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Abstract

The Australian Defence Force is held in high regard; the Department of Defence is not. Longstanding concerns about inefficiency, compounded by a succession of fiascos and bungles, have entrenched the perception that Defence is poorly managed. Earlier attempts at reform have yielded mixed, often disappointing, results (see Ergas and Thomson 2011), and the years since 2009 have seen a series of reviews aimed at improving performance, culminating in 22 defence-related reviews in 2011–12 alone.

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Australia's Defence: A Review of the 'Reviews'

Henry Ergas¹

The Australian Defence Force is held in high regard; the Department of Defence is not. Longstanding concerns about inefficiency, compounded by a succession of fiascos and bungles, have entrenched the perception that Defence is poorly managed. Earlier attempts at reform have yielded mixed, often disappointing, results (see Ergas and Thomson 2011), and the years since 2009 have seen a series of reviews aimed at improving performance, culminating in 22 defence-related reviews in 2011–12 alone.

Eight recent reviews deal primarily with the fallout from the so-called Skype incident at the Australian Defence Force Academy (ADFA), in which an ADFA cadet allegedly broadcast images of himself and a female cadet engaged in sex. While those reviews are of considerable interest and potentially significant consequence, they will not be discussed here; rather, my focus is on the reviews which go directly to the efficiency with which 'Defence' uses resources.²

The most far-ranging reviews are the Audit of the Defence Budget, undertaken by George Pappas with support from McKinsey and Company (Pappas 2009) and the Review of the Defence Accountability Framework, undertaken by Rufus Black (Black 2011). Others, such as the Collins Class Sustainment Review (Coles 2011) and the Plan to Reform Ship Repair and Management (Rizzo 2011), are more narrowly focused.

Despite the range there are some common themes. Central among these are deficiencies in Defence's management systems. Simply put, there are many plans, but no plan; myriad accountabilities, but no accountability. The result is a structure in which decisions are poorly integrated and in which individuals, while they know what they are intended to do, are not responsible for its being done. Moreover, while the structure generates torrents of data, the sheer scale and diffusion of information, and the lack of tight connection between decisions on the one hand and what is measured on the other, further undermine accountability. Coles, for example, notes an instance in which 'a junior officer [was] required to render a very detailed progress report every day which was

1 The University of Wollongong and Deloitte Access Economics; ergas.henry@gmail.com The author is as usual, greatly indebted to Mark Thomson for our many discussions of these issues. Responsibility for the opinions expressed lies entirely with the author.

2 Henceforth 'Defence' is used in the wider sense of both the Department and the ADF.

sent to over 100 recipients', with presumably few reading it, and even fewer feeling any sense of responsibility for the progress it supposedly tracked. Adding to the lack of accountability is the reluctance of senior management, and of the leadership in the services, to use what powers they have to hold individuals to account for poor performance. The unsurprising consequence is a chronic failure to exploit opportunities for improvement, accompanied by periodic instances of acute breakdown.

The Collins Class submarine program: Murphy was an optimist

Nothing better illustrates the chronic problems than the saga of the Collins Class submarines, now in its twenty-fifth year. Astutely analysed in *Lessons from Australia's Collins Submarine Program* (Schank *et al.* 2011), this was a project which showed Mr Murphy, of the eponymous law, to be an incorrigible optimist, at least as far as major defence ventures are concerned.

Yet it would be wrong to blame bad luck for the Collins' difficulties. Rather, from the start, almost everything that could *be done* wrong was *done* wrong. As the Coles review puts it, 'the problems originate from the very beginning of the program when, perhaps without fully appreciating the potential consequences, the Commonwealth embarked on the acquisition of a submarine which, for good reason, is quite unlike any other in the world'. Many years later, Coles concludes, we are still in a situation where 'despite the fact that virtually all senior people we spoke to were clear that the Collins Class capability is "strategic" for Australia, there is no clear or shared public understanding of why this is a strategic capability nor of the implications this has for sustainability.'

As for acute breakdowns, those too have been in abundant supply, with the most recent being in September 2010 when the Chief of Navy imposed an 'operational pause' on the seaworthiness of the 'amphibious landing platform' HMAS Manoora,³ causing a collapse in Australia's amphibious ship capability. That collapse, which would have made it impossible for the ADF to respond promptly to a major disturbance in our archipelagic region, is thoroughly diagnosed in the review undertaken by Paul Rizzo. The causes, he finds, include 'poor whole-of-life asset management, organisational complexity and blurred accountabilities, inadequate risk management, poor compliance and assurance, a "hollowed-out" Navy engineering function, resource shortages in the System Program Office in DMO [the Defence Materiel Organisation], and a culture that places the short-term operational mission above the need for technical integrity.'

3 Since decommissioned.

Even more disturbingly, the Rizzo review notes that these problems were 'long-standing, well known to Defence and DMO, and the subject of many prior reports'. And there are indeed close parallels between the conclusions of the Rizzo review and those of the 2007 Board of Inquiry into the Sea King accident at Nias Island, which concluded that the tragedy causing the death of nine ADF members during the response to the Indian Ocean tsunami was not an 'isolated random event' but due to 'systemic failings across the ADF and parts of the Defence organization' (Royal Australian Navy 2007).

The Pappas review: Linking weapons systems selection to future military challenges

It is against the backdrop of those grim assessments that the reviews' recommendations must be seen. Some of those recommendations have been somewhat overtaken by events. This is especially so for the cost-reduction recommendations of the Pappas review, which formed the basis of a major search for savings known as the Strategic Reform Program (SRP), initiated in the 2009 Defence White Paper.

The SRP was somewhat misleadingly cast as aimed at achieving efficiencies. But rather than increases in defence output per unit of output, much of it, in reality, simply involved spending less to produce less. As Thomson (2012) shows, some of the savings targets were more credible than others. Moreover, while some of the targets (notably for sustainment spending) were achieved, others (notably for personnel costs) were not, statements by Defence to the contrary notwithstanding. Be that as it may, the SRP — described in the 2010–11 Budget as 'the Government's key initiative in 2010–11' — was effectively abandoned in the 2012 Budget, to be replaced by essentially arbitrary reductions in allowed outlays.

The Pappas review did, however, also recommend changes to Defence's planning and control framework, including a streamlined planning process and, especially, a tighter integration of strategic planning on the one hand and capability decisions on the other. Achieving such tighter integration between the identification of future military challenges and the selection of major weapons systems has been a central goal of Australian defence reformers since the days of Sir Arthur Tange (Secretary of the Department of Defence from 1970 to 1979).⁴ Tange was determined to introduce into Defence's weapons-acquisition process

⁴ Tange's 1973 report, 'Australian Defence: Report on the Reorganisation of the Defence Group of Departments', laid the basis for the fusion in 1976 of the former service ministries into a single department headed by a 'dyarchy' of a civilian Secretary and a military Chief of the Defence Force (CDF).

the techniques of systems analysis and program budgeting pioneered by Robert McNamara during his tenure as US Secretary of Defense (1961–68). Those techniques were, in Tange's view, crucial to moving away from a 'requirements' approach, in which the services specified the weapons systems they intended to purchase with little or no regard to cost. Rather, Tange insisted, a 'disciplined' framework needed to be applied, which balanced system capabilities with costs and took full account of substitution possibilities between alternative ways of achieving a military objective. While some progress in this direction was made in the Tange years and in the subsequent decade, by the late 1990s those gains had been lost, and capabilities selection had returned to being largely based on 'wish lists' and logrolling between the services.

The Pappas report also highlighted the problems that still arise in the actual acquisition of capabilities, including cost overruns and serious delays. The formation of the Defence Materiel Organisation in 2000 as a separate, specialist acquirer of defence materiel and sustainment services on the services' behalf was intended to put acquisition on a commercial basis. Subsequent reviews, notably by Malcolm Kinnaird in 2003 (Kinnaird 2003) and by David Mortimer in 2008 (Mortimer 2008), brought new disciplines to the acquisition process, including a two-stage review process before major programs proceed. Nonetheless, Pappas shows, cost overruns and delays persist, with the greatest problems being in projects that involve systems especially built for, or extensively customized to, Australian conditions. In the light of those problems, Pappas, echoing an earlier recommendation by Mortimer, recommends that all 'customised' solutions be subjected to rigorous cost-benefit testing compared to a military off-the-shelf (MOTS) alternative.

The Black review: Accountability and contracts

The Black review takes Pappas' emphasis on improved planning and control and pushes it considerably further. While the Black review is littered with deplorable management jargon, at its heart is a sensible attempt to deal with three principal/agent problems that are of central importance to defence efficiency. These are the relations between the government as the principal and Defence as its agent; between the Department as the principal and its staff as the agent; and between each of the military services as the principal and the support services of the Department and DMO as their agent. In each of these, Black proposes ways to clarify expectations, improve the measurement of performance and enhance the incentives for success.

Specifically, Black notes that while Defence has myriad plans, and a complex, multi-tier planning process, it lacks a corporate plan. Rather, it has a Defence

Management Finance Plan, which, in practice, is an amalgam of a range of stand-alone plans, often prepared by individual fiefdoms within Defence, with targets for the current year and projections four to 10 years ahead. In contrast, Black proposes an overarching annual corporate plan that would set out succinctly the guidance for the Department, including the (preferably quantified) targets it would achieve. This would both allow better monitoring of Defence by the government and Parliament, and allow improved communications of priorities within Defence itself.

Such a plan, Black suggests, would be naturally linked to the objectives set for individual units within Defence, and hence would inform a cascading series of targets and associated performance indicators, reaching down to individuals. It would, in this way, help address principal/agent issues within Defence, though Black notes three additional prerequisites for enhanced accountability. First, the current structure of management by committee, which diffuses responsibility and excuses poor performance, must be replaced by a system in which major decisions are associated with a clearly identified individual decision-maker. Second, the practice of frequent rotation, which results in uniformed personnel shifting jobs every two years or so, needs to be replaced by an arrangement which provides sufficient stability that performance can be assessed, accompanied by opportunities to develop and exploit specialist skills in areas such as project costing and delivery. Last but not least, there must be real rewards and penalties associated with individual performance, though Black emphasises (and, in my view, somewhat exaggerates) the constraints imposed by the *Public Service Act 1999* and by the regulations made under the *Defence Act 1903* (which apply to members of the ADF).

Finally, with respect to issues between the three services and the procurement and support arms of the Department, Black proposes substantial reforms to the existing system of performance agreements. While these generally include targets and associated metrics, Black finds that the metrics rarely allow timely and effective monitoring of outcomes. Additionally, Black notes that the agreements neither include unit-cost information nor allow for trade-offs between unit cost and capability. Black recommends that the agreements be structured in a way that both informs and permits such trade-offs, presumably along with some mechanism for the sharing of gains. This would help move these agreements closer to customer/contractor relationships in the commercial world.

There is much to commend in these recommendations. But there are also inherent limitations. Black, for example, greatly overestimates the power of 'contract like' mechanisms within what remains a centrally planned economy, with no scope for contestability, few tools for price discovery, and far weaker incentives to seek gains than to avoid losses. Moreover, long experience in Defence itself

shows that developing the kinds of contracts Black recommends is as costly and time-consuming as it is technically challenging, though that is not to say a move in that direction could not yield net gains.⁵

The greatest weakness, however, lies in the failure of the reviews to address this question: how it is that the difficulties have proven so persistent in the face of determined reform efforts. There is, in these reviews, a startling absence of historical perspective: each does a good job of addressing its remit; but none asks why previous, no less competent, reviews did not succeed.

The most natural response to this question would be in terms of the phenomenon Sigmund Freud, in his famous essay on 'Beyond the Pleasure Principle', termed 'repetition compulsion': the tendency in neurosis to repeat behaviour, even when it repeatedly leads to failure.

In the mind of the neurotic, Freud stressed, the mere fact of repetition gives behaviour a degree of legitimacy, an element of predictability and routine, which helps control the external world and is preferable to the pain and stress of breaking out of the cycle of failure. Like individuals, public-sector institutions suffer from behavioural pathologies — pathologies made all the more durable by the fact that, unlike firms in the private sector, those institutions are not subject to displacement by more effective competitors. Moreover, the fact that success and failure are so difficult to measure, and that assessments can be so readily fudged, only exacerbates the problems. The inherent tendency of bureaucracies to indulge in 'group think', to suppress the awareness of difficulties, to convert attitudes into hard and fast organisational cultures, and to treat dissent as disloyalty, then helps ensure that what has failed once will fail again and again.

There are certainly elements of this in Defence, perhaps to an even higher degree than in other areas of public administration. But Defence's difficulties in recent years stem less from those pathologies than from the evolution it has undergone.

'Things fall apart; the centre cannot hold'

Without trying to fill in the details, a sketch of the relevant story could run along the following lines.

Subsequent to the Tange reforms of the 1970s, Defence entered into a long period of retrenchment, in which defence spending grew very slowly, if at all. Indeed, as Thomson (2012) points out, the defence budget, measured in real

5 Writing commercial contracts for the relevant services will usually be very difficult. Yet it remains desirable to try to travel in that direction, as it forces Defence to try as hard as it can to specify mutual expectations. But the journey is, perhaps, more valuable than the destination.

terms, was greater in 1985–86 than it was a decade later. The result was a force whose capabilities were extremely limited, as became painfully apparent in the Timor intervention of 1999–2000. That intervention acted as a wake-up call to the Howard government, which began a process of increased spending that accelerated with the terrorist attacks of 11 September 2001. The ADF expanded by about 20 per cent; defence spending in real terms grew by over 3 per cent annually, so that the defence budget (again, in real terms) increased from \$17 billion at the end of the 1990s to \$27 billion in 2009–10; and a slew of new, extremely sophisticated equipment was brought into service.

All this allowed substantial increases in capability. Indeed, it is difficult to believe the ADF could have sustained the range and tempo of operations in which it has since been involved without the post-1999 expansion. Yet those increases in capability were extremely uneven, with far greater improvements in the Army than in the other services. And the management processes in Defence itself failed to keep up with the greater scale on which Defence operates, the greater complexity and cost of the platforms it operates, and the greater demands of accountability being placed on government departments generally. Overall, the centre did not prove strong enough to control the greatly scaled-up parts, leading to a complete mismatch between promises and achievements.

The extensive reorganisation and outsourcing of tasks undertaken in the Defence Reform Process (DRP) of 1997–99 contributed materially to the severity of the problems that mismatch eventually created. The DRP had three consequences. First, it led to a significant loss in technical capability, as too little attention was paid to ensuring sufficient skills were retained within the ADF for it to fulfil its core responsibilities. Second, the DRP introduced a corporate model based on the centralised provision of core services, but without the processes needed to manage shared services in the highly complex matrix structure of Defence. And third, the DRP failed to put in place the management accounting systems that would allow cost control and could provide a basis for determining and monitoring outcomes.

What might otherwise have been mere weaknesses thereby became crippling structural flaws. An unduly ambitious procurement program added to the difficulties, as commitments to new platforms exceeded the capacity of DMO to manage, of industry to deliver and, ultimately, of the government to fund. To this unhappy mix, the election of the Rudd government brought new woes, as that government, with its expansive vision of Australia's role, was as willing to make bold commitments to ends as it was reluctant (and ultimately unable) to commit the requisite means. That gap, most manifest in the wake of the 2009 White Paper (Department of Defence 2009), led to an ever greater tension between goals and resources, which transformed long-running problems into

crises. As these broke out, the government responded through a sequence of reform programs that any organisation would have found difficult to absorb and implement, much less one with as weak a corporate centre as Defence.

And that is the nub of the problem. Lasting reform is impossible unless it greatly strengthens Defence's corporate centre, in terms of its ability to challenge the services — for instance, on capability decisions — develop meaningful plans, and monitor and enforce outcomes. That was always a problem with the Department: unlike McNamara, who had greatly strengthened the Office of the Secretary of Defense (OSD), Tange managed through sheer intelligence and force of personality. The result was that while the US OSD was able to force the services to substantially lift their game, its Australian counterpart was far too weak to do so.

As a result, even by the 1980s, it was apparent that the corporate headquarters function in Defence was unable to achieve Tange's goal of imposing 'a disciplined relationship between strategy and force structure within the constraints of what is financially feasible' (Tange 2008: 22). And here too the DRP, in its quest to avoid duplication, made matters worse by removing that element of review and criticism of the services' capability wish lists that civilian analysts had previously provided.

But none of the proposals advanced in the reviews tackle head-on the need to significantly strengthen Defence's corporate centre, nor has the government shown any appreciation of its importance. It is therefore difficult to see how the sensible outcomes of these reviews could be successfully implemented in their substance; rather, merely being adhered to in their form (as has happened to so many reform proposals in the past).

There is every risk that the proposals advanced in these reviews will go that way. That would be a pity, for they reflect a mass of careful, considered work. But then again, so did their predecessors.

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