australian Defence Force and, further, the Chief of the Defence Force's powers may be interpreted as being subject to (and potentially constrained by) the authority of the Service Chiefs to command their respective Services. The Defence Act no longer reflects actual practice and in effect undermines the authority of the Chief of the Defence Force over the Services. This creates uncertainty in relation to command arrangements.²⁴

In addition, the Vice Chief of the Defence Force, who is appointed under section 9AA of the Defence Act, has no explicit command authority. There is insufficient recognition of the Vice Chief of the Defence Force's role, particularly as the deputy to the Chief of the Defence Force.²⁵

In accordance with **One Defence** and our first principle of clear authorities and accountabilities, **we recommend the following legislative changes to formally recognise the authority of the Chief of the Defence Force and the Vice Chief of the Defence Force:**

- The Chief of the Defence Force to have full command of the Australian Defence Force by removing the legislative limitations on the Chief of Defence Force's command power;
- The Vice Chief of the Defence Force to be recognised explicitly as the 'Deputy' of the Chief of the Defence Force. This amendment would require clarifying that the Vice Chief of the Defence Force has command responsibilities as well as administrative responsibilities in relation to the Australian Defence Force as directed by the Chief of the Defence Force; and
- The Service Chiefs to be explicitly subject to the direction of the Chief of the Defence Force. A legislative amendment removing their statutory authority would ensure absolute clarity of the Chief of the Defence Force's command and authority.

The changes recommended to establish the strong, strategic centre are not reliant on these legislative changes and this recommendation should not be used as a reason to delay implementation.

²⁴ Internal Defence legal advice.

²⁵ *ibid*.

Strategic Advisors: Policy, Intelligence and Finance

Operating as **One Defence** requires the provision of high quality, coherent and timely policy advice to the Secretary, Chief of the Defence Force and the Government to inform long term capability and investment as well as a range of operational decisions.

A number of stakeholders raised concerns regarding the quality of policy advice in Defence. Several former Ministers stated that policy advice was diffuse, inconsistent and fragmented with one former Minister stating that his lack of confidence in Defence's policy advice led to engagement of third parties to 'second guess' it.²⁶ It is crucial that the Secretary and the Chief of Defence Force, as the primary policy advisers to Government on Defence issues, are provided with high quality strategic policy advice from within Defence. **We recommend that policy advice be strengthened by bringing all policy functions into one organisational unit in order to improve the quality of advice provided to Government.**

Defence also requires a mechanism for providing internal contestability, at arm's-length from owners and sponsors, up to the point of decision. This will ensure strategy, plans and resource allocations are tightly aligned and appropriately prioritised. It will also foster increased transparency and credibility with central agencies.

This differs from the current approach which is not at arm's-length because the internal contestability function reports directly to the military 3 star position responsible for the development of requirements.

We recommend that a strong and credible internal contestability function be built and led by the Deputy Secretary Policy and Intelligence with responsibility for:

- **Strategic contestability:** ensuring the force structure, portfolio of capability investments and individual projects deliver government policy objectives and the strategic needs as directed by the Government in the White Paper.
- **Scope, technical and cost contestability:** convening in-house expertise with expert challenge panels comprising internal and external people that contest key project deliverables (such as scope, schedule, budget, risks, technical aspects) throughout approval processes. Deputy Secretary Policy and Intelligence in conjunction with the Chief Finance Officer and external providers would also provide independent contestability of costing models.

In order to proceed, projects would require sign-off by the Deputy Secretary Policy and Intelligence for their consistency with financial, technical and strategic guidance.

Although we recommend consolidation of policy and contestability, the intent is for Defence to have a small team of experts with strong credibility and influence with Government. The group must build a strong external network of experts and draw on external support. It is also recognised that the Vice Chief of the Defence Force should be actively engaged in the formulation of policy advice that relates to the Australian Defence Force.

Intelligence assessment and collection is a key input into high quality policy formulation and capability decision-making. It is also a key output for Defence aligned to, and in accordance with, the Government-endorsed National Intelligence Priorities. We see the opportunity to further improve policy formulation and capability contestability by bringing the individuals involved at the intersection of policy and intelligence closer together under one Deputy Secretary.

We also see opportunities for improved career development between these areas of expertise. In both areas, Defence needs the highest standards of written and analytical skills. There are circumstances where the intelligence agencies will be able to examine policy and capability options in their formative stage and assess likely international reactions and responses. In turn, policy and capability contestability officers will be able to work with intelligence analysts to ensure that all lines of enquiry are being addressed in the development of their assessments.

We recommend that the policy and intelligence functions be combined under a Deputy Secretary Policy and Intelligence, who will have responsibility for providing policy advice and intelligence assessments to the Secretary and the Chief of the Defence Force.

²⁶ Interviews with stakeholders.

In recommending this structural change we considered the spans of controls and responsibilities of the two Deputy Secretary positions currently providing these functions and determined that only one position was required. To ensure that the scope of the Deputy Secretary Policy and Intelligence role does not become unmanageable and to better align service delivery to customer requirements, **we recommend the Defence Security Authority be repositioned under the Associate Secretary.**

We have considered very carefully the orthodox line of separation between policy advice and intelligence assessment. We have confidence that this new **One Defence** arrangement will operate with integrity for the following three reasons:

- The Defence intelligence agencies work to individual high level mandates that explicitly require independence of assessment. These mandates should continue and be reauthorised by the Secretary on an annual basis. These mandates provide the agency heads at the two star (Defence Intelligence Organisation) and Senior Executive Service Band 2 level (Australian Signals Directorate and Australian Geospatial-Intelligence Organisation) with an unambiguous statement that no-one is to direct them to a particular finding or assessment;
- The Defence intelligence agencies are nested within Australia's broader intelligence community. This keeps them aligned with, and anchored to, their core functions and outputs; and
- The Inspector-General of Intelligence and Security²⁷ regularly reviews the independence of the intelligence agencies as part of a government-mandated work program. This complements the confidential reporting mechanism available to Defence intelligence staff. This mechanism encourages staff at any level working in an intelligence agency to lodge a complaint to the Inspector-General of Intelligence and Security should they believe undue influence is being exerted on their assessments.

In essence, we are satisfied that these safeguards will ensure that organisational change does not lead to a 'merger' of the policy and intelligence functions and that, rather, it will substantively enrich policy advice and capability contestability. We emphasise that the authority and autonomy of the heads of the three Defence intelligence agencies should remain unchanged and be annually endorsed by the Secretary.

Chief Finance Officer

The Chief Finance Officer is responsible for providing budgetary contestability in the capability development process as well as in the corporate planning and budgeting processes. This involves ensuring portfolio level cost estimates align with the available budget. The position of Chief Finance Officer should always be filled by a person with formal accounting qualifications and an extensive accounting and finance background.

The Chief Finance Officer also needs to be capable of leading a collaborative dialogue with the Group and Service level budget holders, as well as the central agencies on the affordability of Defence's plans. This dialogue needs to be informed by a deep understanding of the underlying cost drivers of the business.

Senior Committees

The Secretary and the Chief of the Defence Force require an effective strategic forum to make major organisational, capability and resource trade-off decisions.

The current Defence Committee is unable to play this role effectively. The membership is too broad which slows decision-making and undermines the ability of the strategic centre to set direction. The agenda of the committee is also expansive, with too little time spent on the big strategic issues.²⁸

27 The role of the Inspector-General Intelligence and Security is to assist Ministers in the oversight and review of the legality and propriety of the activities of the Australian intelligence agencies, and to ensure these activities are conducted in a way that is consistent with human rights.

28 Boston Consulting Group analysed meeting agendas of the most recent six months of the Defence Committee and Secretary and Chief of the Defence Force Advisory Committee and interviewed senior leaders. Analysis showed overlapping agendas and committee consideration of matters that were the individual responsibility of either the Secretary or Chief of the Defence Force. The committees were also functioning in large part as information forums for Defence's senior leadership.

We recommend the Defence Committee be repositioned as the primary decision- making committee of Defence and the heart of the strategic centre with two supporting committees — Enterprise Business Committee and Investment Committee.

The new Defence Committee should continue to be chaired by the Secretary given the Secretary's overall responsibility for resource management in the Department. Its membership should be limited to the members of the strategic centre: the Secretary, the Chief of the Defence Force, the Associate Secretary, the Vice Chief of the Defence Force, the Deputy Secretary Policy and Intelligence and the Chief Finance Officer. The meetings of the committee should be confined to members only. Additional attendees should only be called in when their advice is required and/or they are presenting to the committee. Alternates should not be permitted.

The Chief of the Defence Force and the Vice Chief of the Defence Force would represent the Service Chiefs. This is in part designed to reduce tension between individual Service and whole-of-Defence objectives and to reinforce the Vice Chief of the Defence Force's role as the military integrator. The Associate Secretary would represent the non-military enabling functions.

A more strategic agenda should be adopted, focused on the major capability and resource trade-offs and the shared accountabilities of the Secretary and the Chief of the Defence Force, for example:

- Integration of strategic policy advice to Government;
- Endorsement of Defence White Paper, Force Structure Reviews and capability proposals;
- Setting top level resource allocations, including the appropriate balance of resources between capital, operating and personnel budgets;
- The approval of plans and scrutiny of performance against those plans including the Defence Investment Plan, Corporate Plan and associated Group and Services Plans; and
- Performance management decisions for the senior leadership group (both military personnel and public servants).

In order to ensure that the Defence Committee has sufficient time to focus on strategic issues including major capability and resource trade-offs, two subsidiary committees are required: the Enterprise Business Committee and the Investment Committee.

To ensure appropriate time and focus can be committed to these strategic committees, **we recommend that all other enterprise-wide committees be reviewed for their relevance and alignment with the One Defence business model with the aim of a substantial reduction in the number of committees.**

The **Enterprise Business Committee** would be chaired by the Associate Secretary and be responsible for ensuring the effective running of the Defence organisation, for example, planning, performance monitoring and reporting, enterprise risk management, information management and service delivery reform. The committee should not deal with matters that are within the purview of individual accountabilities or could be resolved through bilateral agreements. Significant reputational and risk issues should be raised to the Defence Committee.

Membership should comprise the Vice Chief of the Defence Force, Deputy Secretary Policy and Intelligence, Chief Finance Officer, Service Chiefs, Deputy Secretary Capability Acquisition and Sustainment and the heads of enabling functions (human resources, information and communication technology, facilities and estate).

The **Investment Committee** would be chaired by the Vice Chief of the Defence Force and would be responsible for undertaking regular holistic reviews of the investment portfolios for capability, estate and information and communication technology, taking into account force requirements, all necessary enabling functions and full-life costs. As Chair, the Vice Chief of the Defence Force would have decision rights to determine the investment portfolio recommendations that are taken to the Defence Committee for approval.

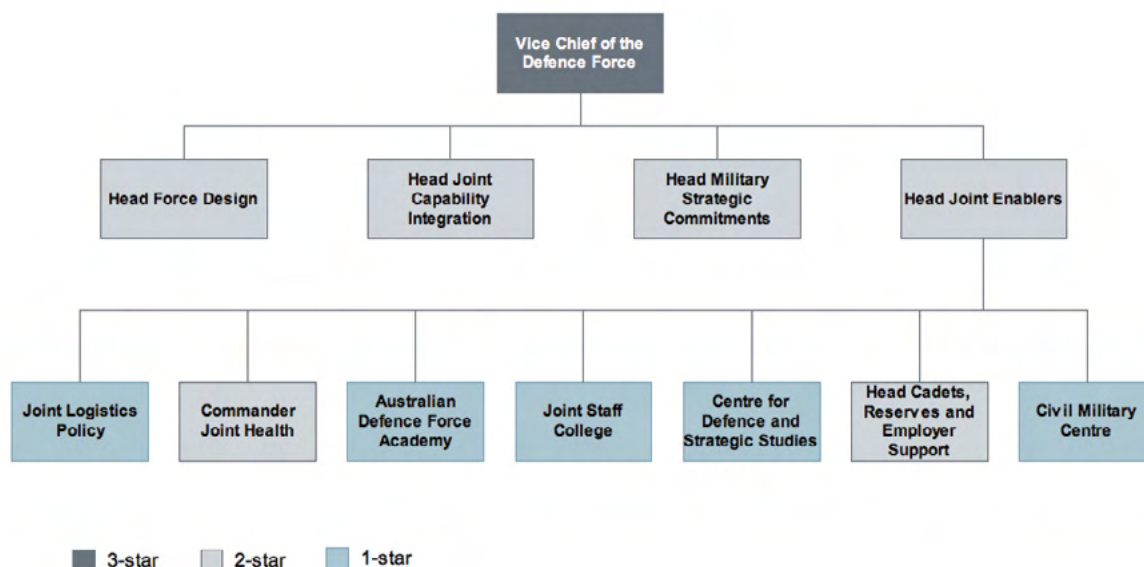
The Committee would also review project approval proposals in line with the new tailored Defence investment approval process outlined in Chapter 3. This would include considering whether the proposal is consistent with strategic guidance and is affordable within approved funding envelopes, and whether risks and interdependencies have been identified and managed.

The Investment Committee would also determine and document the accountability for project delivery. This would include what parts of the organisation would lead and who would be responsible for the achievement of capability outcomes. Failure of projects to be delivered on budget, on schedule and within full-life costs would have clear consequences within the new performance management approach (see Chapter 5).

Membership should comprise the Associate Secretary, Deputy Secretary Policy and Intelligence, Chief Finance Officer, Service Chiefs and Deputy Secretary Capability Acquisition and Sustainment. A senior official from the Department of Finance should be invited to participate as a means of building stronger partnerships with key central agencies.

The above changes represent an increase in workload for the Vice Chief of the Defence Force. To address this concern and ensure that the Vice Chief of the Defence Force has the capacity to fulfill the responsibilities as defined, **we recommend that the organisational structure reporting to the Vice Chief of the Defence Force be simplified through the incorporation of a two star Head of Joint Enablers role.** This would reduce the number of direct reports to the Vice Chief of the Defence Force from eight to four and enable him/her to focus on championing joint capability and the future force while the new two star officer manages the military enabling functions. Below is a possible option but ultimately the Chief of the Defence Force and the Vice Chief of the Defence Force will decide the specific structure.

Diagram 6: Possible Vice Chief of the Defence Force Group Structure



Enterprise Planning and Holding Leaders to Account

The strengthened role of the Vice Chief of the Defence Force and the implementation of an arm's-length contestability function are critical to a strong, strategic centre. In addition, effective corporate planning and performance monitoring are vital to ensure the direction set in the strategic centre is effectively cascaded through the organisation and leaders are held to account for their performance.

Defence needs to improve its corporate planning processes and ensure alignment with the *Public Governance, Performance and Accountability Act 2013*. **We recommend a strengthened centre-led, enterprise-wide planning and performance monitoring process be adopted.**

The major changes Defence must make in its corporate planning are:

- **Scope:** The corporate planning process should encompass all the major planning documents starting from the Corporate Plan and Defence Budget to Preparedness Directives and International Engagement Plans, down to the individual Group and Service plans in a consistent, resource-aligned planning cascade;
- **Central authority for alignment:** The role of the Associate Secretary would be to develop the overall Corporate Plan and provide central challenge of the resulting subsidiary planning documents, including the Group and Service plans. This would ensure alignment with strategy and priorities as well as appropriate identification and management of risks and interdependencies. The Chief Finance Officer would be responsible for ensuring that the plans align to resource allocations as part of the same planning process; and
- **Performance management:** The Associate Secretary should also play the role of chief performance officer, undertaking ongoing monitoring and performance management against the agreed Corporate Plan and subsidiary planning documents.

We recommend that the Associate Secretary be the central authority to deliver enterprise planning and performance monitoring processes, in line with the requirements of the *Public Governance, Performance and Accountability Act 2013*.

Strategic relationships

The **One Defence** business model is based on strong alignment between strategy, funding and capability. This requires transparency so that key resource trade-offs are resolved explicitly during strategy and planning processes. Key to implementation of the new business model is high quality government engagement based on our first principle of transparency. This will enable the Minister and the National Security Committee of Cabinet to understand the alignment between strategy, funding and capability and the cumulative impact of decisions on this alignment.

At present the relationship between strategy, funding and capability decisions is weak. There is no mechanism to reconcile the cumulative effect of previous Government decisions on strategy, capability and funding and therefore to highlight when they are no longer aligned. This stems from a lack of a common baseline for the capital and operating budget and a regular process whereby Defence reconciles the approved changes it has made or the offsets that have been found.

Several former Ministers and central agency heads referred to situations where they had been confronted with projects that had exceeded their budget accompanied by statements that Defence 'had absorbed' the overrun.²⁹ Such limited transparency reduces Defence's credibility.

Open and continuous dialogue with the Minister for Defence is important particularly in relation to major capital and operating funding decisions. **We recommend that the Minister for Defence meet with the Defence Committee twice yearly to consider a formal strategic assessment of the alignment between Defence's strategy, funding and capability.**

²⁹ Interviews with stakeholders.

Central agencies lack a common understanding of the major operating cost drivers of Defence. Without an agreed set of cost models, it is difficult to have a constructive dialogue in relation to appropriate responses to budget pressures.

It is evident that central agencies also lack confidence in the capacity of Defence to exercise internal contestability. This leads to a debilitating cycle referred to in Chapter One where more process is layered on Defence in an effort to obtain the information required and defray risk. Central agencies acknowledge they do not always have sufficient context or background to enable them to deal with every issue.³⁰

We recommend Defence conduct regular reviews of the capital program in consultation with the Minister and central agencies. Defence needs to establish a common baseline for capital and operating costs, reconcile changes proposed to the baseline and articulate what has been traded off to fit within the overall budget. The inclusion of a senior representative from the Department of Finance on the Investment Committee would also facilitate this engagement.

30 These matters were canvassed in interviews between the Secretaries of central agencies and the review team.

3

One Defence Capability Development Life Cycle



Key Recommendation 2

Establish a single end-to-end capability development function within the department to maximise the efficient, effective and professional delivery of military capability

The capability development life cycle (see **Annex E**) is critical in enabling Defence to perform its primary role of defending Australia and contributing to the protection of its national interests. Defence must efficiently and effectively procure capability and provide robust and timely advice to Government through an end-to-end capability development process.

Defence's capability development function has been subjected to extensive external reviews and scrutiny. We recognise that, over the last 12 years, significant effort has been expended to improve the capability development process. The Defence Procurement Review led by Malcolm Kinnaird in 2003 strengthened the two pass process, led to the creation of the Capability Development Group and the establishment of the Defence Materiel Organisation as a prescribed agency.³¹

Our view is that, whilst these reforms have improved elements of the capability development process, it is now timely to review the appropriateness of this model, particularly given the shortcomings identified in this review and the persistent external commentary about fundamental inadequacies in the Defence capability development system.

For example, the Senate Foreign Affairs, Defence and Trade References Committee report on Defence procurement procedures states that:

... the weight of evidence indicates that not only has Defence's preoccupation with process been misguided but it has been counterproductive. In response to identified problems, Defence has created a procurement process that is convoluted and overburdened by administration. The committee is of the view that the entire organisational structure of Defence must be simplified and streamlined. Only by reducing the number of stakeholders (groups) involved in the process can the excessive administrative burdens and committees be reduced.³²

In our view, the binary choice of whether the Defence Materiel Organisation should be in or out of the Department as outlined in the Terms of Reference is too simplistic. Defence needs a smart buying function which operates within the larger government system and global supply chains.

The current capability development construct creates a disconnect between customers and the purchaser as well as multiple and unnecessary handover points which increase complexity and risk.³³ Given the pre-eminence of capability development in executing the Defence mission, **we recommend that a single end-to-end capability development function be established within Defence.**

31 Department of Defence, *Procurement Review 2003* (hereafter the Kinnaird Review), August 2003, available at <www.defence.gov.au/publications/dpr180903.pdf>.

32 Senate Foreign Affairs, Defence and Trade References Committee, *Procurement procedures for Defence capital projects: Final Report*, August 2012, p. 250.

33 It became evident during the course of the review that there were handover points between the Force Structure Review and Capability Development Group, between Capability Development Group and the Defence Materiel Organisation, and between the Defence Materiel Organisation and the Capability Manager. See in particular Australian National Audit Office, Performance Audit Report no. 57 2010–11, *Acceptance into Service of Navy Capability*, June 2011, p. 78–80, available at <www.anao.gov.au/Publications/Audit-Reports>.

We acknowledge that the establishment of a single, end-to-end capability development function in Defence that is efficient, effective and professional will require transformational change. In summary, the required changes include:

- Abolition of the Capability Development Group and the Defence Materiel Organisation in their current form;
- Creation of a Capability Acquisition and Sustainment Group under a Deputy Secretary reporting to the Secretary;
- Moving to a leaner ‘smart buyer’³⁴ model that better leverages industry, is more commercially oriented and delivers value for money;
- Strengthening the front end of the capability development life cycle by revising the two pass process, establishing an entry gate and creating more opportunity to tailor and fast track projects;
- Standardising project governance processes and procedures for capability delivery and internal review;
- Abolition of the Defence Capability Plan in its current form and replacing it with a Defence Investment Plan that incorporates all major investments;
- Strengthening and placing at arm’s-length a continuous contestability function that operates throughout the capability development life cycle from concept to disposal; and
- Transferring accountability for requirements setting and management to the Vice Chief of the Defence Force and the Service Chiefs within a regime of strong, arm’s-length contestability.

Implementation of these changes will require focus and commitment from all members of Defence involved in the capability development life cycle. These changes need to start quickly, be pursued with energy and be guided by new and strong leadership.

Current state

It is clear that the processes in the current capability development life cycle are cumbersome, excessively bureaucratic and inefficient. The organisation is more focused on process adherence than high quality capability outcomes. In our view the following are the most significant, but not the only, shortcomings of the current situation:

- An artificial handover point between Capability Development Group and the Defence Materiel Organisation that complicates the focus on capability outcomes;³⁵
- A complexity of organisation and process which has led to an extremely top heavy Defence Materiel Organisation with a structure that, in some cases, is eleven layers deep.³⁶ This has led to a disempowered delivery organisation;
- Elements of the Defence Materiel Organisation which have little or no perceived value as they are not core to the acquisition and sustainment function;³⁷
- An excessive number of System Program Offices evidenced by 83 per cent of expenditure being managed by 31 per cent of System Program Offices;³⁸

34 In this context: ‘A smart buyer is one who retains an in-house staff who understands the organization’s mission, its requirements, and its customer needs, and who can translate those needs and requirements into corporate direction. A smart buyer also retains the requisite capabilities and technical knowledge to lead and conduct teaming activities, accurately define the technical services needed, recognize value during the acquisition of such technical services, and evaluate the quality of services ultimately provided. As long as the owner retains the in-house capabilities to operate as a smart buyer of facilities, there does not appear to be any greater risk from contracting out a broad range of design review-related functions, so long as such functions are widely available from a competitive commercial marketplace. If the owner does not have the capacity to operate as a smart buyer, the owner risks project schedule and cost overruns and facilities that do not meet performance objectives.’ See United States Government Accountability Office, GAO/GGD-00-172R, *Study on Facility Design Reviews*, July 2000, available at < <http://www.gao.gov/assets/90/89986.pdf>>.

35 Analysis of interviews with stakeholders.

36 Analysis of Defence personnel data.

37 PriceWaterHouseCoopers, *DMO End State Design Final Report*, December 2013.

38 Strategy&, Report to DMO, October 2014.

- A lack of sufficient commercial skills in staff of both Capability Development Group and the Defence Materiel Organisation including capacity to assess and manage risk;³⁹
- Capability Managers who are accountable for developing, delivering and sustaining the current and future capability needs of the Services but are remote from the critical requirements definition phase which occurs in the Capability Development Group;
- Inappropriate utilisation of military staff who should be the effective stewards of requirements setting within the rigour of strong, strategic, financial and technical contestability;⁴⁰
- An excessive amount of process⁴¹ in the capability development life cycle which has become a box-ticking, compliance exercise rather than one focused on outcomes;
- Institutionalised and costly project slippage;⁴²
- Poor management with schedule delays being used to mask cost and technical blowouts and to deflect accountability;⁴³
- An unsophisticated approach to engaging industry, especially early in the project life cycle, and an obsessive focus on adherence to probity and competition requirements;⁴⁴
- An almost total absence of common internal review processes and procedures;⁴⁵
- No appropriately granular mechanism to manage internal cost and schedule and an inadequate methodology for estimating operating and sustainment cost;⁴⁶ and
- Failure to adequately project manage all of the Fundamental Inputs to Capability⁴⁷ and the lack of a holistic portfolio level investment plan.⁴⁸

39 Australian National Audit Office, Performance Audit Report no. 6 2013–14, *Capability Development Reform*, October 2013.

40 *ibid.*

41 Boston Consulting Group's analysis of the Military Integrated Logistics Information System Inventory Procurement Policy and Risk Environment Assessment, and material provided by the DMO Standardisation Office during the course of the review.

42 Analysis of data provided by Capability Investment and Resources Division.

43 Interview with members of the Independent Project Performance Office.

44 Interviews with stakeholders.

45 Interviews with Defence Materiel Organisation senior leaders.

46 Australian National Audit Office, Performance Audit Report no. 6 2013–14, *Capability Development Reform*, October 2013, pp. 177–190, confirmed in interviews with stakeholders and data provided by Capability Investment and Resources Division.

47 The elements required to generate capability comprise personnel, organisation, collective training, major systems, supplies, facilities and training areas, support, and command and management.

48 Analysis of data provided by Capability Investment and Resources Division.

Structure

The creation of a Capability Development Group was intended to ensure a single point of accountability for managing the capability development process and achieving robust outcomes. For the reasons listed above this has not worked as envisaged. **We recommend disbanding the Capability Development Group in its current form and dispersing its functions to more appropriate areas:**

- The contestability and submission development function performed by Capability Investment and Resources Division should move to Policy and Intelligence;
- The requirement development function should be transferred to the Vice Chief of the Defence Force and the Service Chiefs;
- Australian Defence Test and Evaluation Office and the Project Management Office should move to Capability Acquisition and Sustainment Group; and
- Group support functions should be disbanded under the strengthened shared services model (see Chapter 4).

The Defence Materiel Organisation has also been beset with problems that have impacted its ability to achieve the required outcomes. It is clear that the organisation has become top heavy, complex and unnecessarily deep.⁴⁹ This significantly contributes to Defence not getting the capability it needs at a reasonable cost or in reasonable time.

De-layering and greater empowerment of the organisation is essential for efficient operation. In order to achieve this **we recommend that the Defence Materiel Organisation be disbanded in its current form and its core responsibilities in relation to capability delivery be transferred to a new Capability Acquisition and Sustainment Group.**

The new Capability Acquisition and Sustainment Group would be formed within the Department under a single Deputy Secretary reporting to the Secretary. This Deputy Secretary should have extensive experience managing large commercial supply chain and project management organisations. Remuneration for this Deputy Secretary should be set by the Secretary of Defence at a level that attracts the commercial skills and experience needed.

The new group would manage a project from Gate Zero⁵⁰ through to Final Operating Capability, including the integration of all Fundamental Inputs to Capability. The formation of this new group would create a centre of excellence in procurement and capability delivery by consolidating a number of functional areas:

- System Program Offices and other core procurement and sustainment functions from the Defence Materiel Organisation under a smart buyer construct;⁵¹
- The supply chain and delivery components from Joint Logistics Command;
- The non-materiel procurement function from Defence Support and Reform Group;
- The Defence Science and Technology Organisation; and
- Elements from Capability Development Group as set out above.

As part of the creation of this new group **we recommend that a new organisational design and structure is developed as part of the implementation process for the Capability Acquisition and Sustainment Group with reduced management layers.**

49 Analysis of Defence personnel data and interviews with stakeholders within Defence Materiel Organisation.

50 Gate Zero is a new, formalised point in the approval process where a concept is given approval to progress for development and potential consideration at first pass.

51 A smart buyer construct will ensure Defence can make strategic decisions regarding the most appropriate procurement and contracting methodologies and will support flexible tailoring options to implement the most suitable methodology.

In Chapter 5 of this report there are significant recommendations with regard to the development of workforce skills and talent management. All of these will be required to make the Capability Acquisition and Sustainment Group an effective and efficient organisation.

We have heard many complaints from the Defence Materiel Organisation leadership about the ability to hire and fire public servants. We agree with the advice provided by the previous Public Service Commissioner that the *Public Service Act 1999* provides more flexibility than Defence has utilised which indicates that this is a managerial rather than legislative issue. For example, the decision to hire ongoing or non-ongoing staff is a matter for each department. Non-ongoing terms can be for either a specified term or a specific project, that is, for three years or for the duration of the project. If the non-ongoing period is greater than 12 months it will need to be advertised formally.

Smart Buyer and Industry

We envisage that the Capability Acquisition and Sustainment Group would comprise a smaller core group of skilled public servants managing a 'smart buyer' function. This function is reliant on an enhanced relationship with industry which would provide expertise in managing projects in the acquisition and sustainment phases. In this context we are not proposing a 'one size fits all' approach. We recognise that each Systems Program Office is inherently different, with different operating and contracting models as well as various and sometimes unique commercial arrangements.

We recommend that each System Program Office be examined and analysed to determine:

- **Where it fits within the smart buyer function; and**
- **The most appropriate procurement model for delivering the capability and achieving value for money.**

In some cases it would be appropriate to outsource completely the acquisition and sustainment functions conducted by a Systems Program Office. In other cases it may be appropriate to outsource sustainment and partner with industry for the acquisition phase. It may be determined that certain Systems Program Offices, such as clothing, may be best dealt with under the non-material procurement function. We consider that it would be possible to rationalise and reduce the Systems Program Office structure and staffing levels as more sophisticated contracting models are established and their individual support functions are consolidated as part of the service delivery reform (see Chapter 4).

The Capability Acquisition and Sustainment Group should outsource significant elements of the project management associated with sustainment contracts to an appropriate provider or providers. Work has already been completed internally that could be leveraged to support this requirement.⁵² We envisage efficient implementation would result in reductions in the public service workforce and the transfer of military personnel to other functions within Defence (see Chapter 6).

Implementing a smart buyer function would allow Defence to focus on planning and governance, and industry to focus on execution. Defence personnel should not be planning technical work but instead providing an oversight role — reviewing and approving plans developed by industry to meet outcomes required by Defence.

We have had significant evidence from industry and other commentators⁵³ that the current reliance on a 'one size fits all' competition policy and the use of complex procurement contracts does not produce the best results from domestic and international industry. It also adds significant cost and time for all participants and encourages unrealistic costing to be included in the decision-making process. The importance and relevance of competitive tension amongst prospective bidders varies from project to project. In some cases there may be only one realistic option.

Implementation of a smart buyer approach will involve tailoring procurement strategies appropriately which will enable industry to be involved earlier and undertake project and contract management activities currently undertaken by Defence. This is particularly relevant in the sustainment phase of the life cycle and should encompass the progress made through the Rizzo and Coles reforms.⁵⁴

⁵² PriceWaterHouseCoopers, *DMO End State Design Final Report*, December 2013.

⁵³ Interviews with stakeholders.

⁵⁴ See Rizzo, Paul, *Plan to Reform Support Ship Repair and Management Practices*, July 2011; and Coles, John, e al., *Study into the Business of Sustaining Australia's Strategic Collins Class Submarine Capability*, Canberra, November 2012.

A number of work units have grown within the current Defence Materiel Organisation that are peripheral to the core business of the delivery organisation. The work of some of these units may be more efficiently carried out by other areas of government, or not carried out at all. One example is Industry Division: its roles and functions should be transferred to the Department of Industry which would have the benefit of placing Defence industry within the broad Australian industrial landscape.

The outputs of Defence industry should be viewed as a Fundamental Input to Capability and be integrated into the acquisition life cycle. This may well mean a more imaginative use of a small number of potential contractors early in the process or the extension and use of already existing collaborative mechanisms (such as rapid prototyping, development and evaluation) at the very early stages of requirements development.

Fundamental Inputs to Capability

We recognise that the responsibility for the total range of Fundamental Inputs of Capability is necessarily distributed throughout the Defence organisation. However, it is important to manage these inputs in an integrated manner in order to bring capability into service.

There is evidence that current shortfalls and delays in the introduction of capability occur between Initial Materiel Release and Initial Operating Capability.⁵⁵ The predominant reason for this is the lack of integration of non-materiel elements such as estate and information and communications technology. Therefore, **we recommend that the Capability Managers specify the Fundamental Inputs to Capability requirements with the Capability Acquisition and Sustainment Group having responsibility for developing and delivering an integrated project plan.** Full accountability for project delivery will not be complete until this has been achieved.

Requirements Setting and Management

The added value in utilising Australian Defence Force personnel in the acquisition and sustainment life cycle is their expertise in the creation and management of requirements. This process has become cumbersome, complex and inefficient despite the good intentions in the creation of Capability Development Group.⁵⁶

Capability Managers, which include the Vice Chief of the Defence Force for joint capability, should own the requirements phase. This is not currently the case. **We recommend the accountability for requirements setting and management be transferred to the Vice Chief of the Defence Force and the Service Chiefs with strategic, financial and technical contestability being located with Deputy Secretary Policy and Intelligence.** We acknowledge this will require the enhancement of skills in the Capability Managers' headquarters and a rebalancing of the workforce in the Capability Acquisition and Sustainment Group.

Arms-Length Contestability

At the same time all requirements at each phase of the life cycle should be subject to strong arm's-length and expert contest. Both the Vice Chief of the Defence Force and the Deputy Secretary Policy and Intelligence should have 'red card' decision rights on projects at each gate for future force design and joint force integration and strategic, technical and financial elements respectively.

55 Australian National Audit Office, ANAO Report no.14, *2013-14 Major Projects Report*, p. 17, available at <www.anao.gov.au/Publications/Audit-Reports>.

56 Australian National Audit Office, Performance Audit Report no. 6 2013-14, *Capability Development Reform*, October 2013, pp. 138-139.

The kernel of an appropriate arm's-length contest organisation is already present in the Independent Project Performance Office in the Defence Materiel Organisation and the Capability Investment and Resources Division in Capability Development Group. **We recommend that the Independent Project Performance Office and the Capability Investment and Resources Division be relocated to Deputy Secretary Policy and Intelligence, significantly enhanced and strengthened to provide such contest.** This is not to be seen as an opportunity for inexperienced personnel to block capability proposals without good reason. The establishment of a robust and disciplined contestability function is intended to provide arm's-length assurance to the Secretary that the capability needs and requirements are aligned with strategy and resources and can be delivered. It needs to be designed to enable the best outcomes.

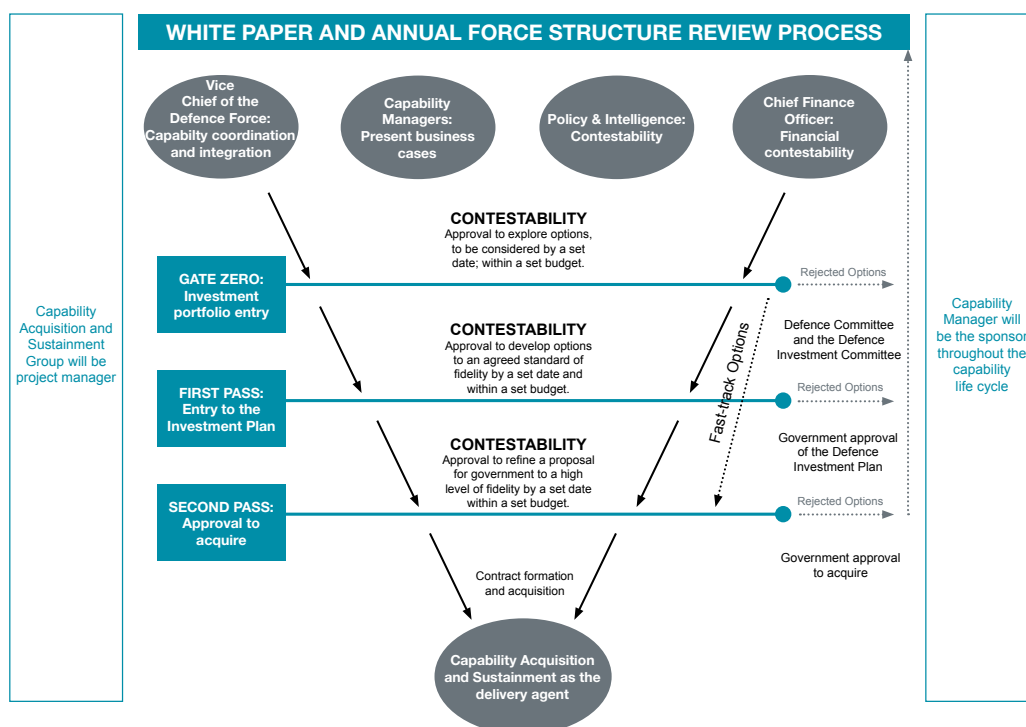
Revised two pass process

The approvals granted at gates in the current two pass process have moved away from the original intent as outlined by Kinnaird.⁵⁷ A number of stakeholders expressed concern over the tendency to finalise a preferred solution too early. Instead of first pass being agreement to assess realistic options, it is often the point at which a preferred solution is agreed.

As a result, the documentation set and resultant effort required to get through first pass has increased, with little discernible improvement in the quality of decisions being made. A number of stakeholders expressed the view that the volume of documentation reduces clarity and makes good decision-making more difficult.⁵⁸

To resolve the issues outlined above, **we recommend a revised Defence investment approval process for all large or complex capability projects.**

Diagram 7: Defence Investment Approval Process



57 Department of Defence, *Procurement Review 2003* (hereafter the Kinnaird Review), August 2003, available at <www.defence.gov.au/publications/dpr1180903.pdf>.

58 Interviews with stakeholders.

This revised process should include gates designed such that projects start with radically different options to meet the strategic need then narrow to a preferred solution within agreed timeframes. The document set for each approval gate should be reviewed and redesigned to be fit for purpose with the goal of significantly reducing the documents required to achieve final approval.

The front end of the process should be strengthened by having a much more thorough review of projects at initiation. Specifically, **we recommend that a new formal gate be incorporated into the process at the entry point — Gate Zero: Investment Portfolio entry.** This gate will be the point at which approval is provided to explore the range of options that may be suitable for a potential project.

At this point the Capability Manager is formally designated as the sponsor and the Capability Acquisition and Sustainment Group provides support during the development of requirements and options. Gate Zero would not be the point at which public announcements are made about a project commitment. Rather, the project would enter the delivery and approval process with agreed time lines and conditions for consideration at first pass.

Each Capability Manager would need to maintain a pipeline of potential new capability projects which are under consideration (based on their view of the evolving capability needs within their domain) but not yet ready to enter the Defence Investment Plan.

At Gate Zero and first pass, approval would be provided for the next stage of work only, based on a view that investment in the next stage was worthwhile given the overall business case. The documentation set required at each gate should include only the analysis required to inform the decision being made at the particular gate.

The current shopping list approach towards the Defence Capability Plan would cease.⁵⁹ The arm's-length contestability function described previously should test that projects are both likely to fit with the future capability needs of Defence and ready in all aspects to proceed to the next gate. If timeframes, technical requirements and financial commitments approved at each gate are not met, the request for approval to proceed to the next gate should be rejected. This means that projects can be restarted at Gate Zero or removed altogether.

Not all projects need to follow the full process — there should be judicious use of a fast track path, subject to strong contestability that confirms delivery risks are acceptable. This will improve efficiency, reduce the duration of the pre-acquisition phase and relieve pressure on the volume of Government approvals. It is the common sense approach of a smart buyer.

The option to skip first pass and proceed straight from Gate Zero to second pass should be considered at the Gate Zero decision point where:

- There is only one feasible supplier of the required platform;
- Defence is acquiring additional units of an existing capability;
- There are mandatory interoperability requirements that require a certain platform choice;
- Operational urgency is more important than optimising capability/cost trade-off; and /or
- The project is relatively simple.

In addition, **we recommend the Government increase approval thresholds for capability development projects, with ministerial approval required only for projects above \$20 million, two ministers above \$100 million and Cabinet above \$250 million.**⁶⁰

59 The Defence Capability Plan is widely seen as little more than a shopping list because the hurdles to being listed in the plan are minimal and individual projects are not assessed on an opportunity cost basis before being listed in the plan.

60 Since July 2011, the Minister for Defence may approve projects valued at \$20 million or less, the Minister for Defence and the Finance Minister may approve projects valued up to \$100 million, and all projects of greater value must be considered and approved by Cabinet.

At present, half of the projects considered by Government are worth less than six per cent of the total program cost. Increasing the thresholds would result in around a 30 per cent reduction in the number of Cabinet submissions required for the current Defence Capability Plan.

This change would accelerate project delivery, ensure that senior attention is focused on critical projects and would start to reduce the transactional nature of interactions with Government, which need not be concerned with smaller capability projects.

Policy and Process

In an organisation which routinely manages complex projects and programs we found it remarkable that there is no common project management architecture or artefacts to support it. There are no standardised reporting mechanisms (reporting is informal, anecdotal, local or crisis based) or management processes, with all divisions having different methodologies and management systems.⁶¹ There has been no consistent application of fundamental tools such as Earned Value Management. Such tools will be required to support the new leadership team.

Standardised management and reporting tools are necessary to enable the leaders of this function to manage the business well. **We recommend that there be significant investment in the development of:**

- **An operational framework which briefly but comprehensively explains how the organisation operates and the roles and responsibilities within it;**
- **A detailed set of life cycle management processes which provide the project and engineering discipline with which to manage complex materiel procurement from initiation to disposal; and**
- **A review architecture which reinforces accountability at all levels and brings together information at each level upon which good management decisions can be made.**

We recognise that this will involve a large amount of work but it is essential that it be done to allow for proper project management governance. All of this needs to be underpinned by a strong and enduring approach to communication to ensure quality employee and stakeholder commitment.

Significant changes will also need to be made to the management information systems to support the timely provision of information. As a benchmark, **we recommend that the Deputy Secretary Capability Acquisition and Sustainment must sign off and assure the Secretary of the operational output of each of his/her divisions every quarter and on major contracts on a monthly basis.** This arrangement should be cascaded throughout the organisation.

It is also incumbent upon the organisation to have a process in place that effectively measures its cost, schedule and productivity **at a project level.** This should be implemented immediately and individual leaders from the first line to the Deputy Secretary Capability Acquisition and Sustainment must be accountable for cost and schedule targets.

Net Personnel and Operating Cost is Defence's current estimate of the personnel, operating and sustainment cost of a proposed capability. It is an estimate of the differential cost above that of the current capability and is included in submissions to Government for approval. This approach is problematic as it does not inform Government of the total cost of the project across the life of the capability. Net Personnel and Operating Cost is also hard to estimate and often inaccurate. **We recommend this process cease immediately.**

Defence needs to spend more time on defining the cost estimates and presenting a total project cost for both acquisition and sustainment. The costs should be independently assured before being presented to Government to ensure appropriate rigour and fidelity. Our proposed approval process will also make accountability for project delivery clear (to specification, on schedule and on budget), with management of consequences an essential feature of the new performance management culture (see Chapter 5).

61 Interviews with members of the Independent Project Performance Office.

Defence Investment Plan

The Defence Capability Plan as a management tool is problematic as it focuses on capital equipment only and is seen generally as a ‘shopping list’⁶² of projects requested by the Services. It is too easy to get a project onto the Defence Capability Plan as the Force Structure Review process is irregular and not appropriately contested. **We recommend development of a Defence Investment Plan which would include all capital and related investments (such as materiel, estate and facilities, workforce and information and communications technology).**

This plan should be reviewed annually, as part of the planning process, and would be a vital part of managing capital trade-offs and prioritising all capital projects across the portfolio. A version of this plan should be made available to industry to enable appropriate planning for future capital projects. Defence must ensure that the Defence Investment Plan includes costing for all the Fundamental Inputs of Capability to bring them into service and not just the materiel element.

Currently Defence over-programs the Defence Capability Plan to ensure money is spent when schedule slippage occurs. We acknowledge that the Defence capital budget is not easily reduced to predictable annual budgets and is subject to fluctuations because of urgent operational requirements, foreign currency risks and uncertainties associated with large developmental projects. Therefore, over-programming is understandable but should be contained to the portfolio level to defray the risk of a budget underspend, managed carefully by the Secretary with information provided via a transparent process to central agencies.

Defence also utilises cost slippage as a budgeting tool due to the Defence Materiel Organisation being historically unable to expend all allocated funding. In practice, a percentage of the acquisition budget is initially withheld from the Defence Materiel Organisation which means at the start of an acquisition project they do not have their total planned budget.

This practice is inconsistent with a smart buyer construct and holding people to account for delivery. **We recommend that, on Government approval, the entire project acquisition budget is allocated to the Capability Acquisition and Sustainment Group to ensure expenditure is in accordance with the project delivery plan.**

Defence Science and Technology Organisation

The Defence Science and Technology Organisation is valued by Defence and national security agencies for its contribution to saving lives, reducing risk, saving money and enhancing capabilities. It provides a range of specialised and technical services across both Defence and the national security community and has developed state-of-the-art technology that is being used across the world today.

We were advised that the Defence Science and Technology Organisation has been on a reform journey for a number of years. Despite a significant reduction in personnel and resources, it has continued to provide the required services to its customers. There are numerous examples of the efficiencies gained and money saved through its work across Defence.⁶³

Whilst we acknowledge that good work is being undertaken by the Defence Science and Technology Organisation, it struggled to articulate clearly to the review team the value that it contributes to Defence outcomes. **We recommend that the Defence Science and Technology Organisation be required to clearly articulate its value proposition. This would include examples and actual amounts of value created.**

We acknowledge that around 80 per cent of the Defence Science and Technology Organisation work is conducted in support of capability projects. As the Defence Science and Technology Organisation is largely a capability enabling group, **we recommend that it become part of the Capability Acquisition and Sustainment Group.**

⁶² The shopping list description refers to the ease with which projects can be included in the Defence Capability Plan and the fact that once a project is in the plan, it will be acquired regardless of any other factor.

⁶³ RJ Trenberth, *Review of DSTO's External engagement and contribution to Australia's wealth*, Defence Science and Technology Organisation, 2004, Canberra; interviews with stakeholders; and DSTO submission to the First Principles Review.

The structure of the Defence Science and Technology Organisation is top heavy with three Senior Executive Service Band 3 equivalent positions and 14 Senior Executive Service Band 2 equivalent positions. **We recommend the Defence Science and Technology Organisation senior leadership be rationalised.**

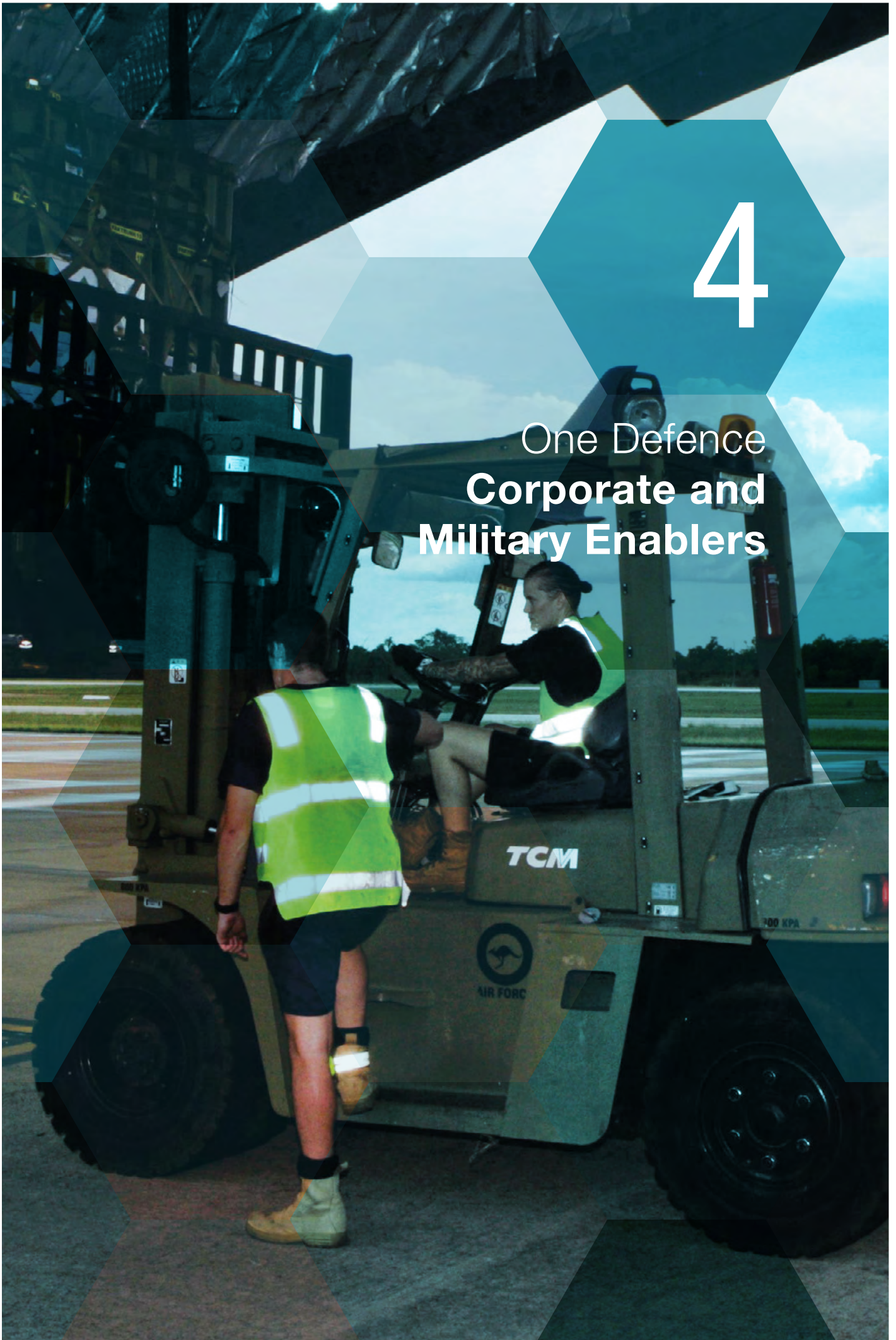
On the information considered during the review, there is no clear case for outsourcing the Defence Science and Technology Organisation and, in fact, this approach may be detrimental to the support it offers to Defence and its other customers.

Whilst wholesale outsourcing would not be wise, there is more opportunity to outsource elements to the broader scientific community, particularly in industry and academia. **We recommend that strong partnerships be established with key academic and research institutions to leverage the knowledge of scientists and create pathways into and out of academia and industry.** In this context the Defence Science and Technology Organisation Advisory Board is not required and **we recommend that it be disbanded.**

The Chief Defence Scientist should examine the methodology utilised to prioritise blue sky research versus the applied research program. The Defence Science and Technology Organisation has a niche role to play in a much larger global scientific research program and it is vital that its blue sky research focuses on matters of special relevance to Australia. **We recommend that Defence, in partnership with academia and industry, review its developmental research priorities, their alignment with future force requirements and capacity to leverage allied partners, in order to promote innovation and make the most valuable contribution to future Defence capability.**

4

One Defence Corporate and Military Enablers



Key Recommendation 3

Fully implement an enterprise approach to the delivery of corporate and military enabling services to maximise their effectiveness and efficiency

The evolution of an enterprise approach to the delivery of both corporate and military enabling services in Defence has been slow and hard-fought. The panel views this with concern. It is again a symptom of a federated business model resisting a **One Defence** approach. We acknowledge that these reforms have struggled because Defence does not yet have the service delivery ethos required of a large operational organisation, and when there are budgetary pressures, the enablers are the first to lose funding. This volatility drives reactive management practices focused on short term fixes which result in longer term opportunity costs and delivery risks.

The enablers are critical to the effective and efficient delivery of capability. Moving to a **One Defence** approach will require further consolidation and standardisation especially in estate, information management, geospatial intelligence and customer-centric service delivery.

Defence Estate

The **One Defence** estate needs to be clearly aligned to current and future capability and force posture requirements. It must meet the requirements of the Services and enabling workforce in the most efficient way. The estate requirements increasingly need to take into account the common and integrated needs of the three Services.

Current State

The Defence estate is a critical enabler of the country's defence capability and supports the generation and sustainment of the Australian Defence Force. It includes bases, training areas and ranges, training institutions, research and development facilities and airfields and wharves to launch operations. It is the largest land holding in Australia (over three million hectares) with 75 major bases and has a gross replacement value of \$68 billion.

Key issues with the current estate portfolio are that:

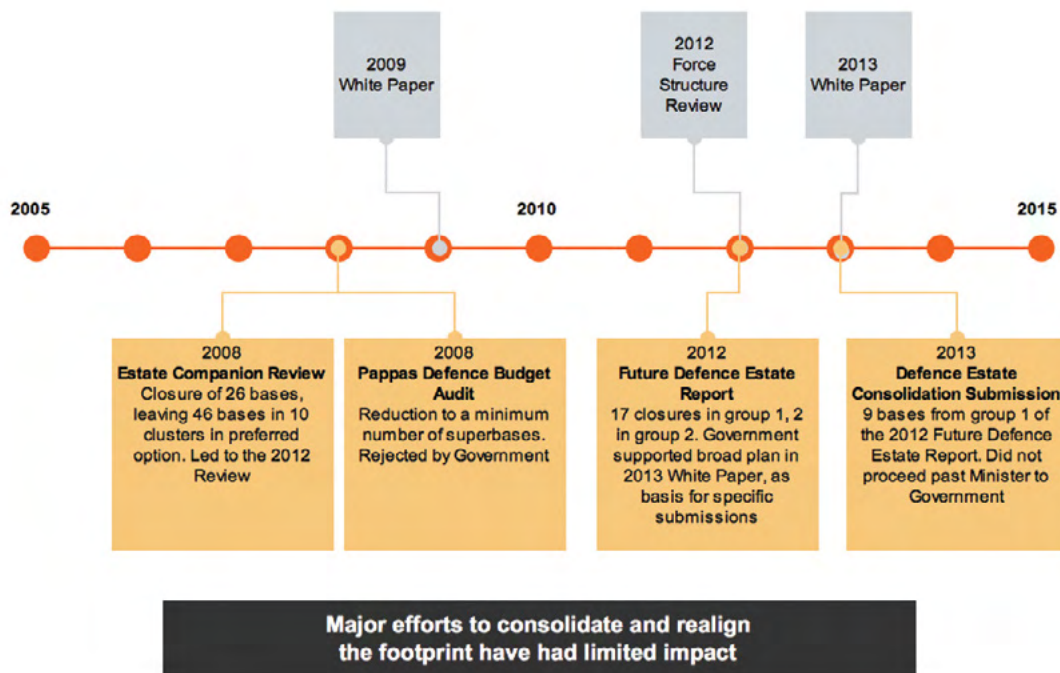
- The current footprint does not align with current and future Australian Defence Force requirements. It has largely evolved over time, is a product of history, much of it now redundant, and in some cases is boarded up to avoid use and minimise maintenance costs;
- There is insufficient funding to maintain the current footprint and the remaining useful life of the estate has reduced from 22 to 16 years since 2001 because of under-investment;⁶⁴
- Defence is now caught in an unsustainable cycle of insufficient funding to maintain the current estate footprint. This leads to deterioration in quality, diversion of a growing proportion of funds to non-value adding maintenance and health and safety compliance, which further exacerbates deterioration of the estate. This cycle is progressively increasing risk, adversely impacting capability and preparedness, diverting funding from investment in the future and making future investment initiatives more difficult;⁶⁵ and
- Improvements in Defence management processes, sourcing and investment prioritisation have proved insufficient to break this cycle.

64 Analysis of Defence data, December 2014. See also Australian National Audit Office, Performance Audit Report no.41 2010–11, *Maintenance of the Defence Estate*, pp.11, 62, available at <www.anao.gov.au/Publications/Audit-Reports>.

65 Department of Defence (prepared by AECOM Australia Pty Ltd.), *The Future Defence Estate Report Volume 1 Executive Summary*, Canberra, November 2012.

Significant consolidation and realignment of the estate is needed, as has been identified in numerous reviews (see Diagram 8). Despite identifying opportunities for consolidation, repeated efforts by Defence to reduce and realign the footprint have proven to be complex and difficult with little success.⁶⁶

Diagram 8: Previous reviews identified opportunities for consolidation



For reasons of history and legacy, releasing parts of the estate can be hard for the Services despite indications from Australian Defence Force leadership that it is supportive of a major rationalisation. More importantly, the failure to consolidate the estate has been a product of political intransigence by governments of both persuasions over many decades, with numerous consolidation proposals from Defence not receiving endorsement to proceed. Even the current base-by-base consolidation approach rarely gains endorsement⁶⁷.

Existing opportunity

Through the 2012 Future Defence Estate Report, Defence has already identified 17 sites (out of 75 major bases) for closure and disposal.⁶⁸ These closures would not affect current operational capability or future needs and would lead to a more strategically and functionally aligned estate as well as improved financial sustainability.

A conservative net present value estimate of the disposal of these sites over 30 years is \$1.4 billion, including property sales at a market value of \$570 million, of which a bare minimum of \$210 million would accrue in the first 10 years.⁶⁹ This net present value estimate also includes the cost of remediation but does not include future maintenance savings.

⁶⁶ Department of Defence, *Estate Companion Review, A Strategic Framework for the Defence Estate*, Canberra, 2008.

⁶⁷ Interviews with stakeholders.

⁶⁸ Advice from Defence Infrastructure Division, December 2014.

⁶⁹ Analysis of data provided by Defence Infrastructure Division, December 2014.

Our requests for Defence to quantify the market value of its land holdings led to this very conservative net present value estimate which in our opinion has been developed in isolation, without consideration of commercial opportunities or consultation with other potentially interested parties.

In our view, this proposal has not been optimised for speedy realisation of commercial opportunities. It suggests limited awareness of the potential value of Defence's properties and the commercial interest in some of its key metropolitan sites. This is puzzling given that the Government has recently provided Defence with a significant incentive to dispose of unnecessary estate by allowing it to use the proceeds of sale for Defence purposes.

Alternative uses for surplus Defence sites in metropolitan areas can be economically beneficial, for example, allowing development of residential and commercial spaces. Much of the land is prime real estate, which makes disposal more compelling from a taxpayer viewpoint. As most of these sites are underutilised, contemporary redevelopment would also help promote the Government's national productivity, employment and infrastructure goals.

While we understand the political sensitivities associated with estate disposal, we do not accept this as an excuse to allow the ongoing waste and inefficiency associated with keeping estate that is surplus to Defence requirements.

Transforming the Defence Estate

A radical change in approach is now required for estate consolidation and realignment and for obtaining government approval. This will pave the way for a smaller, more efficient and more strategically aligned estate footprint.

We recommend that Defence define the estate need as determined by future force requirements and that Government agree to dispose of all unnecessary estate holdings starting with the 17 bases identified in the 2012 Future Defence Estate Report.

There needs to be a clear link between capability, future force needs and estate requirements (including timing, location and cost). This link will emerge from the White Paper 2015, Force Structure and corporate planning processes. Under the **One Defence** business model, the strengthened role of the Vice Chief of the Defence Force in future force design should include the articulation of force posture requirements. The estate must be managed so that it can be invested in, sustained, and disposed of as enduring future force requirements dictate.

The First Principles Review high level implementation plan recommends a process to get the estate rationalisation started. It provides a timeline to make ready and sell the unnecessary parts of the estate that are surplus to requirements. Noting that proceeds from sales will be available for reinvestment, Defence needs to be able to clearly explain to the Government and community the reasons parts of the estate are no longer required and the benefits to the nation of investing in other Defence priorities. **We recommend that Defence strengthen its capability to present options to Government for estate disposal including obtaining expert external advice as required.**

Defence will need to consider further rationalisation beyond the current 17 identified sites. This rationalisation should balance the interests of Defence, community, local government and economic development, and include a mix of sites in terms of commercial attractiveness and political sensitivity. As part of this approach, Defence will need to create an open dialogue with the community to explain the future Defence estate needs and the case for consolidation.

We have been advised that current approval processes for infrastructure projects can add significant time delays. Consolidation, disposal and reinvestment in Defence infrastructure routinely requires the consideration and approval of the Parliamentary Standing Committee on Public Works.

Since 2006, the infrastructure projects forwarded by Defence for the Committee's consideration have increased both in number and in value. For instance, in 2014, the Committee approved expenditure of \$1.5 billion on facilities to support the Joint Strike Fighter, and Defence expects to manage between 150 and 200 major capital facilities and infrastructure projects each year for the next decade.⁷⁰

⁷⁰ Data provided by Defence Infrastructure Division, October 2014.

Under current arrangements, projects with a value of \$2 million or more are notified to the Committee with a request to proceed as medium works,⁷¹ while works valued at \$15 million or more must be referred to the Committee for consideration and report to the Parliament before work can proceed.⁷²

The present thresholds of \$2 million for medium works and \$15 million for major works were last revised in 2010 and 2006 respectively. They do not align well with thresholds for the approval of military equipment, so that more extensive consideration may be required for the approval of facilities works of a lower value than the military equipment they are intended to support. The present thresholds add more than a month to the time required to commence medium works, and three to six months to the time required to commence major works.⁷³

In order to improve procedural efficiency **we recommend that the Government amend the *Public Works Committee Act 1969* to set a \$75 million threshold for referring proposed works to the Public Works Committee, and reconsider recent adjustments to the 2015–16 Budget operational rules that run counter to more efficiently managing investment spending.** These are further constraints that should be removed as their removal would reduce overhead, cost and delays to infrastructure projects.

Information Management

Information management is a critical enabler for **One Defence**. In the military environment, information management must provide the war fighter with common battlespace awareness and information superiority through integrated and interoperable information. It underpins the next generation of Command, Control, Communications, Computers, Intelligence, Surveillance and Reconnaissance (C4ISR) systems, and links sensors and weapons platforms. It is crucial to offset the relatively small size of the Australian Defence Force and enable a competitive war fighting advantage over Australia's adversaries.

Within the corporate arena, information management must enable the organisation to make informed decisions, measure performance, provide timely, credible, traceable and relevant management information, and support enterprise-wide business processes. It must be underpinned by a trusted single source of enterprise-wide data, and to the extent possible, common and standardised applications and infrastructure.

Current State

Information management has been a persistent challenge for Defence and has been identified as an issue in numerous reviews of the organisation. Previous projects and approaches have been unsuccessful in driving the required information management outcomes and it is apparent that current practices are materially impeding operational effectiveness and efficiency.⁷⁴ Defence's information management needs are not being met and this will only be exacerbated as innovations in technology and technologically advanced Defence capabilities (for example, the Joint Strike Fighter) further raise the bar for information management capabilities.

We have been furnished with examples of inadequate interoperability between and within military platforms that impact on operational effectiveness.⁷⁵ Similarly, there are significant shortcomings in the corporate arena that limit Defence's ability to make fast well-informed decisions and maintain information security protocols which may result in failure to meet legislative and regulatory compliance.⁷⁶

71 See paragraph 1.31 of *Procedure Manual: Parliamentary Standing Committee on Public Works (8th edition)*, March 2010, available at <www.aph.gov.au/Parliamentary_Business/Committees/Joint/Public_Works>.

72 See s. 18(9)(a) of the *Public Works Committee Act 1969*, as amended.

73 Data provided by Defence Infrastructure Division, October 2014.

74 Air Vice Marshal John Blackburn (rtd), <http://www.sldinfo.com/an-australian-perspective-on-the-way-ahead-for-a-pacific-strategy/> [accessed 18 February 2015].

75 Defence classified briefing materials provided to the review team regarding air, land and sea platforms.

76 Briefing materials provided to the review team by the Chief Finance Officer and Chief Joint Logistics on accounting and inventory systems.

Inefficiencies and waste are evidenced by a costly and complex application landscape that limits flexibility and ‘locks’ data into systems. As noted in Chapter One, the Chief Information Officer stated that Defence has over 2500 applications, including 300 financial applications.

While the Department’s intent has been to make the Chief Information Officer responsible for information management across Defence, in practice accountability has remained fragmented and unclear. There has been a lack of effective governance and control which has led to siloed solutions, especially in the military arena where the Chief Information Officer Group has less domain expertise and is further removed from the end user.

Transforming Information Management

Remediating and transforming information management in large organisations is inherently messy. In making our recommendations, we are mindful of getting the governance right and gradually building interoperability, compatibility and simplicity over time.

The information management agenda must be driven from the top with the Secretary and the Chief of the Defence Force as champions, with clear authority across Defence delegated to the Associate Secretary to oversee robust and effective governance processes.

To ensure military interoperability, a C4ISR design authority, reporting to the Vice Chief of the Defence Force, should be put in place to define the warfighting environment and architecture, and set military interoperability requirements.

We recommend that the Associate Secretary be directed and resourced to implement enterprise information management that provides Defence with trusted information to inform decision-making and military interoperability, with the Vice Chief of the Defence Force as the design authority for C4ISR.

We also recommend that the information management agenda be governed at the Band 3/3 star level by the Enterprise Business Committee to set overall direction and priorities, including the management of trade-offs and conflicts.

As directed by the Associate Secretary, the Chief Information Officer’s responsibilities would be to implement the enterprise information management agenda and be the authority for all enterprise networks. The Chief Information Officer would authorise all information management expenditure as a part of the planning cycle.

The technical authority for enterprise information management frameworks including architecture, standards, policy and master data management must reside with the Chief Information Officer. Responsibilities would include the mandate to stop projects — corporate or C4ISR — that do not comply with interoperability standards or, under exceptional circumstances, escalate decisions to the Enterprise Business Committee as the governance forum for information management. **We recommend supporting the Chief Information Officer to meet these responsibilities by formally recognising the Chief Technology Officer as the technical authority with appropriate ‘red card’ decision rights.**

Defence should establish a number of foundational information management building blocks to implement **One Defence** frameworks for architecture, standards and master data management.

Accordingly, we recommend that Defence establish enterprise-wide frameworks for architecture standards and master data management.

We also recommend that Defence embark on a pragmatic implementation road map to standardise business and information processes and their supporting applications.

This will necessitate a move over time to a small number of standardised information and communications systems supporting enterprise-wide processes and a radically simplified application landscape through retiring legacy solutions and adopting enterprise master data.

We note a number of domain-specific information management reform programs are already under way or planned in Defence. These must be aligned and leveraged under the new model including the human resource management and payroll system, the garrison and estate management system, financial information system reform, and logistics system modernisation. The Chief Information Officer will have to ensure that all of this work is consistent with the information management transformation agenda.

We recommend that Defence ensure adequate resourcing and funding for information management reform is prioritised as part of the fully costed 2015 Defence White Paper.

Geospatial intelligence

The Terms of Reference make particular reference to geospatial intelligence. We note that an external provider has conducted two reviews with the findings presented to the Defence Committee which was unable to make a decision about implementing the recommendations. This in our view is an example of Defence being unable to make decisions that are in the best interest of the enterprise as a whole.

Current State

Defence does not have a unified geospatial information enterprise. It has a series of stand-alone organisations that collect, analyse, maintain and distribute single domain foundation geospatial information. They have separate systems, business models, workforce planning, internal governance and capability development processes — all operating with little reference to each other or to a coherent plan for collective action.⁷⁷

Geospatial information management is currently under-resourced, with poorly coordinated investment, limited leadership, obscure accountability, low management prioritisation and disaggregated thinking about strategy and direction.⁷⁸ Current, planned and future Australian Defence Force platforms and operations are all critically reliant on integrated geospatial data and services. The remediation of this key enabler is urgent.

Transforming geospatial intelligence

The systems necessary to deliver these geospatial intelligence services are complex and operate at very high security classifications. They will only deliver the required services to the war fighter at the right time through greater integration of the associated production and distribution systems and stronger professional linkages between the maritime, land, and aerospace geospatial intelligence domains.

Stronger linkages with the Australian Geospatial-Intelligence Organisation would lead to more effective geospatial intelligence support for war fighter operations and would add significant expertise to the Australian Geospatial-Intelligence Organisation.

Strengthening the Services' linkages with the Australian Geospatial-Intelligence Organisation should be achieved through the adoption of more effective information and communication systems and appropriate secure facilities. Service geospatial intelligence staff should be further embedded with the Australian Geospatial-Intelligence Organisation, and vice versa, to provide direct input to the geospatial picture, supported by an array of broader products from the intelligence community.

We note that the Services' geospatial intelligence workforce is currently based outside Canberra so 'virtual' embedding will be needed for some time. A more holistic integration into a single agency would realise greater efficiencies and productivity.

We see, therefore, the urgent need for the Australian Geospatial-Intelligence Organisation to have more central control of connectivity and resourcing of the broader virtual Defence geospatial enterprise. Like Defence's United

⁷⁷ Department of Defence (prepared by KPMG), *Geospatial Enterprise Review Phase 2 Final Report*, September 2014, p. 8

⁷⁸ Ibid., page 5.

Kingdom and United States counterparts in this area, moving to a single agency offers Defence the best model for the provision of geospatial information and services into the future.

We recommend that geospatial information functions be consolidated into the Australian Geospatial-Intelligence Organisation following improved resourcing and connectivity.

Service Delivery Reform Program

The renewed focus on developing a service delivery system within Defence initiated by the Secretary and Chief of Defence Force in April 2014 is acknowledged, particularly as it recognises that previous approaches to implementing shared services have not worked well.

We also note the whole-of-government agenda focused on the implementation of shared services. Defence is expected to align with this approach and be subject to external scrutiny of outcomes and performance by a public service wide governance board.

Current State

Notwithstanding the intent of the work Defence is doing in this area and the whole-of-government agenda, we remain concerned by:

- The limited ability of some areas to deliver on the true intent of a customer-provider model. Human resources provided by Defence People Group is an example of this: users have implemented workarounds and employed their own human resource staff because of the Group's inability to deliver;⁷⁹
- The resistance of some leaders to accept the shared service model;⁸⁰ and
- The reluctance to empower single accountable officers in such areas as information management, public affairs and finance.

It is critical for the development of the **One Defence** system that the shared services model is fully implemented. This will mean standardising services, removing duplication of functions, professionalising the workforce and ensuring there are single, clear lines of ownership and accountability.

Defence lacks a service delivery culture. This manifests itself in providers and customers not appropriately negotiating with each other, enabling functions not providing responsive services and customers duplicating functions as they do not believe they will get the required services.

Senior leaders within enabling services must address this issue by ensuring their functions have the capability of a third party external provider. Customers have to work in good faith with the providers to ensure the model is implemented in the best way to achieve the agreed outcomes for the enterprise.

We have not had sufficient time to analyse the transactional work being done in Defence. Our experience, as well as others we have spoken to, suggest that routine administrative transactions such as travel, accounts payable and computer support involve unnecessary dense manual processes and rework. Poor processes have clearly been established and inefficiencies abound. Such transactional work, especially when it is poorly done, is a distraction from the Defence mission.

79 Briefing materials provided to the review team as part of the Internal Reform Program analysis.

80 Chief Executive Officer, Defence Materiel Organisation, correspondence to Defence Chief Finance Officer, 24 October 2014.

Transforming Service Delivery

Consistent with the **One Defence** model, **we recommend that the service delivery reform program, including full integration of the current Defence Materiel Organisation corporate functions, be completed.**

We recommend that all corporate services (with the exception of finance but including the Defence Security Authority) be consolidated under the Associate Secretary. This would involve:

- Specialist leads (for example human resources, information and communications technology, public affairs and communication) providing policy, standards, evaluation and assurance;
- The human resources model doing strategic rather than transactional work as this is central to achieving the cultural change required for delivering **One Defence**. The human resources lead role should define the strategic human resources framework for Defence including policies and strategic workforce plans (see Chapter Five). The line areas would be responsible for managing their workforce within this framework. Human resources staff should have primary accountability to the line managers with links back to the central human resource role;
- All other enabling areas being connected to the centre but having a structure in place to support their customers throughout the department; and
- Transactional services being consolidated and outsourced. Quality assurance systems should be put in place to measure the performance of external service providers. Where transactional work remains in house, quality assurance systems should also be put in place.

We recommend that all military enabling services (Joint Logistics Command Policy, Joint Health Command, Australian Defence College, Australian Civil-Military Centre) be consolidated under a two star officer reporting to the Vice Chief of the Defence Force.

This consolidation under a two star officer will allow the Vice Chief of the Defence Force to focus on the new future force and joint responsibilities as well as the military enablers. We are confident that the span of command and disparate responsibilities can be appropriately aggregated under a single officer. It is our view that the Joint Health position should remain at the regular two star level and the Reserve position should be retained at the reserve two star level.

5

One Defence **Workforce**



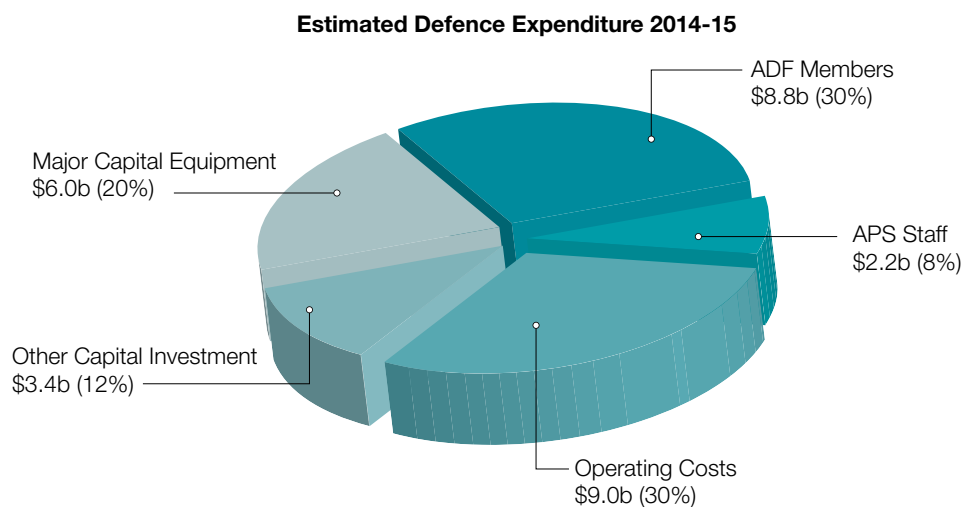
Key Recommendation 4

Ensure committed people with the right skills are in appropriate jobs to create the **One Defence** workforce

Overview

The diagram below shows the major elements of Defence's \$29.4 billion budget for 2014–15. Employee expenses are estimated at \$11.0 billion. Australian Defence Force personnel (a permanent force of more than 57,000) will cost \$8.8 billion or 30 per cent of the Defence budget. Defence public servants (an enabling workforce of 19,400) will cost \$2.2 billion or 8 per cent of budget.⁸¹

Diagram 9: Major elements of Defence's budget



The proportion of employee costs relative to capital and operating costs is strongly influenced by the ebb and flow of funding for major capital equipment. For instance, current estimates put employee costs at 37.5 per cent of the budget and capital at 32.0 per cent, reflecting government decisions made in previous years to defer capital expenditure.

However, by 2018–19, employee costs are forecast to fall to 35.0 per cent as deferred capital expenditure resumes. The employee, capital and operating costs will and should continue to fluctuate with strategic priorities. The prime consideration is whether these proportions reflect the most effective and efficient use of funds to support current and future force requirements.

⁸¹ Department of Defence, *Portfolio Additional Estimates Statements 2014-15*, Canberra, 2015, pp. 21-22.

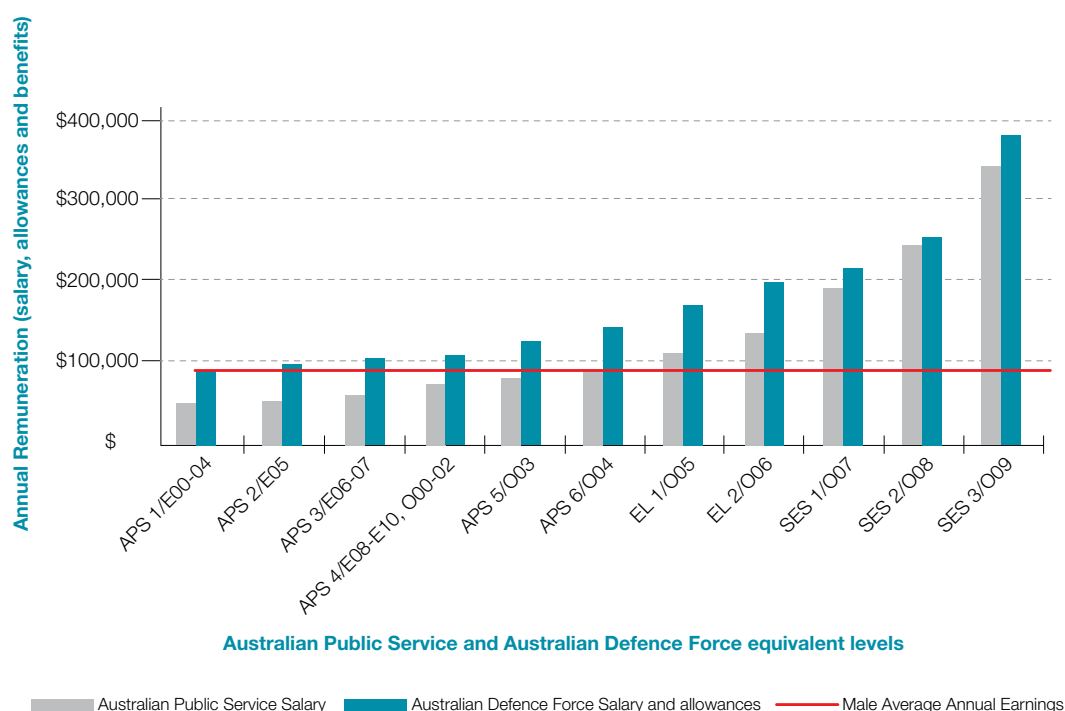
Defence's enabling workforce

The work of the Navy, Army, Air Force and Joint Operations Command is enabled by a workforce of 23,700 people employed mainly in the non-Service groups, including the Defence Materiel Organisation. It comprises 19,400 public servants, 4300 Australian Defence Force personnel and 350 employees contracted into Defence.

The total direct employment cost of Defence's enabling workforce in 2013–14 was \$3 billion. \$2.3 billion of this was incurred in respect of public servants (approximately \$110,000 per employee) with the remaining employee costs borne by the Services (approximately \$180,000 per Australian Defence Force member). Rates of remuneration are illustrated in Diagram 10 which demonstrates that:

- Including basic allowances, the average annual remuneration of Australian Defence Force personnel is some 30 per cent higher than the equivalent public servant;⁸² and
- Defence public servants at the Executive Level 1 level or higher are paid above the national average, as are Australian Defence Force personnel at all but the junior ranks.⁸³

Diagram 10: Australian Public Service and Australian Defence Force equivalents



82 In addition to basic pay, Australian Defence Force members receive allowances in respect of their service as well as assistance with housing and health costs, see Department of Defence, *Annual Report 2013–14*, vol. 2, p. 38, available at <www.defence.gov.au/annualreports/13-14/>.

83 The table of APS and ADF equivalent ranks is at Annex F. ADF remuneration in Diagram 10 includes Service and Uniform Allowances only. Male Adult Total Average Earnings (the generally accepted wages benchmark) are from the Australian Bureau of Statistics, cat. no. 6302.0, May 2014, available at <www.abs.gov.au/ausstats/abs@.nsf/mf/6302.0>.

Significant additional numbers of people are employed by external providers delivering contracted services to Defence, including:

- An estimated 27,000 people employed by industry to deliver inputs to capability, including major military equipment; and
- Several thousand staff employed by contractors to maintain and secure Defence bases.

Defence's public servants are the most likely, of all Commonwealth agencies, to have only ever worked in one agency (Defence), and the most likely to have been promoted only within Defence. One in four Defence public servants come from the Australian Defence Force, on a path of lifetime employment spanning enlistment, Australian Defence Force service, movement to the public service and, finally, age retirement. It is a cradle to grave model which is not without its benefits. However on balance we would contend that this insular approach and lack of diversity contributes to the inability of Defence to change.

Because it has such a large workforce delivering a wide range of services in support of the Australian Defence Force, it is vital that Defence drives inefficiency, duplication, redundancy, poor fit for roles and mediocre performance out of the organisation.

A plan to deliver a professional workforce

While the Navy, Army and Air Force have detailed workforce plans, Defence does not have a strategic workforce plan for its enabling workforce. Without it, Defence struggles to identify skills gaps across the agency and place the right people with the right skills in the right roles at the right time to deliver Defence's mission.

A strategic workforce plan is a necessary prerequisite for building a highly professional workforce with the necessary skills and balance of public servants and Australian Defence Force personnel. Defence has made slow progress since its first attempt in 2010 to outline overall workforce challenges and opportunities. Some groups have developed workforce plans of varying maturity and detail. As recently as 2013, Defence started classifying its enabling staff by job family and identifying their learning and development requirements.

However, on the whole, efforts have been piecemeal, inconsistent and focused on the number of budgeted staff and roles, rather than the skills required today and in the future. The fact that Defence does not systematically collect, store and update comprehensive information on the skills of its enabling workforce is a major failing.

As a consequence, Defence lacks the necessary skills to achieve its mission in some areas. Defence leadership has recognised this issue and in November 2014, conducted its first assessment of public service workforce skills gaps. This highlighted critical shortages in job families such as engineering and technical and project management. A June 2014 internal audit of the Defence Materiel Organisation's engineering and technical workforce concluded that:

The state of the Defence Materiel Organisation's Engineering and Technical workforce is a risk to Defence capability. Defence Materiel Organisation has limited visibility of their workforce skills. Defence Materiel Organisation has no targeted strategies for attraction and retention of the right skills and resources required for future capability. Defence Materiel Organisation has no ability to model engineering and technical workforce requirements for the future. It appears that [Defence People Group] does not support Defence Materiel Organisation's strategic workforce management program as they do not have clarity from Defence Materiel Organisation on what workforce gaps they have in relation to skills, experience, qualifications and diversity.⁸⁴

⁸⁴ Ernst and Young, *Internal Audit of the Professionalisation of Engineers (2013/14 No. 6) Final Report*, Defence Materiel Organisation, Canberra, 23 June 2014, p. 5.

We recommend that, as part of the budget and planning process, Defence build a strategic workforce plan for the enabling functions, and incorporate workforce plans for each job family in order to drive recruitment, learning and development, performance and talent management. We envisage Defence will require professional assistance to complete this large task.

This strategic workforce plan should:

- Be based on job families and functions as they are refined, with lead responsibility allocated to job family sponsors;
- Forecast the supply and demand for particular skills;
- Identify skills surpluses or shortages across the whole organisation and reallocate resources accordingly;
- Incorporate professionalisation plans and skilling maps, especially for critical job families such as strategic policy, engineering, maintenance and logistics, procurement and contracting, and program/project management;
- Locate parts of the business in places other than Canberra to help attract the required skills;
- Be informed by a census of the current skills and qualifications of the enabling workforce; and
- Incorporate targets for recruitment, learning and development, talent management and career planning that are reported to and tracked by the Defence Committee.

It is imperative that Defence develops this strategic workforce plan and aligns its human resources activities, updating these annually to ensure they continue to reflect Defence needs. Combined with the development of effective career paths and performance management, the skills and professionalisation of Defence's enabling workforce will be enhanced.

The role of Australian Defence Force personnel

There are 2400 public servants currently assigned to Navy, Army, Air Force and Joint Operations Command, where they carry out non-military duties that would otherwise be done by Australian Defence Force personnel. One reason for this is because it is cheaper to use public servants than Australian Defence Force personnel.

Australian Defence Force personnel incur a cost premium. This comes from the extensive support Australian Defence Force personnel are provided in order to train for and execute their duties. There are also financial benefits they receive in compensation for the arduous nature of those duties and the impact that military life has on their families.

At almost every rank, Australian Defence Force personnel are more expensive than their public service equivalents. Therefore, as a value for money proposition with the efficient use of Commonwealth funds in mind, it makes sense to only utilise Australian Defence Force personnel in roles that cannot be done by a public servant.

Currently, there are more than 4300 postings of Australian Defence Force personnel to non-Service groups. This costs around \$300 million annually over and above what it would cost to fill the roles with public servants. These postings are made for three main purposes:

- To bring to bear military specialist knowledge and experience (such as helping develop a proposal for new military equipment);
- To train Australian Defence Force personnel in tasks that are necessary for their career development; and
- To provide respite from Australian Defence Force duty (for example, shore duty after being at sea).

We learned that the basis for the numbers of Australian Defence Force personnel posted from each Service are largely historical. The numbers of billets in non-Service groups were broadly set some years ago. While some posting billets fill the need for specialist skills, most placements are less critical to the effective operation of the enabling workforce.

Typically, Australian Defence Force personnel spend the first year of their posting learning the job, the second year-and-a-half performing in the job, and the final six months transitioning to the next job. This relatively short rotation adds more inefficiency and cost especially if it is a poor fit for role.

In addition to the deleterious impact on the enabling workforce, it begs the question of whether the current posting arrangements actually provide best value to the Australian Defence Force, and whether the goals of training and respite can be better achieved in some other way.

We recommend that Defence employ Australian Defence Force personnel in non-Service roles only:

- **When it is critical to achieving capability; and**
- **For a minimum of three years to achieve best value for money from the premium paid.**

Overlap and redundancy

In the course of this review, we became aware of overlap between the enabling workforce and the Australian Defence Force's own corporate workforce. This workforce is substantial and at April 2014, included 12,800 Australian Defence Force personnel delivering corporate functions within the Services.

Specific examples include:

- The total logistics and transport workforce of 5700 people comprises 600 Navy, 1900 Army and 900 Air Force staff assigned to movements and logistics, plus 2300 staff in the enabling logistics workforce;
- A legal workforce of nearly 400, with 150 legal staff spread across the Services and another 240 in the enabling workforce;
- 3700 staff in people and human resources-related jobs, of which 2200 are in the enabling workforce and 1500 are spread across the Services;
- 190 Army finance and pay officers in addition to the 1400 strong finance workforce in Defence and Defence Materiel Organisation; and
- Over 900 administration officers in Army in addition to the 2500 in the enabling workforce.

The incidence and scale of overlap and redundancy (paying 30 per cent more for Australian Defence Force personnel) is self-evidently inefficient. A proportion of Australian Defence Force personnel are carrying out tasks that could be more cost effectively assigned to a public servant or contractor.

We recommend that as many functions as possible be performed by public servants or outsourced if they are transactional in nature.

There were also instances of overlap within the enabling workforce. We found that:

- the Defence Materiel Organisation had declined to amalgamate its 500 finance people with the 900 finance staff in the rest of Defence to reduce duplicated effort, notwithstanding advice that amalgamation carried scant legal risk;
- Navy and Army had re-established capability development units within their headquarters as a response to the perceived poor performance of Capability Development Group and the Defence Materiel Organisation; and
- Joint Capability Coordination and the Chief Information Officer Group were executing overlapping functions intended to make military equipment interoperable.

Defence struggles to convince its senior managers and staff to forgo their allegiance to their group or Service and instead combine to deliver unified services across the organisation, irrespective of the function. Defence has now embarked, for the second time, on a program of reform to deliver shared services toward a common end rather than bespoke services within silos (see Chapter 4).

The challenge for Defence's management is making optimal use of the public service and Australian Defence Force workforce, the costs of which are, with important exceptions, largely determined by factors outside the direct control of Defence's senior management.

Employee costs require careful management

Consistent with the enterprise bargains that have been agreed with Defence's public servants (in accordance with the bargaining framework set by Government from time to time) and the remuneration tribunal decisions that set Australian Defence Force pay and conditions, the salary costs of Defence's public service and military workforce have largely kept pace with price inflation over the last five years. However, employee expenses have risen above inflation because of:

- 'Automatic' performance pay increments for public servants, due largely to the failure of Defence leadership to apply the existing performance management framework effectively (discussed later); and
- The rising costs of military health, housing and Fringe Benefits Tax allowances.

Australian Defence Force housing costs rose from \$655 million (8.5 per cent of Australian Defence Force employee expenses) in 2009–10 to \$821 million (9.7 per cent of Australian Defence Force employee expenses) in 2013–14. This represents an annual rate of increase of 5.8 per cent per annum, somewhat above the 5.0 per cent experienced by the broader community.⁸⁵

Allied to this has been a continuing increase in Fringe Benefits Tax paid in respect of Australian Defence Force personnel from \$298 million to \$384 million over the same period (6.5 per cent per annum), mainly for rental and housing assistance. Combined, these costs now account for more than 14 per cent of Australian Defence Force employee expenses and their growth is accelerating faster than the community norm, for reasons that are not clear. Given our limited timeframes, this area requires further examination by Defence.

Of more concern are sharply rising health costs, from \$266 million in 2009–10 to \$389 million in 2013–14, increasing at a rate of 9.9 per cent per annum, more than twice the rate of 4.7 per cent per annum experienced by the general community.⁸⁶ The reasons for this are not well understood and are also of concern for the future management of Australian Defence Force workforce costs.

There may be limited scope for Defence to control these costs, which arise as an integral part of the employment offer that attracts and retains Australian Defence Force personnel and their families. It does, however, highlight the real importance of making the best possible use of the military workforce. It is a priority for Defence leadership to revisit and recalibrate practices that detract from efficient use of the Australian Defence Force, including where:

- Australian Defence Force personnel are posted into the enabling workforce;
- Australian Defence Force personnel are executing duties that could, with little modification, be undertaken by public servants or contractors; and
- More efficient use can be made of the posting cycle to reduce the costs of churn.

We recommend that Defence review the entirety of its enabling and military corporate workforce to ensure that it supports the Australian Defence Force with the minimum of overlap and redundancy, and with the greatest overall economy, efficiency and effectiveness.

⁸⁵ Australian Bureau of Statistics, *Selected Living Cost Indexes, Australia*, Housing costs of employee households, cat. no. 6467.0, September 2014, available at <www.abs.gov.au/ausstats/abs@.nsf/Lookup/6467.0Main+Features1Sep%202014?OpenDocument>.

⁸⁶ Ibid., Health costs of employee households, September 2014.

Defence middle management out of shape

Organisations get out of shape over time if left unattended. As noted in Chapter One, Defence has been drifting and has not been reshaped in decades. It is now poorly structured.

There are up to 12 layers in some parts of the organisation, from the Secretary to his front line staff. More than half of all Defence staff are seven or more layers away from their chief manager. This stifles innovation and slows down communication, decision-making and execution. No more than six or seven layers of management is common practice, even in the largest organisations.⁸⁷

Though the management layers are deep, spans of control are surprisingly small for most of Defence's middle managers. There are nearly 2000 managers at the Executive Level 2 equivalent level and they typically supervise three or less staff. There are a further 4000 or so staff at the next level down (the equivalent of Executive Level 1) and they typically supervise only one or two staff. By way of comparison, the benchmarks for this level have middle managers supervising five to eight staff.⁸⁸

Though Defence's middle managers are paid well above the community average (see Diagram 10), four out of five supervise less than a handful of staff, and almost half of the upper rank of middle managers report to another manager of the same rank.

Our analysis has shown that there is substantial work to be done to ensure proper spans of control across all job families. We acknowledge the specialist nature of some work. Defence will always need such specialists — linguists, mathematicians, scientists, engineers, cryptographers and cyber-specialists — who should be retained for their unique expertise and employment practices will need to recognise this. However, specialists are a small part of Defence's middle management cohort.

Narrow spans of control in middle management indicate layers of hierarchy and process that weaken innovation, empowerment and accountability, and encourage micromanagement and underutilisation. They also result in poor career development.

The Defence enabling workforce has also experienced classification creep. The pilot work value review of the Capability Development Group of October 2014 found a significant proportion of staff at higher classifications whose main duties were more suited to lower classifications.⁸⁹ Work value reviews continue and early indications are that over-classification has occurred in other parts of the enabling workforce.

We conclude that significant change is required to the management and structure of Defence's enabling workforce if it is to operate as an integrated entity maximising public value, delivering Defence policy outcomes to Government and supporting the tasks of the Australian Defence Force.

We recommend that Defence:

- **Reduce organisational layers;**
- **Increase the spans of control of managers;**
- **Align workforce standards in accord with the requirements of the Australian Public Service Commission; and**
- **Engage external assistance to facilitate this work as required.**

⁸⁷ Boston Consulting Group, <<http://www.bcg.com/documents/file15242.pdf>>.

⁸⁸ *ibid*.

⁸⁹ Briefing materials provided to the review team in September 2014 identified 58 per cent of the Capability Development Group workforce as incorrectly classified or allocated to tasks suited to lower classifications.

High Performance Standards and Fostering Talent

Performance management is a requirement of all managers and employees in the enabling workforce. Staff develop annual performance agreements in conjunction with their supervisor; clear goals are to be set and recorded, with progress discussed part way through the year and again at the end of the year, when performance is rated. That rating determines whether the employee's salary is increased by the quantum set out in the Defence Enterprise Collective Agreement.

This concept and approach is essentially sound, and if properly executed, performance goals should align with Defence's priorities as expressed in the Corporate Plan. However:

- A sample of performance agreements showed that performance goals are not always clear or focused on outcomes, nor aligned to outcomes and requirements cascaded down from the Secretary to every level; and
- Hard conversations and decisions are not taking place. Performance assessment data shows that in 2014 less than two per cent of staff were rated below satisfactory.

The financial impact has been quantified: over the period 2010–2014, pay increases for pro-forma performance assessments have added to each year's wage bill and now add tens of millions of dollars of expense. The evidence shows that Defence has a sound performance management tool at its disposal, but is not using it effectively.

We view this as a failing of leadership and management. Staff need to be informed of priorities, what is to be done, why it is necessary and how it contributes to the larger Defence mission. Leaders have to set the example through behaviour. Difficult conversations not held are detrimental to the performance of individuals, and to the morale of other staff who see pay increases awarded for underperformance.

Failures of leadership are confirmed by recent survey data that show Defence's public service leadership trailing that of the Services and the broader Australian Public Service in key areas.⁹⁰ There is a disparity between how Defence senior leaders see themselves and how they are seen by their subordinates.

Defence staff reported little confidence in their senior leadership. The leadership was seen as not very effective at leading and managing change and did not appear to be held accountable for their performance.⁹¹ By contrast, Defence senior leadership performance appraisals rated less than one per cent of senior staff as less than effective: more than half were rated 'superior' and one in eight were rated 'outstanding'.⁹²

There are clear grounds for Defence's leadership to reform and strengthen the performance management system to:

- Introduce clear, outcome-focused accountabilities, cascaded down from the Secretary's accountabilities and the priorities outlined in the Corporate Plan;
- Make it more transparent and apply it consistently with normal distribution techniques being incorporated;
- Recognise and reward high performance and team leadership, including by 360 degree appraisal; and
- Apply real consequences for poor performance generally and not dealing with underperformance.

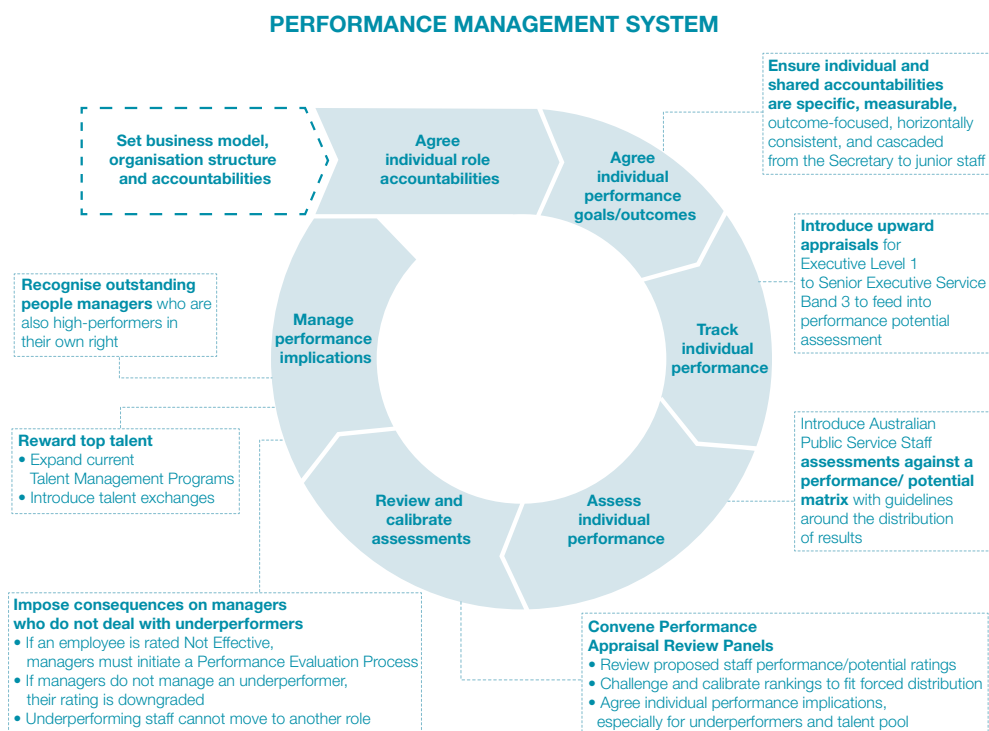
90 Australian Public Service Commission, *State of the Service Report 2013–14*, 2014, available at <www.apsc.gov.au/about-the-apsc/parliamentary/state-of-the-service-2013-14>.

91 Analysis of data from Defence's *YourSay Organisational Climate* surveys of 2013 and 2014.

92 Data provided by Defence People Group.

The review team notes that these reforms will support the statutory requirements of the Australian Public Service Commission that come into effect on 1 July 2015. It is imperative that the elements we have outlined are incorporated as part and parcel of the management of the Defence enabling workforce. **We recommend that Defence implement a transparent performance management system that is consistently applied, recognises and rewards high performance and introduces consequences for underperformance and failure to deal with it.** An example is shown in Diagram 11 below. We have concluded that external assistance is required for a period to catalyse the process and set it on the right path.

Diagram 11: Performance Management System



The outputs of employees in this performance management system are determined by the enterprise plan, cascaded through the organisation. The intended impact of the recommendations is to drive fundamental change to Defence's management and performance culture.

We recommend that as part of the performance management system, Defence take steps to create a culture where leadership, professionalism, and corporate behaviour are valued and rewarded.

6

One Defence Optimising Resources and Dispelling Myths



Key Recommendation 5

Manage staff resources to deliver optimal use of funds and maximise efficiencies

This First Principles Review is focused on optimising Defence as an organisation. In line with our first principles we have recommended that Defence transform from a disaggregated and complex organisation into one that strongly focuses on its core business and outcomes. It must strip back and simplify the unnecessarily complicated processes and structures and introduce greater transparency, contestability and professionalism. These transformations will inevitably lead to efficiencies. We have identified some efficiencies that will arise if our recommendations are comprehensively implemented.

Measuring Efficiency

There are some commonly used efficiency measures in relation to Defence which are either outdated or misleading and not appropriate for measuring the organisation's performance. Better metrics of efficiencies would draw on financial data showing the proportion of funds expended on core functions, outputs or force element. That is, what is spent where in order to achieve the required outcomes.

We recommend that the use of measures such as the teeth-to-tail ratio and the one third budget split, should cease for reasons discussed in detail below. In addition, we recommend that appropriate efficiency measures are developed which link to the delivery of agreed outcomes.

Teeth-to-Tail Ratio

The teeth-to-tail ratio is a widely used⁹³ coarse measure of the administrative overhead of military forces. For instance the National Commission of Audit argues that, 'A simpler and leaner structure is a priority ... A particular focus should be the ratio of the combat force to other personnel (the so called 'teeth to tail' ratio). Defence should develop a programme to improve this over time.'⁹⁴

The National Commission of Audit and other observers interpret higher ratios as indicating a leaner and therefore more effective fighting force. However, the fundamental conceptual and methodological shortcomings of the measure are such that the opposite can be true.

The United States of America, for example, reports declining teeth-to-tail ratios as warfare becomes increasingly mechanised and its armed forces adopt sophisticated technology. This means that United States forces are becoming more effective and efficient as their teeth-to-tail ratio declines.⁹⁵ The Australian experience is that the ratio declines as an effective supply chain grows to support extended periods of operations.

93 See, for instance, S. Gebicke and S. Magid, 'Lessons from around the world: benchmarking performance in Defence', *McKinsey on Government*, no. 5, Spring 2010, pp. 4–13; Major General M. Suman, 'Teeth to Tail Ratio: an archaic concept', *Indian Defence Review*, vol. 21(4), October–December 2006, pp. 71–75.

94 National Commission of Audit, *Towards Responsible Government, The Report of the National Commission of Audit – Phase One*, February 2014, p. 131, available at <www.ncoa.gov.au>.

95 J.J. McGrath, *The Other End of the Spear: The Tooth-to-Tail Ratio (T3R) in Modern Military Operations*, Combat Studies Institute Press, Fort Leavenworth, Kansas, 2007, p. 66.

The teeth-to-tail ratio, while simple, is an unreliable indicator of the effectiveness of the Australian Defence Force or the efficiency of its supporting structures and enabling workforce because:

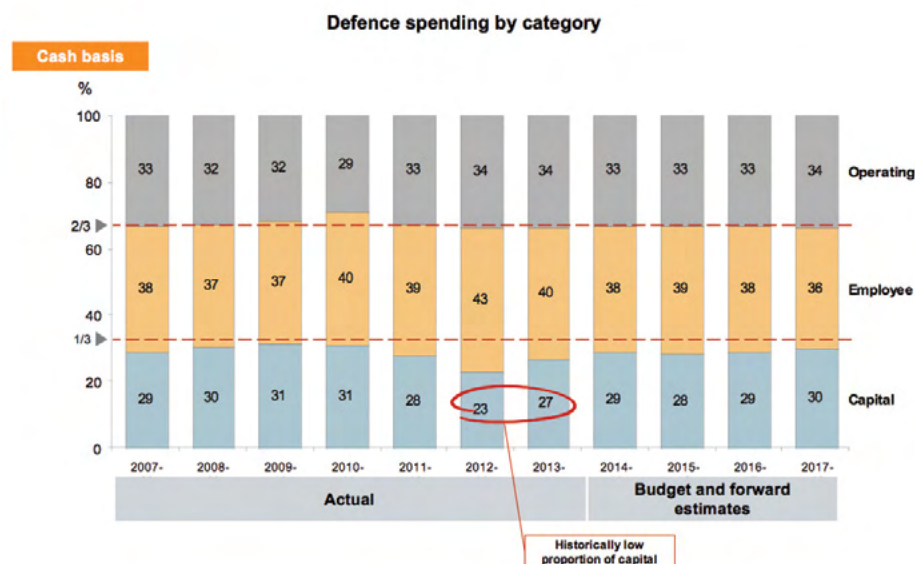
- The ratio can be varied upward or downward by excluding the intelligence and security workforce from the calculations and/or moving other elements of the Australian Defence Force into the tail. The ratio has also declined as armed forces have mechanised, adopted new technology and become more effective;
- It can decline when military positions are civilianised, notwithstanding the cost efficiencies achieved to the overall benefit of Defence;
- It can decline when the more economical and flexible civilian enabling workforce expands to support the Australian Defence Force's requirements making available a greater proportion of uniformed personnel for duties at the 'sharp end'; and
- It can increase when Defence's enabling work is transferred to another entity, commercialised or outsourced to realise an economic benefit, though the number of people funded for enabling work may not change significantly.⁹⁶

One Third Budget Split

Historically, the mix between capital, operating expenses and employee costs has been relatively constant at one third each. This seems to be a coincidence rather than any considered strategy or acknowledgement that the one third split is the optimal mix of budget expenditure.

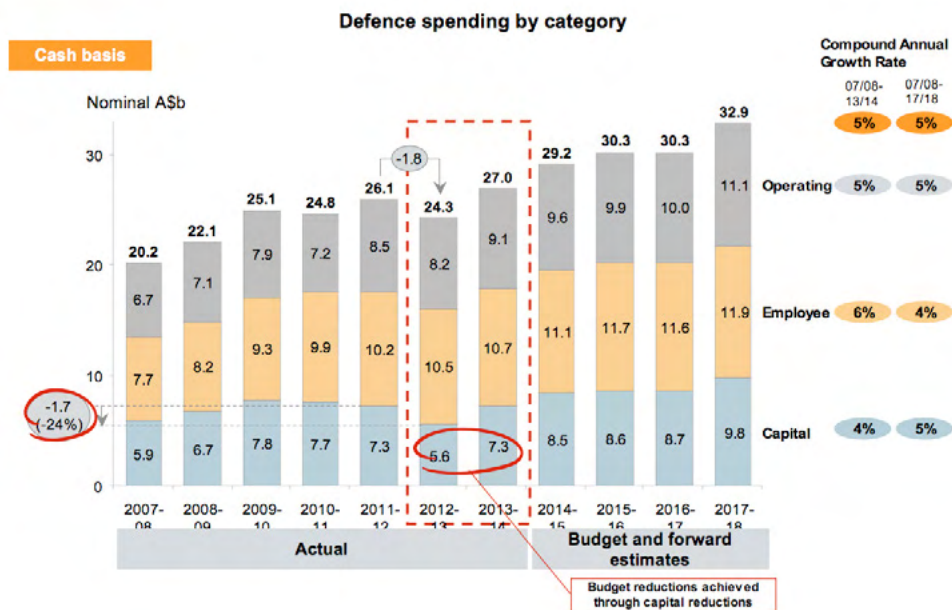
In more recent years, there has been a reduction in the proportion of budget allocated to capital, raising questions about the balance between the three budget elements. At a glance it may suggest that increasing personnel costs are putting the capital investment budget under pressure (as noted in this review's Terms of Reference at 3d), but in fact this trend has been driven more by volatility in overall funding than by growth in personnel costs.

Diagram 12: Capital spending fell as a proportion of total spending in recent years, but is forecast to recover



96 From 1993, the ratio rose as recommendations of the Wrigley Review and the 1991 Force Structure Review were implemented, including through the Commercial Support Program, and when Aerospace Technologies of Australia and Australian Defence Industries were privatised. See Department of Defence, *Force Structure Review 1991*, Canberra, pp. 41–45; Department of Defence, *Annual Report 1991–92*, Canberra, 1992, p. 10; Joint Standing Committee on Foreign Affairs, Defence and Trade, *Funding Australia's Defence*, Canberra, May 1998, pp. 59–60.

Diagram 13: Overall funding volatility drives capital reductions



Current forecasts suggest that the capital budget will return to approximately one third of the overall budget over the forward estimates. However, judging appropriateness and force fitting this alongside an historic ratio is not the right approach as it will drive the wrong outcomes.

As noted in Chapter 5, the employee, capital and operating costs will and should continue to fluctuate with strategic priorities. The prime consideration is whether these proportions reflect the most effective and efficient use of funds to support current and future force requirements.

Focus on public service workforce

Both of the measures discussed above are commonly used to draw attention to public servant workforce numbers. They are often combined with growing personnel costs, without detailed analysis, to suggest a bloated, overpaid and inefficient public service workforce and an ensuing focus on 'civilian' reductions as a key efficiency measure.

As we noted in Chapter 5, the public service workforce equates to eight per cent of the overall Defence budget and public servants are, on average, 30 per cent less expensive than military personnel. The focus on setting arbitrary targets for public service reductions in Defence does not encourage good business practice.

The current way public service numbers are managed in Defence drives some perverse behaviour and unintended outcomes — the focus on staffing numbers separate from budget allocation is not consistent with how other departments manage their budgets.

At the project level, Defence treats staff as a 'free good'. Employee costs are not considered part of a project's costs and a manager cannot adjust numbers of staff based on project need. An alternative approach is to manage a total project budget that includes employee expenses. This encourages managers to exercise judgement and discretion to 'trade' within that operating budget (assessing their need for how many staff and what levels, skills and contracted expertise are required) to most efficiently and effectively deliver the outcomes required.

At the enterprise level, the focus on public service numbers makes it difficult to achieve the most efficient workforce mix. While public servants are less expensive than military personnel, the Services are wary about giving up military positions because the public servant replacements may be lost via possible future reductions. In fact, they have replaced public service staff with military personnel to ensure functions continue.

If the current practice continues, it will be extremely difficult to implement our recommendations in Chapter 5 regarding the best workforce mix to match required outcomes. **We recommend that the focus on public service reductions as the primary efficiency mechanism for Defence cease. We also recommend that Defence manage its workforce numbers in line with good resource management practice where Defence is held to account for delivering on required outcomes within available resourcing.**

Workforce Efficiencies from Implementing One Defence

As noted above, efficiencies were not the primary driver of the review. We debated whether to include numbers relating to workforce reductions because arbitrary targets and ranges can be manipulated. Mandating a target at the high end of a range or adopting a low end target and doing the bare minimum to achieve it, can easily become a distraction to implementation. It has the potential to shift the focus from achieving the overall outcome of the recommendations and measuring changes in effectiveness to measuring numbers.

The critical factor to consider here is that the identified efficiencies are the result of analysis and linked to a specific reform initiative. It is about better allocation of resources rather than arbitrary approaches to reductions.

Downsizing is already occurring within Defence with full time equivalent staff reducing from approximately 22,300 in mid-2012 to around 19,500 in October 2014. These reductions have largely been achieved through natural attrition and a tightening of recruitment practices.

Whilst these arbitrary approaches are delivering results, the review team believes a more targeted approach would produce more control over the shape and skills of the workforce.

We have set broad targets and would expect that detailed targets would be developed as part of the implementation process, based on more in-depth analysis. It is our view that effective implementation of our recommendations will deliver substantial and quantifiable efficiencies.

Strong strategic centre

In advice to the Secretary and Chief of the Defence Force, we have recommended that seven Senior Executive Service Band 3 positions and one 3 star position be removed which is a 32 per cent reduction in positions at this level. We expect that as part of the implementation process, organisational restructuring will cascade throughout the senior leadership group and will necessarily change the shape and reduce the numbers of the leadership group.

Capability development life cycle

The creation of the Capability Acquisition and Sustainment Group will lead to the reduction of around 1000 public servants and a reallocation of around 950 Australian Defence Force personnel.⁹⁷ These suggested reductions are consistent with the level of reduction recommended by another third party review of the Defence Materiel Organisation.⁹⁸ These reductions would result from:

- Integration into the Department with a reduction in the number and costs of financial and other transactions between Defence and the Defence Materiel Organisation as well as the full implementation of shared corporate services;
- Implementing the smart buyer model with associated reduction in the number of System Project Offices and appropriate outsourcing to industry (in both acquisition and sustainment);
- Removing duplicated functions such as industry policy, reform and contestability functions; and
- Using military and public service expertise appropriately.

Streamlining the two pass process will reduce duplication, project documentation and the time taken to develop such material. Removing the current practice of cost slippage as a budgeting rule should improve schedule management and enable projects to be delivered within agreed timeframes. Decreasing the bureaucracy, managing costs more appropriately and having a tailored, skilled work force will generate significant efficiency for the department.

Middle management spans and layers

Defence's enabling organisation is significantly out of shape with up to 12 layers in some parts of the organisation, from the Secretary to front line staff, and very narrow spans of control (a median of two), particularly in the middle management layers of the organisation. Through our recommendations in Chapter 5, we seek to improve the structure of the enabling workforce.

Savings will be generated as spans of control are increased and management roles reduced. This initiative is in line with the direction from the Australian Public Service Commission that all departments review their spans of control. The Commission has also published guidance on expected spans of control depending on the type of function, all of which are higher than the Defence median.⁹⁹ The majority of these role reductions would come from public service middle management (around 650 roles) where the spans of control are the lowest (see Chapter 5), but would also include military roles which would be returned to the Services (around 100 roles).

Roles should be assessed to ensure they are appropriately classified and to ensure that people are delivering a consistent standard of work for which they are being remunerated. Methodologies need to be put in place to retain top talent and ensure the right people are in the right roles to lift the level of professionalisation within the enabling organisation.

Other areas

Further long term savings will be realised from service delivery reform, estate disposal, information management improvement, decreased duplication, standardisation of services and better procurement and contracting processes but, at this stage, the exact numbers have not been quantified.

We note the Commission of Audit's finding that the staffing levels in Defence Headquarters have grown significantly since 1998. Attempts at getting consistent and quality assured data proved difficult, possibly due to varied definitions of headquarters and service structures. A lack of appropriate data, and the complexity and level of detail required to form a firm view on this issue was beyond the remit of the First Principles Review.

⁹⁷ Boston Consulting Group analysis of Defence work force data.

⁹⁸ PriceWaterHouseCoopers, *DMO End State Design Final Report*, December 2013.

⁹⁹ Briefing material prepared by Australian Public Service Commission for Secretaries' Board, October 2014.

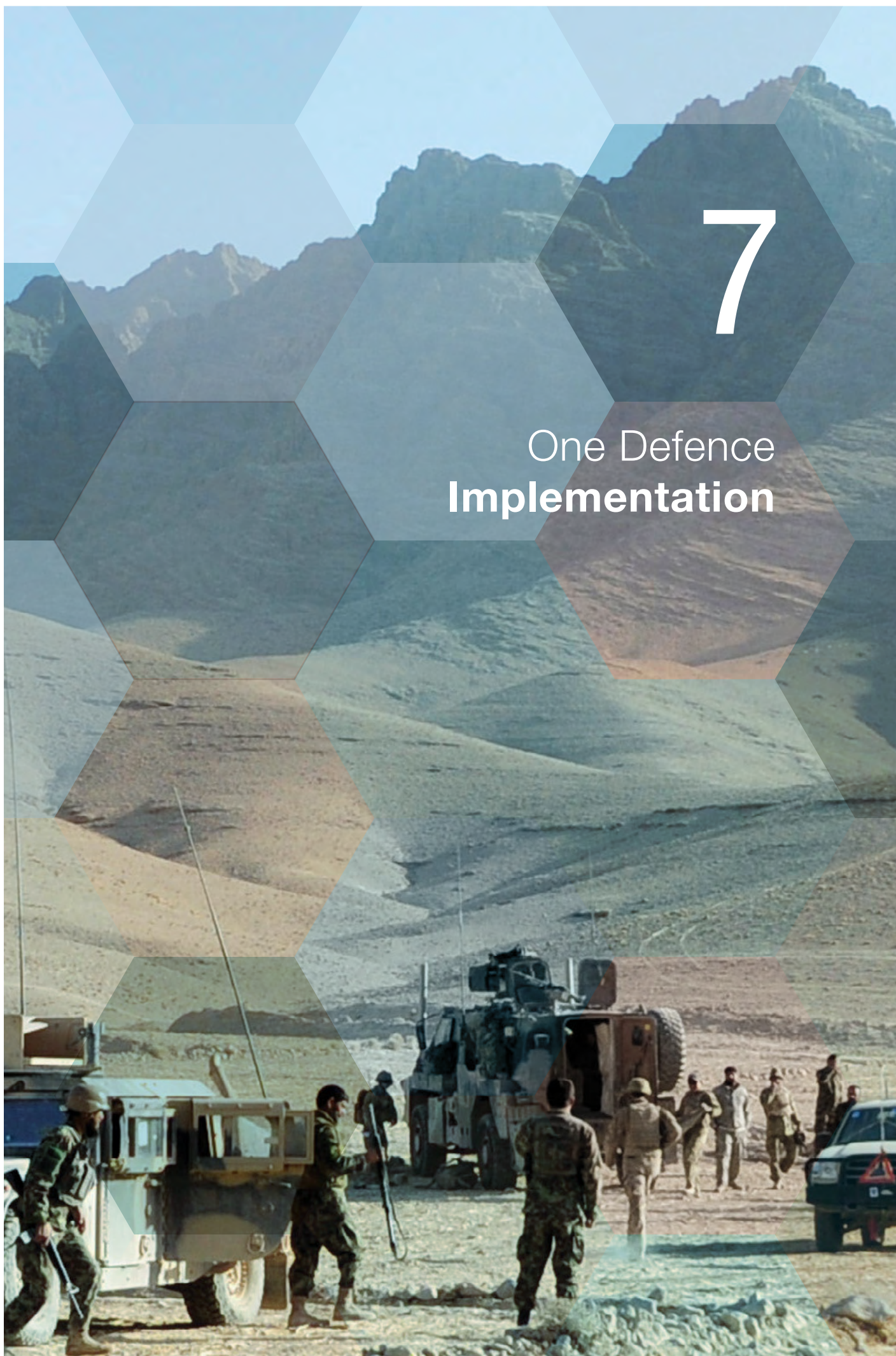
We would, however, suggest that this is another opportunity for Defence to find productivity savings. The headquarters function needs to be considered in light of the **One Defence** model being established and the changing roles of the senior leadership, particularly the Vice Chief of the Defence Force and the Service Chiefs. **We recommend that as part of the implementation process, Defence examine the headquarters functions for opportunities to achieve more effective and efficient arrangements.**

Conclusion

As we have noted, staff reductions are already occurring in Defence with further projected reductions in future financial years. This report provides a targeted approach to staff reductions based on implementing our recommendations, which could lead to a Defence public service workforce within the range of 16,000 to 17,000 full time equivalents. The initiatives will also lead to the reallocation of around 1000 Australian Defence Force personnel back to the Services, consistent with any findings of the Force Structure Review.

7

One Defence Implementation



Key Recommendation 6

Commence implementation of **One Defence** recommendations immediately with required changes in place within two years

Effective implementation is critical to the success of reform and delivering the transformational change described throughout this report will be hard work. The scope of the changes proposed include: reduction and redefinition of the senior leadership and their respective authority and accountabilities; comprehensive adjustments to organisational structures, systems and processes (especially in the core capability development process); more integrated and customer-centric enablers; and, reshaping the workforce, changing the workforce mix, introducing a holistic workforce management and a comprehensive performance management system.

As we stated in Chapter One, our recommendations for creating **One Defence** are a package which should be implemented in their entirety rather than cherry-picked and selectively modified. In combination, the magnitude of the proposed changes is comparable to those of the Tange Review — a once-in-a-generation opportunity.

Change needs to be led, and it will involve a change in behaviours. It will only happen with strong, clear and uncompromising leadership from the top (political, civilian and military) supported by energetic, committed and professional leadership teams, with external scrutiny for a period of time.

Implementation Approach

Managing transition is often something that is not given sufficient attention. At the outset, Defence needs to acknowledge that the changes proposed will be difficult and there will be setbacks that will need to be worked through. But Defence must avoid defaulting to further consideration and dissection of the problem. There needs to be unwavering commitment to seeing the change through. There must be a dedication to building **One Defence** and to putting the enterprise at the forefront of considerations so that the total offer is of greater value than the sum of its parts.

Defence needs to generate reform momentum and move to the **One Defence** model as quickly as possible. There should be a focus on delivering high impact, low cost changes in the immediate term. Substantial change needs to happen early that, in effect, pushes Defence to a point of no return on its transformation journey.

While speed in implementation is important, Defence should be given an appropriate period to embed changes at all levels, deliver the required outcomes, and assess the impact and need for further reform or adjustment. Therefore, **we recommend no additional reviews on the organisational issues covered by this Review are imposed on Defence, particularly within the early years of implementation.**

Further, it is our view that apart from the Pathway to Change initiatives, this review should reset the reform agenda for Defence. **We also recommend that past reviews and current reform initiatives should be assessed for currency and alignment to the One Defence model.** There should be no distractions by other reviews new or historic.

Key Milestones

In accordance with the Terms of Reference, and unlike most previous reviews, we have developed a high level plan to act as a guide for implementation. This plan includes proposed key milestones and target deadlines.

It is important that we provide sufficient clarity to avoid any misinterpretation and wherever possible give Defence a head start to mobilising implementation without being so prescriptive as to remove the ownership of change from the Defence leadership. The plan sets expectations about the pace with which change should occur and provides advice and direction for the development of substantially more detailed implementation plans by the Defence leadership.






In developing these plans, Defence needs to strike the right balance between delegation to the functional owners of the change and centralised control. Central design authority and guidance must be set by the Secretary and the Chief of the Defence Force. All subordinate plans must align with this central framework to ensure the **One Defence** outcome is centrally managed and to maintain consistency with intent and outcome.

Functional managers or work stream leads need to be assigned, with their initial task to be the development of specific work stream implementation plans within three months. These work stream plans should be rolled into one integrated plan, owned by the Secretary and the Chief of the Defence Force, which once endorsed, will become the baseline against which progress is reported and individuals held accountable.

We have front-end loaded the reforms wherever possible to encourage Defence into rethinking all elements of its business and to guard against reverting to the old way of working. Many of the structural and leadership changes are scheduled in the first three months. Where it is sensible and achievable, as many of these changes as possible should occur immediately to demonstrate leadership commitment to the transformation.

The vast majority of the change should be delivered within two years. We recognise that the scale of change is large and complex. However, it is our view that two years is realistic. To plan beyond this would risk loss of momentum and change being overtaken by 'business as usual' priorities. A tail of activity might run beyond two years, for example completing the roll-out of the smart buyer model or finalising estate disposals.

HIGH LEVEL IMPLEMENTATION PLAN

	 IMMEDIATE	 + 3 MONTHS	 +9 MONTHS	 +15 MONTHS	 +24 MONTHS
A Accountabilities and delayering	<p>Secretary/Chief of the Defence Force accountabilities communicated across Defence (Ministerial directive)</p> <p>Principles and approach defined for organisational redesign to inform detailed plan</p> <p>Secretary/Chief of the Defence Force direct reports and other Band 3 positions created, roles charters agreed and appointments initiated</p> <p>Workstream sponsors and initiative leads appointed, teams mobilised</p>	<p>Defence Senior Leadership Group (Band 1/2/3) clarified, role charters agreed and appointments initiated</p> <p>Detailed implementation plan for organisational redesign and staff reductions for remainder of Defence organisation complete</p> <ul style="list-style-type: none"> Baseline organisational data (e.g. roles, reporting lines, comp.) compiled <p>Surplus Senior Executive Service/Star ranked staff identified and expected savings quantified</p>	<p>Executive Level 1/2 level positions clarified with role charters and performance agreements, appointments initiated and existing organisation re-pointed</p> <p>Surplus Executive Level 1/2 staff identified and expected savings quantified</p>	<p>Full new organisation design complete with role charters and performance agreements, all appointments commenced (excluding System Project Offices - addressed in smart buyer roll-out)</p> <p>All surplus staff identified and expected savings quantified</p>	<p>Workforce aligned to target size</p>
B Strategic centre	<p>New Defence Committee membership confirmed</p> <p>Workstream sponsors and initiative leads appointed, teams mobilised</p>	<p>Defence Committee, Defence Enterprise Business and Investment committees operating</p> <p>Detailed design and implementation plan developed for new strategic centre</p> <ul style="list-style-type: none"> Policy and contestability functions Corporate planning Force design (including two pass process) Finance functions Capability managers Draft legislative amendment for consideration by parliament 	<p>New functions in strategic centre operating</p> <p>Defence Investment Plan developed and being managed</p> <p>New approvals process redesigned, all projects transferred</p> <p>Centre led processes for enterprise planning and budgeting defined and underway for 2016/17</p> <p>Department planning</p> <p>All existing committees reviewed for fit with One Defence and retained or abolished</p>	<p>All roles filled in new strategic centre</p> <p>New framework for reporting in place</p> <ul style="list-style-type: none"> Agreed outcomes (such as preparedness, new capability delivery, enterprise) Financial reporting in place 	<p>New financial approval thresholds in place</p>
C Capability delivery	<p>Appointment process for new Deputy Secretary initiated</p> <p>Workstream sponsors and initiative leads appointed, teams mobilised</p>	<p>Detailed design and implementation plan developed for Capability Acquisition and Sustainment Group</p> <p>Defence Science and Technology Organisation: value proposition articulated and new engagement mechanism up and running</p>	<p>Transition of existing functions into new group - parts of Capability Development Group/ Defence Materiel Organisation/ Defence Science and Technology Organisation/ non-materiel procurement/logistics re-pointed under new lead</p> <p>Non-core functions disbanded or shifted to other parts of the organisation</p> <p>Integrated requirements, acquisition and sustainment delivery and costing methodologies defined and ready for implementation</p> <p>Smart buyer model agreed – outsourcing, System Project Office sequencing and consolidation, target benefits set</p>	<p>All projects and System Project Offices operating under new delivery and costing methodologies</p> <p>Smart buyer roll-out complete for high importance/ simple set of System Project Offices. New contract structure and System Project Offices roles implemented</p>	<p>Smart buyer rollout completed medium importance/ medium complexity set of System Project Offices</p> <p>Plan for smart buyer model roll-out for remaining System Project Offices agreed</p>
D Workforce reform	<p>Workstream sponsors and initiative leads appointed, teams mobilised</p>	<p>New performance agreements agreed for Senior Executive Service/Executive Level 2</p> <p>Detailed design and implementation plan for new workforce system developed</p> <ul style="list-style-type: none"> Performance management Strategic workforce management Australian Defence Force postings <p>Confirm/appoint senior accountable officers to build skill and competence in key job families</p>	<p>Renegotiate the number, type and length of new Australian Defence Force postings that start in 2016</p>	<p>New performance agreements agreed for Executive Level 1 and below</p> <p>Roll-out performance management system for Senior Executive Service/ Executive Level 2</p> <p>Strategic workforce plans for all job families</p> <ul style="list-style-type: none"> Skills audit of current personnel Future skill requirements and gaps Embedded in human resources plans <p>Australian Defence Force career plans updated for impact of reform</p>	<p>Roll-out of performance management system to all of Defence Australian Public Service completed – bell curve distribution for performance and performance managed</p> <p>Renegotiate the number, type and length of new Australian Defence Force postings starting in 2017 based on Strategic Workforce Plan</p> <p>First report of progress against the strategic workforce plans prepared</p>
E Enabling services	<p>Defence Materiel Organisation corporate services shifted to centralised, shared service</p> <p>Workstream sponsors and initiative leads appointed, teams mobilised</p>	<p>Interim plan for Estate consolidation developed, including a definition of need and identifying first tranche disposals</p> <p>Detailed design and implementation plan for Information Management developed, including alignment of existing/planned initiatives to Information Management agenda</p> <p>Design and service offers by service delivery function completed</p>	<p>Detailed design and implementation plan for Estate consolidation developed</p> <p>First tranche disposals – initial transactions in market</p> <p>Enterprise Information Management business requirements compiled</p> <p>C4ISR authority in place</p> <p>Regional service delivery model completed</p>	<p>Second tranche of estate disposals in the market</p> <p>Information management architecture, standards, master data management in place</p> <p>Service delivery reform completed</p>	<p>Third tranche of estate disposals in the market</p> <p>First tranche of Information Management initiatives implemented and systems and/or applications decommissioned</p>
One Defence program	<p>External Oversight Board appointed by Minister</p> <p>Program governance and implementation office in place</p> <p>Communication with wider Defence, unions and key stakeholders on program impacts underway</p>	<p>Overall plan including target outcomes reviewed by External Oversight Board and reported to the Minister</p> <p>Keep/stop/review for existing reforms completed</p>			<p>Undertake an independent health check on progress</p>

Governance

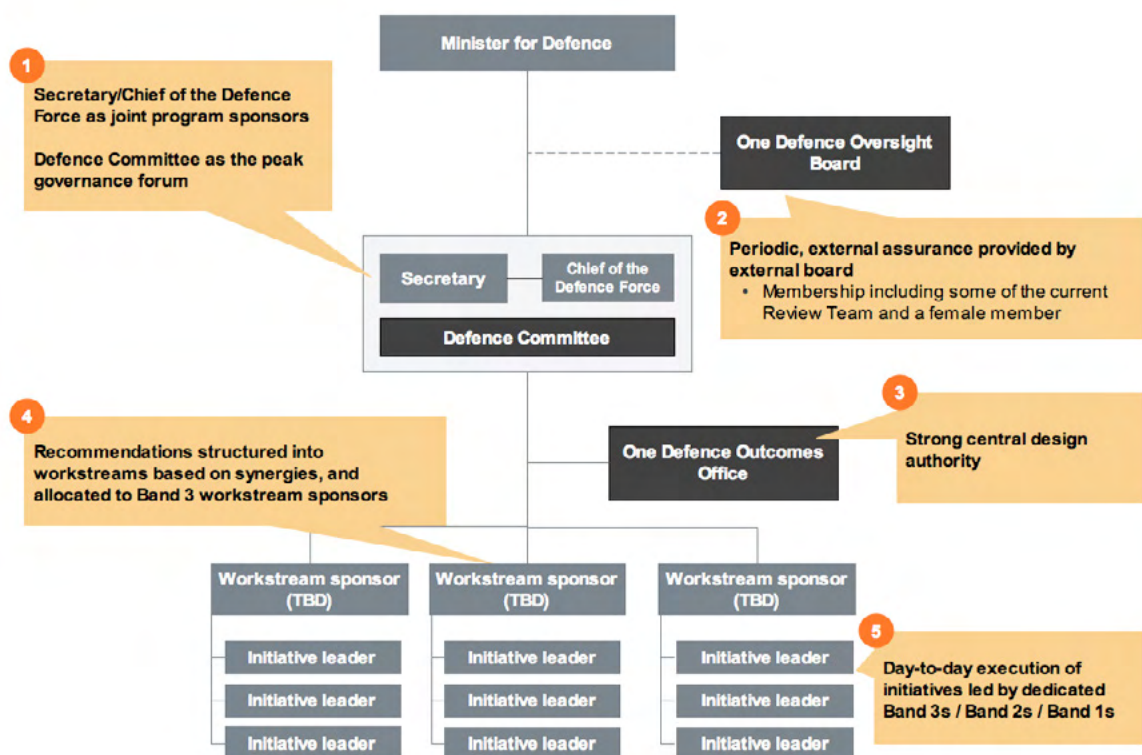
A strong governance and assurance framework is necessary to ensure the successful creation of **One Defence** and to provide visibility of the progress in implementation to the Minister and Government.

We recommend establishing an Oversight Board to provide close external scrutiny, advice on implementation progress and regular reports to the Minister. It will be an important source of independent advice to the Minister and a key component of ensuring the **One Defence** outcomes, as envisaged by the review team, are delivered. We believe there is benefit in having a mixed membership that includes some members of the First Principles Review team.

In accordance with the Terms of Reference, **we recommend the Minister, with input from the Department and the Oversight Board, report progress on implementation to the Government in March 2016 and March 2017.**

Defence will need to establish a highly skilled transition team using a combination of in-house and contracted expertise. This team will provide strong central design authority to ensure alignment with the **One Defence** model and review achievement of outcomes.

Diagram 14: Governance Structure



Behavioural Shift

Many of the recommendations in this report are about changes to organisational structure and processes (the physical mechanisms). Underlying these changes though is the need for a behavioural shift in order to give true effect to the **One Defence** system. Behavioural elements include ‘the attitudes, belief systems and core values that drive behaviour and guide daily activities and decision-making throughout the institution’.¹⁰⁰

Changes to structure and processes will not of themselves change behaviours. This is part of the implementation challenge for the Defence leadership and will require close monitoring. It will be difficult and there will be setbacks but there must be consistent pursuit of the new model — the new good. Leaders at all levels will need to be actively engaged with the change. Any pockets of resistance must be dealt with quickly.

Leadership

To say this transformational change needs to be led from the top is an understatement. Ultimate accountability for implementation of **One Defence** rests with the Secretary and the Chief of the Defence Force, but they must be supported fully by the Associate Secretary and the Vice Chief of the Defence Force and the Defence senior leadership group more broadly.

The transformation must be centrally driven, but locally delivered. The right balance between central control and direction, and line management autonomy and expertise is critical. The strong, strategic centre (as discussed in Chapter Two) must set a clear framework and direction for moving to **One Defence**. Within this construct, the enterprise planning process should be used to review overall progress and individual leaders should be held accountable through their performance agreements and an appropriate performance review framework.

We have noted that the organisational drift has been partly caused by leadership churn. To prevent continuing drift and to provide the greatest chance of implementation success there should be, as much as is realistically possible, minimal leadership turnover. The leadership team needs constancy and unity in order to tackle Defence’s problem of inertia and make the bulk of the changes within two years. **We recommend stability in the key leadership positions, particularly over the next two years to provide consistency of direction and ownership of the change.**

As noted in the Foreword, the **One Defence** transformation is an opportunity for Defence to establish better relationships with the Government, Ministers, external stakeholders, central agencies, its own leadership and workforce. It is an opportunity for Defence to reset its reputation and re-position Defence as a truly integrated agency that consistently produces the best public value, and is able to meet the current and future demands on it. Most importantly, it will allow Defence to effectively deliver on its primary focus: to protect and advance Australia’s strategic interests through the provision of appropriately prepared and equipped armed forces.

¹⁰⁰ Protiviti, *Establishing and nurturing an effective risk culture*, 2010, p.14, available at <www.protiviti.com/en-US/Pages/Whitepapers.aspx>.

8

Annexes



Annex A: Terms of Reference including alignment with recommendations

FIRST PRINCIPLES REVIEW OF DEFENCE

Terms of Reference

The First Principles Review of Defence will:

1. ensure that the Department of Defence's business structures support the ADFs principal tasks, as determined by the 2015 Defence White Paper, and other whole of government responsibilities out to 2030;
2. ensure a commercially astute, focused and accountable materiel acquisition and sustainment capability;
3. improve the efficiency and effectiveness of Defence;
4. guide the implementation of recommendations from the Commission of Audit not otherwise covered above; and,
5. ensure the ongoing delivery and reporting of agreed recommendations.

Issues for Consideration

In addition to any issues the review team considers important to examine in addressing the Terms of Reference, the Review team should also consider the following matters:

1. Ensure that the Department of Defence's business structures support the ADFs principal tasks, as determined by the 2015 Defence White Paper, and other whole of government responsibilities out to 2030, including by:
 - a) Reviewing the cost, efficiency, timeliness and appropriateness of Defence's current business model and processes, including compliance with external processes and responsiveness to Government, with an aim to simplify and improve accountability;
 - b) Reviewing the capacity of Defence to develop strategy and key policy options, particularly, future White Papers, Force Structure and prioritisation of capability investment;
 - c) Examining the efficient arrangements of the intelligence functions, particularly those involving geospatial intelligence; and
 - d) Examining the functioning of the separate and shared responsibilities and accountabilities of the Secretary and Chief of Defence Force.
2. Ensure a commercially astute and focused materiel acquisition and sustainment capability, including by:
 - a) Examining the benefits and costs of the following three approaches to reforming the Defence Materiel Organisation (DMO) and recommending a preferred option and how it should be implemented:
 - i) Current model with improvements to commercial skills and improved arrangements to manage larger and more complex projects;
 - ii) DMO to be re-integrated into Defence with a focus on contract management, as recommended by the Commission of Audit; and
 - iii) An independent and commercialised DMO in whole or in part.
 - b) Either as part of 2a, or separately, undertake an examination of specific initiatives to improve business processes including, but not limited to, the following:
 - i) Options to further improve the professional knowledge and skills within the capability development function, particularly program and project management, systems engineering and cost and schedule estimation (particularly at DCP entry);

- ii) Options to provide greater assurance to Government on the capital and sustainment costs and schedule of large complex capabilities including utilising relevant private sector experience;
- iii) Options to significantly accelerate the capability development process, including examination of whole of government issues and risk based approaches;
- iv) How Defence sustains and supports capabilities and extending lessons from the Coles review across all areas of sustainment;
- v) Options for improved project control particularly through the mandatory use of Earned Value Management for all elements of projects that meet an appropriate threshold; and
- vi) Opportunities for improved certainty in program-level cash flow estimation, project and program level funding arrangements for DMO and alternatives to the use of over-programming as a management tool in the DCP.

3. Recommend further options to improve the efficiency and effectiveness of Defence by:

- a) Assisting Defence to develop appropriate implementation plans, including appropriate benefits realisation plans, to deliver agreed outcomes of the Commission of Audit and the First Principles Review, to be followed by a progress review in March 2016 to measure the effectiveness of the implementation of the recommendations;
- b) Developing recommendations for the further rationalisation of IT systems, particularly financial and personnel, and further clarify accountability for them and their cost effectiveness;
- c) Examine and recommend options for reaching and maintaining a sustainable balance between Defence's personnel, operating and capability budgets;
- d) In the above context, specifically consider what can be done about rising personnel costs, particularly for the ADF, that are putting the capital investment budget under significant pressure;
- e) Examine outstanding recommendations from other reviews and make recommendations on whether they might be retired or re-invigorated; and
- f) Recommend further options for the enhanced commercialization of Defence functions, including DSTO but excluding DHA.

4. Recommendations from the Commission of Audit not otherwise covered above.

COMMISSION OF AUDIT

Recommendation 24: Defence

Ensuring the nation's defence and security is a core function of the Commonwealth Government. The Commission recommends a number of steps be taken to improve the efficiency, effectiveness, accountability and transparency of Defence spending through:

- a. ensuring preparation of the new Defence White Paper identifies capability options and associated costs for different sets of strategic risks. As part of this process, the Government should also assess the balance of strategic and fiscal priorities and how this compares with the commitment to increase Defence expenditure to two per cent of GDP within a decade;
- b. as a pre-condition for setting any new funding profile for Defence under the White Paper, the Government should ensure that Defence improves the effectiveness and transparency of expenditure by improving Defence budget arrangements and governance, capability development and delivery;
- c. transparency and control for government should be significantly improved by stronger budget processes including through the Expenditure Review Committee. For new capital, in particular new equipment projects, this would include holding funds in separate budget allocations and releasing them as projects are approved. Such expenditure should be treated as administered funding rather than departmental funding, so that there is greater financial control and scrutiny of this expenditure through established budget processes;
- d. a new ministerial directive to the Secretary of the Department of Defence and the Chief of the Defence Force specifying their separate and shared responsibilities and holding them individually accountable for Defence performance;
- e. reintegrating the Defence Materiel Organisation into the Department of Defence, with the size of the Defence Materiel Organisation being significantly reduced and with a renewed focus on contract management as opposed to project management;
- f. establishing a more professional Capability Development Group within Defence with an increased use of project development professionals skilled in cost and risk assessment;
- g. reducing the staffing size of Defence headquarters in Canberra, including senior staff, to 1998 levels; and
- h. Defence publishing performance indicators that reveal progress with reform, including the 'teeth to tail' ratio and the additional cost of unique and Australian built procurement decisions.

First Principles Review Recommendations against Terms of Reference and Commission of Audit

	FIRST PRINCIPLES REVIEW RECOMMENDATIONS	FIRST PRINCIPLES REVIEW TERMS OF REFERENCE	COMMISSION OF AUDIT TERMS OF REFERENCE
1	Establish a strong strategic centre to strengthen accountability and top level decision-making	1 (a), 1 (b), 1 (d), 2 (b) (ii), 3 (c)	24 (b)
1.1	We recommend the First Principles Review is adopted as the road map for Defence reform at least for the next five years with no other reviews in that period	3 (a)	
1.2	We recommend a new One Defence business model	1 (a), 1 (b), 1 (d), 2 (a) (ii)	24 (b)
1.3	We recommend the diarchy be retained	1 (a), 1 (b), 1 (d)	24 (d)
1.4	We recommend the individual and shared accountabilities of the Secretary and Chief of the Defence Force be clarified, formally documented and promulgated through the organisation	1 (a), 1 (b), 1 (d)	24 (d)
1.5	We recommend a streamlined top level management structure for the Department that is aligned with the One Defence business model	1 (a), 1 (b), 1 (d), 2 (b) (ii), 3 (a)	24 (e), (g)
1.6	We recommend the strategic centre include the Associate Secretary and Vice Chief of the Defence Force as the integrators for the Defence enterprise and the future force and joint capabilities respectively	1 (a), 1 (b), 3 (b)	24 (b)
1.7	We recommend the Vice Chief of the Defence Force's decision rights be greatly strengthened, including the right to stop projects proceeding through the approval process until joint force integration is proven	1 (a), 1 (b), 2 (b) (ii), 2 (b) (iii), 3 (c)	24 (b)
1.8	We recommend legislative changes to formally recognise the authority of the Chief of the Defence Force and the Vice Chief of the Defence Force, including removing the statutory authority of the Service Chiefs	1 (a), 1 (b), 1 (d), 2 (b) (ii)	24 (b), 24 (d)
1.9	We recommend that policy advice be strengthened by bringing all policy functions into one organisational unit in order to improve the quality of advice provided to Government	1 (a), 1 (b)	24 (b)
1.10	We recommend a strong and credible internal contestability function be built and led by the Deputy Secretary Policy and Intelligence with responsibility for strategic contestability, scope, technical and cost contestability	1 (a), 1 (b), 2 (b) (i), 2 (b) (ii), 2 (b) (iii), 2 (b) (vi), 3 (b), 3 (c)	24 (b)
1.11	We recommend that the policy and intelligence functions be combined under a Deputy Secretary Policy and Intelligence, who will have responsibility for providing policy advice and intelligence assessments to the Secretary and the Chief of the Defence Force	1 (a), 1 (b), 1 (c)	24 (g)
1.12	We recommend the Defence Security Authority be repositioned under the Associate Secretary	1 (a), 1 (b)	24 (b)
1.13	We recommend the Defence Committee be re-positioned as the primary decision making committee of Defence and the heart of the strategic centre with two supporting committees – Enterprise Business Committee and Investment Committee	1 (a), 1 (b), 2 (b) (ii), 2 (b) (iii), 2 (b) (vi), 3 (c)	24 (b)
1.14	We recommend that all other enterprise-wide committees be reviewed for their relevance and alignment with the One Defence business model with the aim of a substantial reduction in the number of committees	1 (a), 1 (b)	24 (b)
1.15	We recommend that the organisational structure reporting to the Vice Chief of the Defence Force be simplified through the incorporation of a two-star Head of Joint Enablers role	1 (a), 1 (b)	24 (b)
1.16	We recommend a strengthened centre-led, enterprise-wide planning and performance monitoring process be adopted	1 (a), 2 (b), 3 (a)	24 (b)

	FIRST PRINCIPLES REVIEW RECOMMENDATIONS	FIRST PRINCIPLES REVIEW TERMS OF REFERENCE	COMMISSION OF AUDIT TERMS OF REFERENCE
1.17	We recommend that the Associate Secretary be the central authority to deliver enterprise planning and performance monitoring processes, in line with the requirements of the <i>Public Governance, Performance and Accountability Act 2013</i>	1 (a), 2 (b), 3 (a)	24 (b)
1.18	We recommend that the Minister for Defence meet with the Defence Committee twice yearly to consider a formal strategic assessment of the alignment between Defence's strategy, funding and capability	1 (a), 1 (b), 2 (b) (ii), 3 (c)	
1.19	We recommend Defence conduct regular reviews of the capital program in consultation with the Minister and central agencies	1 (a), 1 (b), 2 (b) (i), 2 (b) (ii), 2 (b) (iii), 2 (b) (vi), 3 (c)	
2	Establish a single end to end capability development function within the Department to maximise the efficient, effective and professional delivery of military capability	1 (a), 1 (b), 2 (a) (i), 2 (a) (ii), 2 (a) (iii), 2 (b) (i), 2 (b) (ii), 2 (b) (iii), 2 (b) (iv), 2 (b) (v), 2 (b) (vi), 3 (c)	24 (e), 24 (f), 24 (g)
2.1	We recommend disbanding the Capability Development Group and dispersing its functions to more appropriate areas	1 (a), 1 (b), 2 (a) (ii), 2 (b) (i), 2 (b) (ii), 2 (b) (iii)	24 (e), 24 (f), 24 (g)
2.2	We recommend disbanding the Defence Materiel Organisation and transferring its core responsibilities in relation to capability delivery to a new Capability Acquisition and Sustainment Group	1 (a), 1 (b), 2 (a) (ii), 2 (b) (i), 2 (b) (ii), 2 (b) (iii), 2 (b) (iv), 2 (b) (v), 2 (b) (vi)	24 (e), 24 (f), 24 (g)
2.3	We recommend that a new organisational design and structure is developed as part of the implementation process for the Capability Acquisition and Sustainment Group with reduced management layers	1 (a), 1 (b), 2 (a) (ii), 2 (b) (i), 2 (b) (ii), 2 (b) (iii), 3 (c)	24 (g)
2.4	We recommend examining each System Program Office to determine where each fits within the smart buyer function, the most appropriate procurement model and achieving value for money	1 (a), 1 (b), 2 (a) (ii)	24 (b), 24 (e)
2.5	We recommend the Capability Managers specify the Fundamental Inputs to Capability requirements with the Capability Acquisition and Sustainment Group having responsibility for developing and delivering an integrated project plan	1 (a), 2 (a) (ii), 2 (b) (i), 2 (b) (ii), 2 (b) (iii), 2 (b) (iv), 2 (b) (v), 2 (b) (vi)	24 (b)
2.6	We recommend the accountability for requirements setting and management be transferred to the Vice Chief of the Defence Force and the Service Chiefs with strategic, financial and technical contestability being located with Deputy Secretary Policy and Intelligence	1 (a), 1 (b), 2 (a) (ii), 2 (b) (i), 2 (b) (ii), 2 (b) (iii)	24 (b)
2.7	We recommend that the Independent Project Performance Office and the Capability Investment and Resources Division be relocated to Deputy Secretary Policy and Intelligence, significantly enhanced and strengthened to provide such contest	1 (a), 1 (b), 2 (a) (ii), 2 (b) (i), 2 (b) (ii), 2 (b) (iii), 2 (b) (vi)	24 (b)
2.8	We recommend revising the Defence investment approval process for all large or complex capability projects	1 (a), 1 (b), 2 (a) (ii), 2 (b) (i), 2 (b) (ii), 2 (b) (iii), 2 (b) (iv), 2 (b) (vi)	24 (b), 24 (c)
2.9	We recommend introducing a new formal gate into the process at entry point - Gate Zero: Investment Portfolio entry.	1 (a), 1 (b), 2 (a) (ii), 2 (b) (i), 2 (b) (ii), 2 (b) (iii), 2 (b) (vi)	24 (b)
2.10	We recommend the Government increase approval thresholds for capability development projects, with ministerial approval required only for projects above \$20 million, two ministers above \$100 million and Cabinet above \$250 million	1 (a), 1 (b), 2 (b) (vi)	

First Principles Review Recommendations against Terms of Reference and Commission of Audit

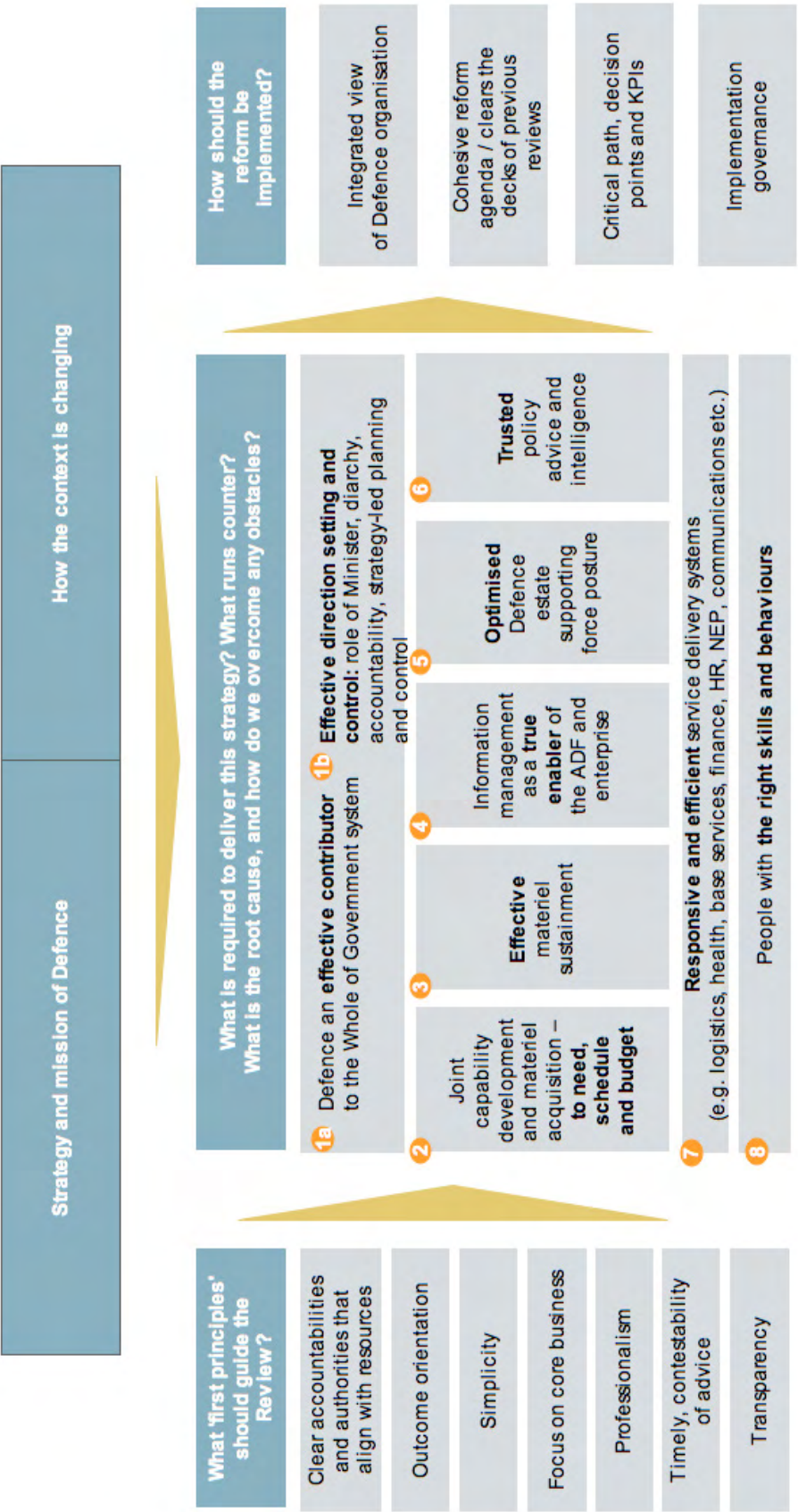
	FIRST PRINCIPLES REVIEW RECOMMENDATIONS	FIRST PRINCIPLES REVIEW TERMS OF REFERENCE	COMMISSION OF AUDIT TERMS OF REFERENCE
2.11	We recommend significant investment to develop an operational framework which comprehensively explains how the organisation operates and roles and responsibilities within it; and detail life cycle management processes which provide project and engineering discipline to manage complex materiel procurement from initiation to disposal; and review architecture to reinforce accountability at all levels and brings together information upon which good management decisions can be made	1 (a), 1 (b), 2 (a) (ii), 2 (b) (i), 2 (b) (ii), 2 (b) (iii), 2 (b) (iv), 2 (b) (v)	24 (b)
2.12	We recommend the Deputy Secretary Capability Acquisition and Sustainment must sign off and assure the Secretary of the operational output of each of his/her divisions every quarter and on major contracts on a monthly basis	1 (a), 1 (b), 2 (a) (ii), 2 (b) (ii), 2 (b) (iv), 2 (b) (v), 2 (b) (vi)	24 (b)
2.13	We recommend the use of net personnel operating costs process cease immediately	1 (a), 1 (b), 2 (b) (i), 2 (b) (ii), 2 (b) (vi), 3 (c)	24 (b)
2.14	We recommend developing a Defence Investment Plan which would include all capital and related investments (such as materiel, estate and facilities, workforce and information and communications technology)	1 (a), 1 (b), 2 (a) (ii), 2 (b) (i), 2 (b) (ii), 2 (b) (vi), 3 (b), 3 (c)	24 (b)
2.15	We recommend that, on Government approval, the entire project acquisition budget is allocated to the Capability Acquisition and Sustainment Group to ensure expenditure is in accordance with the project delivery plan	1 (a), 1 (b), 2 (a) (ii), 2 (b) (i), 2 (b) (ii), 2 (b) (vi)	24 (b)
2.16	We recommend that the Defence Science and Technology Organisation be required to clearly articulate its value proposition. This would include examples and actual amounts of value created	1 (a), 1 (b)	
2.17	We recommend the Defence Science and Technology Organisation become part of the Capability Acquisition and Sustainment Group	1 (a), 1 (b), 2 (b) (i), 2 (b) (ii)	24 (b)
2.18	We recommend the Defence Science and Technology Organisation senior leadership be rationalised.	1 (a), 1 (b), 3 (c)	24 (g)
2.19	We recommend the Defence Science and Technology Organisation establish strong partnerships with academic and research institutions to leverage knowledge and create pathways into and out of academia and industry	1 (a), 1 (b), 2 (b) (i), 3 (f)	24 (b)
2.20	We recommend disbanding the Defence Science and Technology Organisation advisory board	1 (a), 1 (b), 3 (c)	
2.21	We recommend Defence, in partnership with academia and industry, review its developmental research priorities, their alignment with future force requirements and capacity to leverage allied partners to promote innovation	1 (a), 1 (b), 2 (b) (i), 3 (f)	24 (b)
3	Fully implement an enterprise approach to the delivery of corporate and military enabling services to maximise their effectiveness and efficiency	1 (a), 1 (b), 3 (b), 3 (d)	24 (b)
3.1	We recommend Defence define the estate need as determined by future force requirements and Government agree to dispose of all unnecessary estate holdings starting with the 17 bases identified in the 2012 Future Defence Estate Report	1 (a), 1 (b), 3 (c)	24 (b)
3.2	We recommend that Defence strengthen its capability to present options to Government for estate disposal including obtaining expert external advice as required	1 (a), 1 (b), 3 (c), 3 (f)	24 (b)
3.3	We recommend the Government amend the <i>Public Works Act 1969</i> to set a \$75 million threshold for referring proposed works to the Public Works Committee, and re-consider recent adjustments to the 2015-16 Budget operational rules that run counter to more efficiently managing investment spending	1 (a), 1 (b), 3 (c)	24 (b)

	FIRST PRINCIPLES REVIEW RECOMMENDATIONS	FIRST PRINCIPLES REVIEW TERMS OF REFERENCE	COMMISSION OF AUDIT TERMS OF REFERENCE
3.4	We recommend that the Associate Secretary be directed and resourced to implement enterprise information management that provides Defence with trusted information to inform decision-making and military interoperability, with the Vice Chief of the Defence Force as the design authority for the next generation of Command, Control, Communications, Intelligence, Surveillance and Reconnaissance	1 (a), 1 (b), 2 (b) (i), 2 (b) (ii), 2 (b) (vi) 3 (b), 3 (c)	24 (b)
3.5	We recommend that the information management agenda be governed at the Band 3/3 Star level by the Enterprise Business Committee to set overall direction and priorities, including the management of trade-offs and conflicts	1 (a), 1 (b), 2 (b) (i), 2 (b) (ii), 2 (b) (vi), 3 (b), 3 (c)	24 (b)
3.6	We recommend supporting the Chief Information Officer to meet these responsibilities by formally recognising the Chief Technology Officer as the technical authority with appropriate 'red card' decision rights	1 (a), 1 (b), 2 (b) (i), 2 (b) (ii), 2 (b) (vi), 3 (b), 3 (c)	24 (b)
3.7	We recommend that Defence establish enterprise-wide frameworks for architecture standards and master data management	1 (a), 1 (b), 2 (b) (i), 2 (b) (ii), 2 (b) (vi), 3 (b), 3 (c)	24 (b)
3.8	We recommend that Defence embark on a pragmatic implementation road map to standardise business and information processes and their supporting applications	1 (a), 1 (b), 2 (b) (i), 2 (b) (ii), 2 (b) (vi), 3 (b), 3 (c)	24 (b)
3.9	We recommend that Defence ensure adequate resourcing and funding for information management reform is prioritised as part of the fully costed 2015 Defence White Paper	1 (a), 1 (b), 2 (b) (i), 2 (b) (ii), 2 (b) (vi), 3 (b), 3 (c)	24 (a)
3.10	We recommend that geospatial information functions be consolidated into the Australian Geospatial-Intelligence Organisation following improved resourcing and connectivity	1 (a), 1 (b), 1 (c)	24 (b)
3.11	We recommend that the service delivery reform program, including full integration of the current Defence Materiel Organisation corporate functions, be completed	1 (a), 1 (b), 2 (a) (ii), 3 (b), 3 (d)	24 (b)
3.12	We recommend that all corporate services (with the exception of finance but including the Defence Security Authority) be consolidated under the Associate Secretary	1 (a), 1 (b), 2 (a) (ii), 3 (b) (d)	24 (b)
3.13	We recommend that all military enabling services (Joint Logistics Command Policy, Joint Health Command, Australian Defence College, Australian Civil-Military Centre) be consolidated under a Two-Star officer who reports to the Vice Chief of the Defence Force	1 (a), 1 (b)	24 (b)
4	Ensure committed people with the right skills are in appropriate jobs to create the One Defence workforce	1 (a), 1 (b), 1 (c), 1 (d), 2 (b) (i), 2 (b) (iii), 3 (c), 3 (d)	24 (b), 24 (g)
4.1	We recommend that, as part of the budget and planning process, Defence build a strategic workforce plan for the enabling functions, and incorporate workforce plans for each job family in order to drive recruitment, learning and development, performance and talent management	1 (a), 1 (b), 1 (c), 1 (d), 2 (b) (i), 2 (b) (iii), 3 (c), 3 (d)	24 (b)
4.2	We recommend that Defence employ Australian Defence Force personnel in non-Service roles only when it is critical to achieving capability and for a minimum of three years to achieve best value-for-money from the premium paid	1 (a), 1 (b), 3 (c), 3 (d)	24 (b)
4.3	We recommend that as many functions as possible be performed by public servants or outsourced if they are transactional in nature	1 (a), 1 (b), 3 (c), 1 (d), 3 (f)	24 (b), 24 (g)
4.4	We recommend that Defence review the entirety of its enabling and military corporate workforce to ensure that it supports the Australian Defence Force with the minimum of overlap and redundancy, and with the greatest overall economy, efficiency and effectiveness	1 (a), 1 (b), 3 (c), 1 (d)	24 (b), 24 (g)

First Principles Review Recommendations against Terms of Reference and Commission of Audit

	FIRST PRINCIPLES REVIEW RECOMMENDATIONS	FIRST PRINCIPLES REVIEW TERMS OF REFERENCE	COMMISSION OF AUDIT TERMS OF REFERENCE
4.5	We recommend that Defence reduce organisational layers; increase the spans of control of managers; align workforce standards in accord with the requirements of the Australian Public Service Commission; and engage external assistance to facilitate this work as required	1 (a), 1 (b), 3 (c), 1 (d), 3 (f)	24 (b), 24 (g)
4.6	We recommend that Defence implement a transparent performance management system that is consistently applied, recognises and rewards high performance and introduces consequences for underperformance and failure to deal with it	1 (a), 1 (b), 3 (f)	24 (b)
4.7	We recommend that as part of the performance management system, Defence take steps to create a culture where leadership, professionalism and corporate behaviour are valued and rewarded	1 (a), 1 (b), 3 (d)	24 (b)
5	Manage staff resources to deliver optimal use of funds and maximise efficiencies	1 (a), 1 (b), 3 (c), 3 (d)	24 (b)
5.1	We recommend that the use of the measures such as the teeth-to-tail ratio and the one third budget split should cease	1 (a), 1 (b), 3 (c), 3 (d)	24 (h)
5.2	We recommend that appropriate efficiency measures are developed which link to the delivery of agreed outcomes	1 (a), 1 (b), 3 (c), 3 (d)	24 (b)
5.3	We recommend that the focus on public service reductions as the primary efficiency mechanism for Defence cease	1 (a), 1 (b), 3 (c), 3 (d)	
5.4	We recommend that Defence manage its workforce numbers in line with good resource management where Defence is held to account for delivering on required outcomes within available resourcing	1 (a), 1 (b), 3 (c), 3 (d)	24 (b)
5.5	We recommend that as part of the implementation process, Defence examine the headquarters functions for opportunities to achieve more effective and efficient arrangements	1 (a), 1 (b), 3 (a), 3 (d)	24 (b), 24 (g)
6	Commence implementation immediately with the changes required to deliver One Defence within two years	3 (a)	24 (h)
6.1	We recommend no additional reviews on the organisational issues covered by this Review are imposed on Defence, particularly within the early years of implementation	3 (a)	24 (h)
6.2	Past reviews and current reform initiatives should be assessed for currency and alignment to the One Defence model	3 (e)	
6.3	We recommend establishing an Oversight Board to provide close external scrutiny, advice on implementation progress and regular reports to the Minister	3 (a)	24 (h)
6.4	We recommend the Minister, with input from the Department and the Oversight Board, report progress on implementation to the Government in March 2016 and March 2017	3 (a)	24 (h)
6.5	We recommend stability in the key leadership positions, particularly over the next two years to provide consistency of direction and ownership of the change	1 (a), 1 (b), 3 (a)	24 (h)

Annex B: Framework for the First Principles Review of Defence



Annex C: Recurring themes identified in recent reviews

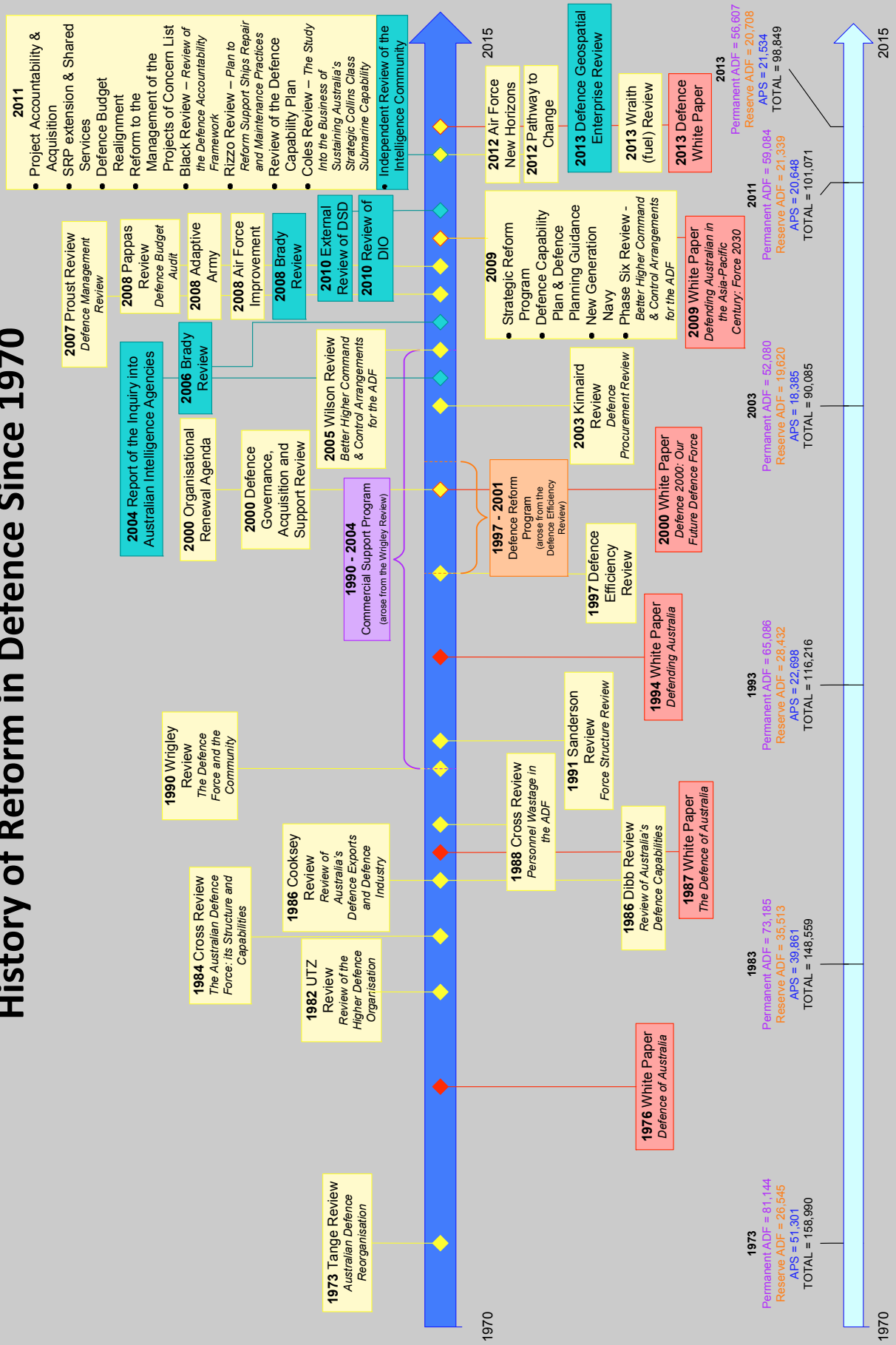
The recurring themes have been identified in the recent, significant reviews of the Australian Defence Force and the Department of Defence cited below:

- McIntosh, Malcolm, et al., *Future Directions for the Management of Australia's Defence - Report of the Defence Efficiency Review*, Canberra, March 1997—referred to as the Defence Efficiency Review;
- Department of Defence, *Report on Defence Governance, Acquisition and Support* (prepared by KPMG), Canberra, April 2000—referred to as Defence Governance, Acquisition and Support;
- Proust, Elizabeth, et al., *Report of the Defence Management Review*, Canberra, March 2007—referred to as the Proust Review;
- Kinnaird, Malcolm, et al., *Defence Procurement Review 2003*, Canberra, August 2003—referred to as the Kinnaird Review;
- Mortimer, David, *Going to the Next Level – the report of the Defence Procurement and Sustainment Review*, Canberra, September 2008—referred to as the Mortimer Review;
- Pappas, George, *2008 Audit of the Defence Budget*, Canberra, April 2009—referred to as the Pappas Review;
- Black, Rufus, *Review of the Defence Accountability Framework*, Canberra, January 2011—referred to as the Black Review;
- Rizzo, Paul, *Plan to Reform Support Ship Repair and Management Practices*, July 2011—referred to as the Rizzo Review;
- Department of Defence, *Review of Shared Services in Defence* (prepared by McKinsey and Company), Canberra, July 2011—referred to as Shared Services;
- Broderick, Elizabeth, *Review into the Treatment of Women in the Australian Defence Force - Phase 2 Report*, Canberra, August 2012—referred to as the Broderick Review; and
- Coles, John, et al., *Study into the Business of Sustaining Australia's Strategic Collins Class Submarine Capability*, Canberra, November 2012—referred to as the Coles Review.

The table overleaf is adapted from that on pages 86 to 88 of the Australian National Audit Office's October 2013 audit report *Capability Development Reform*, and sets out recurring themes relating to the capability development and delivery process. A more general timeline of reviews of the Defence portfolio since 1970 is presented on the following page.

	APRIL 2000 DEFENCE GOVERNANCE, ACQUISITION AND SUPPORT	AUG. 2003 KINNAIRD REVIEW	SEPT. 2008 MORTIMER REVIEW	APRIL 2009 PAPPAS REVIEW	JAN. 2011 BLACK REVIEW
Turnover of capability development staff	High turnover of capability development staff prevents the development of skills and experience necessary in such a complex and specialist area.	✓	✓	✓	✓
Chronic and critical shortage of skills essential to develop robust major capability proposals	Cost estimation is a technical discipline and requires specialist skills. High levels of skill are critical to delivering capability and making accurate cost estimates that enable informed capability/cost decisions. Capability Defence Group personnel (both cost estimators and Desk Officers—now known as ‘project managers’) have low average cost-estimating experience. Cost estimates must reflect whole-of-life costs.	✓	✓	✓	✓
Initial entry of a project into the Defence Capability Plan warrants close attention. The Defence Capability Plan should be realistic, affordable, prioritised and consistent with government expectations.	Underestimation of the cost of new equipment specified in the Defence Capability Plan and of the associated operating costs, and lack of prioritisation of Defence Capability Plan projects. Over-programming and over-planning, which include both including more projects in the Defence Capability Plan than Defence can afford and starting more projects than required, to accommodate potential schedule slippage in projects.	✗	✓	✓	✓
Lack of independent scrutiny of proposals undermines quality.	Absence of scrutiny of capital investment proposals to assess affordability, schedule risk and commercial aspects of acquisition by staff who are organisationally independent of the proposal sponsor.	✓	✓	✓	✓
Technical risk is critical and should be clearly and consistently assessed and communicated to government.	Technical risk is a major factor in the acquisition of new defence capabilities. It is the major cause of both post-approval project slippage and cost escalation.	✗	✓	✓	✓
Acquisition decisions should be based on a comprehensive whole-of-life cost estimate.	Understanding whole-of-life costs is essential to effective decision-making on capability options. Inadequate attention given to managing and costing defence capabilities on a whole-of-life basis results in funding shortfalls for ongoing operating, maintenance and support costs.	✓	✓	✓	✓
Effective information systems that provide cost information for major capabilities	Defence systems cannot readily provide consistent, reliable or complete information of the operating cost of current capabilities. Incomplete cost information about current capabilities prevents Defence from making reliable fact-based estimates of future operating costs, and means estimates of those costs are based on general assumptions rather than reliable historical data on cost drivers.	✓	✓	✓	✓
Rigorous analysis of costs and risks associated with requirements set beyond those of off-the-shelf equipment	Requirements beyond off-the-shelf equipment generate what Mortimer described as ‘disproportionately large increases to the cost, schedule and risk of projects’ and therefore should be based on ‘a rigorous cost-benefit analysis of additional capability sought against the cost and risk of doing so’. This analysis must be clearly communicated to government. Each and every decision to pursue a unique Australian solution needs to be made with a full understanding of not just the benefits but also the extra cost and risk of doing so.	✓	✓	✓	✓
Committees and accountability	Too many committees with too many members; representational in nature rather than limited to those essential to provide informed advice to accountable decision-makers; features of committees result in dissipated accountability and responsibility; improved committee processes required.	✓	✓	✓	✓

History of Reform in Defence Since 1970



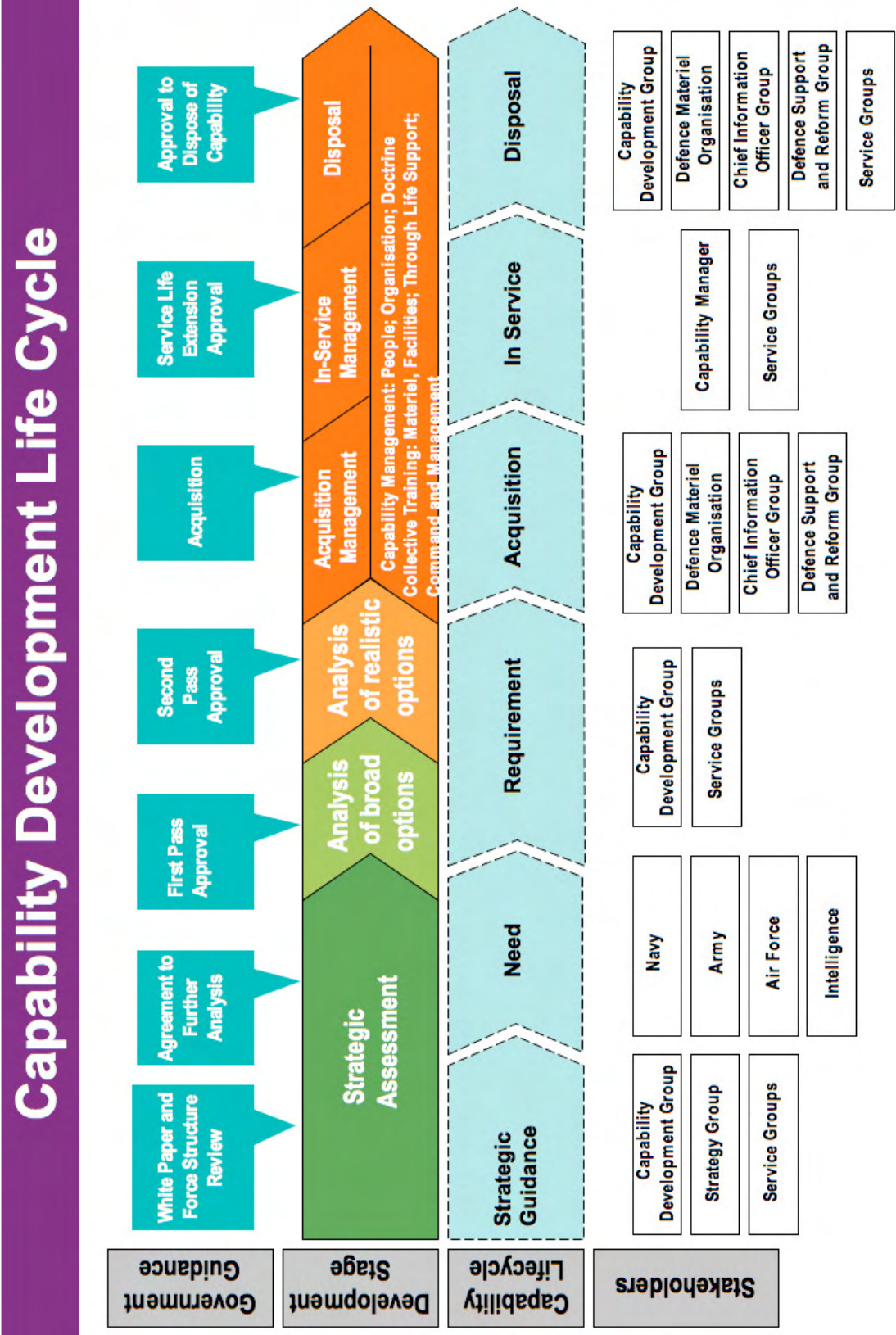
Annex D: Growth in Defence senior leadership numbers

Changes to Defence's top-structure June 1998 to June 2014, based on headcount data

	1998	2014	CHANGE	
3 star	4	7	75%	increase
2 star	25	44	76%	increase
1 star	83	149	80%	increase
All star ranked	112	200	79%	increase
Australian Defence Force other ranks	55,062	56,836	3%	increase
Australian Defence Force other ranks per star-ranked officer	492	284	-42%	decrease

Senior Executive Service 3	7	13	86%	increase
Senior Executive Service 2	27	51	89%	increase
Senior Executive Service 1	53	110	108%	increase
All Senior Executive Service	87	174	100%	increase
non- Senior Executive Service Australian Public Service	17,856	21,020	18%	increase
other Australian Public Service per Senior Executive Service	205	121	-41%	decrease

Senior leaders	201	374	86%	increase
Other staff	72,918	77,856	7%	increase



Annex F: Australian Public Service classifications and Australian Defence Force equivalent ranks

AUSTRALIAN PUBLIC SERVICE CLASSIFICATION	ARMY RANK	ROYAL AUSTRALIAN NAVY RANK	ROYAL AUSTRALIAN AIR FORCE RANK	AUSTRALIAN DEFENCE FORCE EQUIVALENT RANK
Australian Public Service 1	Private	Seaman	Aircraftman	E00 E01 E02
		Able Seaman	Leading Aircraftman	E03
	Lance Corporal			E04
Australian Public Service 2	Corporal	Leading Seaman	Corporal	E05
Australian Public Service 3	Sergeant	Petty Officer	Sergeant	E06
	Staff Sergeant			E07
Australian Public Service 4	Warrant Officer Class 2	Chief Petty Officer	Flight Sergeant	E08
	Officer Cadet	Midshipman	Officer Cadet	O00
	Warrant Officer Class 1	Warrant Officer	Warrant Officer	E09 E10
	2nd Lieutenant	Acting Sub Lieutenant	Pilot Officer	O01
	Lieutenant	Sub Lieutenant	Flying Officer	O02
Australian Public Service 5	Captain	Lieutenant	Flight Lieutenant	O03
Australian Public Service 6	Major	Lieutenant Commander	Squadron Leader	O04
Executive Level 1	Lieutenant Colonel	Commander	Wing Commander	O05
Executive Level 2	Colonel	Captain	Group Captain	O06
Senior Executive Service Band 1	Brigadier	Commodore	Air Commodore	O07
Senior Executive Service Band 2	Major General	Rear Admiral	Air Vice Marshal	O08
Senior Executive Service Band 3	Lieutenant General	Vice Admiral	Air Marshal	O09
Secretary	General	Admiral	Air Chief Marshal	O10

Annex G: List of stakeholder interviews

Current and previous members of Parliament	
Darren Chester	Parliamentary Secretary to the Minister for Defence
Jason Clare	Former Minister for Defence Materiel and Science
Greg Combet	Former Minister for Defence Materiel and Science
Stephen Conroy	Deputy Leader of the Opposition in the Senate
Mathias Cormann	Minister for Finance
John Faulkner	Former Minister for Defence
David Fawcett	Senator for South Australia
David Feeney	Former Parliamentary Secretary for Defence
John Howard	Former Prime Minister
David Johnston	Former Minister for Defence
Mike Kelly	Office of the Leader of the Opposition
Grant Lovett	Office of the Treasurer
Brendan Nelson	Former Minister for Defence
Stuart Robert	Assistant Minister for Defence
Andrew Shearer	Office of the Prime Minister
Standing Committee for Foreign Affairs Defence and Trade	

Departments and Agencies	
Elizabeth Broderick	Sex Discrimination Commissioner
Megan Clarke	Former Chief Executive CSIRO
Allan Gygnell	Former Director Office of National Assessments
Jane Halton	Secretary Department of Finance
Chris Jordon	Commissioner of Taxation
Simon Lewis	Secretary Department of Veteran Affairs
Ian McPhee	Auditor-General
Martin Parkinson	Former Secretary Department of the Treasury
Michael Pezzullo	Secretary, Department of Immigration and Border Protection
Steve Sedgwick	Former Commissioner Australian Public Service Commission
Michael Thawley	Secretary, Department of the Prime Minister and Cabinet
Ian Watt	Former Secretary Department of the Prime Minister and Cabinet

Annex G: List of stakeholder interviews (Continued)

Academia and the community	
Ross Babbage	Professor
Paul Dibb	Emeritus Professor, Australian National University
Alan Dupont	Professor of International Security, University of New South Wales
Peter Høj	Vice-Chancellor, University of Queensland
Neil James	Executive Director, Australian Defence Association
Mark Thompson	Australian Strategic Policy Institute
Hugh White	Professor of Strategic Studies, Australian National University
John White	Winter/White AWD Report

United Kingdom	
Paul Blakiston	Director Future Defence Equipment and Support Model
Simon Bollom	Chief of Material (Air)
Vicki Brookes	Head Defence Reform Unit
Barry Burton	Head of Commercial (Defence Equipment and Support)
Chris Deverell	Chief of Material (Land)
Bernard Gray	Chief of Defence Material
Simon Cholerton	Operations Director (United Kingdom Trade and Industry)
Stephen Hillier	Deputy Chief of the Defence Staff (Military Capability)
Will Jessett	Director Strategy and Planning
Peter Levene	Chair, Defence Reform Group
Tom McKane	Former Director General Strategy
Jonathan Slater	Director General Head Office and Commissioning Services
David Williams	Director General, Finance
Pete Worrall	Chief of Material (Joint Enablers)

Industry and Unions
Australian Submarine Corporation
Australian Manufacturing Workers' Union
BAE Systems
Bechtel Corporation
Boeing Company
Community and Public Sector Union
Dyncorp International
Ernst and Young
Hans J Ohff
Jacobs Engineering Group
KBR Incorporated
KPMG
LEK Consulting
Lockheed Martin
The May Group
Noetic Group
Northrop Grumman Corporation
PriceWaterhouseCoopers
Professionals Australia
QinetiQ Group
Raytheon Company
Strategy&
Teekay Shipping
Thales Group

Annex G: List of stakeholder interviews (Continued)

Department of Defence – (Current and former)	
Marc Ablong	First Assistant Secretary White Paper
Timothy Barrett	Chief of Navy
Peter Baxter	Deputy Secretary Strategy
Mark Binskin	Chief of the Defence Force
Geoffrey Brown	Chief of Air Force
John Caligari	Chief of Capability Development Group
Chris Deeble	Program Manager Joint Strike Fighter
Harry Dunstall	General Manager Commercial
Maria Fernandez	Director Australian Geospatial Organisation
Patrick Fitzpatrick	Director General Maritime Acquisition
Mike Gibson	First Assistant Secretary Capability Investment and Resources
David Gould	General Manager Submarines
Justine Greig	Director General People Strategy and Culture
Ray Griggs	Vice Chief of the Defence Force
Steve Grzeskowiak	Deputy Secretary Defence Support and Reform
Stephen Gumley	Former CEO Defence Materiel Organisation
Allan Hawke	Former Secretary, Department of Defence
Neil Hart	Co-lead Force Structure Review Team
Tony Hindmarsh	Head Defence Materiel Organisation Reform
Angus Houston	Former Chief of the Defence Force
David Hurley	Former Chief of the Defence Force
David Johnston	Chief of Joint Operations
Peter Jones	Former Chief Capability Development Group
Michelle Kelly	Head Defence Industry Division
Warren King	Chief Executive Officer Defence Materiel Organisation
Peter Lawrence	Chief Information Officer
Duncan Lewis	Former Secretary, Department of Defence
Ed Louis	Director General Independent Project Performance Office
Kate Louis	Assistant Secretary White Paper Enterprise Management
Carmel McGregor	Former Deputy Secretary Defence People
Shireane McKinnie	General Manager Joint, Systems and Air

Department of Defence – (Current and former)	
Paul McLachlan	Head Land Systems
Steve Meekin	Deputy Secretary Intelligence and Security
David Morrison	Chief of Army
Terry Oldfield	Director Gate Reviews
Richard Oliver	Head People Policy and Culture
Leisl O'Meara	General Counsel, Defence Materiel Organisation
Neil Orme	Co-lead Force Structure Review Team
Phillip Prior	Chief Finance Officer
Dennis Richardson	Secretary of Defence
Brendan Sargeant	Chief Operating Officer
Rebecca Skinner	Deputy Secretary Defence People
Ric Smith	Former Secretary Department of Defence
Colin Thorne	General Manager Land and Maritime
Nick Warner	Former Secretary Department of Defence
Steve Wearn	Chief Finance Officer Defence Materiel Organisation
Adrian Wellspring	Director APS Career Development and Talent Management
Alex Zelinsky	Chief Defence Scientist

Defence Boards and Advisory Committees	
Ian Chubb	Defence Science and Technology Advisory Board
Catherine Fox	Gender Equality Advisory Board
Michael L'Estrange	Defence Science and Technology Advisory Board
Frank Lewincamp	Independent Project Performance Office
Julie McKay	Gender Advisor to the Chief of the Defence Force
Ralph Neumann	Independent Project Performance Office
Paul Rizzo	Chair, Defence Audit and Risk Committee
Intelligence and Security Round Table	
Materiel Audit and Risk Committee	
White Paper Panel	

Annex G: List of stakeholder interviews (Continued)

Public Submissions

84 public submissions were received. 17 met the editorial guidelines for publication and included submissions from the following interested people, unions and industry:

- Mr Phil Andrews
- Mr Bob Williams
- Mr Chris Donald
- Mr Phil Andrews
- Mr Warren Canning
- Accenture
- Australian Academy of Technological Sciences & Engineering
- Australian Business Defence Industry
- Australian Industry & Defence Network
- Australian Manufacturing Workers' Union
- BAE Systems
- Community and Public Sector Union
- Jacobs Australia
- Kiah Consulting
- QinetiQ Australia
- Royal United Services Institute
- The Returned and Services League of Australia

Annex H: Departmental Secretariat

Our sincere thanks to the following members of the departmental secretariat:

Roxanne Kelley	Head Reform and Corporate Services
Paul Symon	Military Officer First Principles Review
Shannon Frazer	Assistant Secretary Enterprise Reform
Jacob Boyle	Director First Principles Review (Governance and accountabilities)
Kim Bond	Director First Principles Review (Enablers and workforce)
Jarrod Howard	Director First Principles Review (Capability Development)
Theresa Coxon	Director First Principles Review (Communications)
Anita Misic	Executive Officer
Phoebe Jenkins	Executive Assistant

