

PLUMBING THE MURKY DEPTHS

ASC stumbles as vultures circle over Sea 1000 carve up plan



■ Trevor J Thomas/ADELAIDE

Each year, a statement in the financial accounts of ASC Pty Ltd seeks to reconcile the 'liquidity risk' of a unique enterprise – not only in terms of the products it produces – but also in terms of: its ownership (on behalf of taxpayers) by the Minister for Finance & Deregulation; and the extent to which the company's Board is generally left to manage the enterprise without expressed written directions from the Finance Minister, nor interventions from its principal customer, the Royal Australian Navy.

ASC is a Government Business Enterprise (GBE), constituted under the Commonwealth Authorities and Companies Act 1997, which requires the company to operate efficiently, earn a commercial rate of return and observe a standardised and transparent reporting framework. Strict procedures governing the relationship between the company, the Department of Defence and the Department of Finance & Regulation are said to have been put in place.

FINANCIAL STABILITY RISK: According to ASC's most recent (2008/09) Annual Report – and as similarly expressed in earlier annual reports – liquidity risk is, "the risk that the Group will not be able to meet its financial obligations as they fall due." Further, it is said the approach of ASC's directors to managing liquidity is to "ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damaging the Group's reputation."

On the back of six months of turmoil following the departure of its managing director last June, 2009/10 is shaping up as a year where ASC's approach to honouring its 'liquidity risk' provisions might just be tested, as the company seeks to absorb additional costs due to: a June 2009 organisational restructuring and round of executive-level and contractor retrenchments; a continuing drain on cash as it completes a

Key Points

- **Following the scrapping of plans for a sale to private** investors, Australia's principal submarine maintainer and air warfare destroyer builder, ASC Pty Ltd, has had a rough six months since the departure of its managing director.
- **A reorganisation and round of top level redundancies** imposed by Defence in response to plummeting submarine availability rates, was next followed by an engine failure after HMAS 'Collins' had just completed maintenance.
- **Facing a potentially expensive warranty claim** – whilst still digesting \$100+m of new infrastructure expenditure – ASC revenues will also be squeezed by a forced re-negotiation of its 25-year 'Collins'-class submarine support contract.
- **Now facing up to mounting challenges in front of the** company is a new, and more youthful, board of directors and new managing director, whose most recent job was overseeing support for the UK's nuclear submarine fleet.

\$135m infrastructure investment program; and a test of the robustness of provisions made in earlier years to sustain a major submarine warranty claim.

In addition, ASC directors will also have to carefully manage a large rise in operating costs and inventory holdings due to the ramp up of air warfare destroyer construction (particularly when AWD blocks start arriving for integration), whilst also suffering a decline in submarine repair-related profitability, due to a forced (by the Defence Materiel



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Organisation) re-negotiation of its 'golden egg' – the 25-year (15+5+5) through life support (TLS) Agreement, originally signed off by the Howard Government in 2003 to underpin stability in ASC's forward revenue projects, as an aid to attracting investors for the intended sale of the company back to the private sector. The sole-source TLS Agreement is significant in underpinning over half of ASC's baseline revenue of \$346.1m. [The Navy budgets some \$330m in direct spend for the 'Collins'-class boats of which around \$200m goes directly to ASC under the TLS Agreement provisions.]

Up until the current financial year, ASC has been a one-product company – initially as builder, and transitioning into the design authority & maintainer of the 'Collins'-class submarines. Hence, all profits made by the company to date have been sourced out of submarine related activities. The TLS Agreement renegotiation, coming seven years into its 25-year contract, is due to kick-in from 1 July 2010, just as the AWD program kicks-up with intensive set up costs and profit-reducing inventory building requirements. The interim future financial performance outlook for the company, is therefore, cloudy when compared to what has been delivered over the last five years (*see table page 18*).

GENESIS OF ASC: ASC Pty Ltd (formerly The Australian Submarine Corporation) was initially formed as a commercial consortium in the late-1980s with Australian and overseas owners, to progress construction of the Royal Australian Navy's six 'Collins'-class submarines. A decade later, when the construction program was beleaguered by delays and technical difficulties arguments, the Commonwealth of Australia (via the Minister for Finance) exercised 'step-in' provisions and assumed 100% ownership of the corporation.

This is the second principle to be kept in mind when reviewing the financial prospects of ASC – the other unique thing about the com-

pany is it's a single-customer business. Hence, it prospers on the basis of the 'customer' being willing to fund the business, more often than not in advance of required work being undertaken. [Financial records examined by ADBR indicate that as part of the restructuring of the company (as a GBE) in 2002/03 – and subsequent to the Commonwealth's assumption of full ownership – ASC was advanced a 'lazy' roughly \$100m in surplus cash.]

We say 'lazy', due to the fact that as the corporation and 'Collins'-class submarine program recovered from its construction difficulties to deliver all six boats, the large majority of these funds (given ASC does not maintain an overdraft) spent most of their time in interest bearing deposits or marketable securities. In fact, a substantive element of ASC's \$5.9m of operating profit after tax (OPAT) in 2002/04 (the first year after the restructuring), can be tracked back to interest income.

Upon signing up in October 2007 to an alliance-based target incentive agreement (ABTIA) to advance the AWD construction program, this pool of 'lazy' cash began to be drawn upon to fund two major investments: a new purpose-built site at the Australian Marine Complex (ASC-West) south of Fremantle – to support the six submarines (all based in the West); and the remediation of land, and construction (at its Osborne site in South Australia) of new buildings and related infrastructure (ie: to support project Sea 4000 complex module build, outsourced module assembly and subsequent AWD ship build, and latter combat systems integration).

As outlined in ASC's 2008/09 accounts, this investment – of roughly \$115.2m (contracted) over the last two years (with the balance of \$135m expended through operating leases) – has stripped from the company the large majority of the 'lazy' cash security that has for the past five financial years underpinned the Directors' approach to reconciling the 'liquidity risk' provision.

In its place, the company (through ASC AWD Shipbuilder Pty Ltd) was refinanced by a substantive advance (\$114.9m, spread across a range of international currencies) to commence working up to a formal start to AWD construction (just declared on 21 January), along with a further \$12m contribution from the Commonwealth for capital works. Interestingly, these funds – termed ‘Restricted Cash’ in the financial accounts – are required to be separately maintained (including interest earned) within a Commonwealth of Australia approved interest bearing account for the sole purpose of receiving and holding advance payments from the Commonwealth.

Further, the production facility brought into being via the special \$12m payment, comes with a ‘deferred purchase option’. That is, what is built with the funds is specifically intended to assist in successful construction of the three currently contracted AWDs. Once this is done, a subsidiary of ASC has an obligation to purchase the facility within three months of the completion of the last AWD, at an amount equal to the lesser of the written down value of the facility at an agreed depreciation rate, and the fair market value determined by a licensed valuer.

FORGIVING CUSTOMER NO MORE: Through to the end of the financial year under review, it also appeared the ASC had benefited from a forgiving owner and principal customer, despite faltering submarine repair and sustainment performance having never been delivered to the original master schedule. Irrespective of the internal crisis that had accumulated by May/June 2009, the Minister is stated in the company’s Annual Report to have not once resorted to providing written directions to the Board.

This apparently amicable arrangement all came to a halt in the run up to the close of 2008/09, when RAN capability commanders were rudely awakened to the reality that, due to mechanical problems and delays to the completion of several repair dockings, it was left virtually without any operational submarines. The response was quick. ASC’s energetic Managing Director, Greg Tunny, quickly left the firm after resigning following reported friction with DMO-CEO, Dr Stephen Gumley, over ASC operating efficiencies and the growth of ‘Collins’ submarine support costs of 14% since 2004/05, with no change in available sea days.

The ASC Board of Directors (whose average age at the time was 63), was next instructed to pull in its horns, and knuckle-down to addressing the findings of an external review (Stroud) commissioned by

Dr Gumley, which is understood to have concluded that due to alleged over-staffing, guaranteed overtime and poor work practices, ASC was running – in key areas – up to 30% less efficiently than international best practice.

The situation was perhaps best summed up by George Pappas’ Defence Budget Audit, which had the following to say – “There are substantial systemic issues across the support landscape for the ‘Collins’-class (including Defence, ASC and its suppliers), which are interacting to drive increased observed cost and low levels of availability. Frequent design modifications and upgrades (including significant legacy issues arising from the build phase), along with overlapping docking periods, drive higher demands on finite resources.”

In turn, Pappas observed, “this leads to further extension in docking periods and causes further instability in the master maintenance schedule (exacerbated by the lack of contingency built into the schedules to absorb emergent work). Schedule instability makes the planning of spares provisioning inaccurate, which further exacerbates productivity issues, extends repair turnaround times and increases docking periods. This cycle is further compounded when low submarine availability compromises training of seamen, which exacerbates crew shortages. These crew shortages can lead to submarines docking early, further disrupting the schedule.”

In response, ASC moved 26 June to excise a whole layer of executive management out of the business through jobs swaps with the AWD project, as well as a rolling program of redundancies that has so far cost the company \$5 million. Next came pressure from the Defence Materiel Organisation (DMO) for acting ASC MD & CEO, Graeme Bulmer, to progress further rolling improvements, followed by the above-mentioned move for a re-negotiation of the original ‘Collins’-class submarine TLS contract.

As Parliament Committees were meeting in Canberra in late-October 2009 to discuss Supplementary Budget Estimates (SBE) hearings, Bulmer announced that ASC was “on track” to meet the Government’s operational requirements for the submarine fleet following the shake-up commenced after Tunny’s departure. He said at the time, the company “has responded to the need to improve submarine availability, and reduce the cost of maintenance. We have made a number of substantial changes to the submarine business to improve the level of submarine availability, and reduce the cost of maintenance ... we are certainly doing everything possible within a resource-constrained environment to achieve this.”

ROAD BACK TO CANBERRA: ASC Goup – Nine Year Financials

Corporate Performance Measure	Financial Year 2000/01 (\$m)	Financial Year 2001/02 (\$m)	Financial Year 2002/03 (\$m)	Financial Year 2003/04 (\$m)	Financial Year 2004/05 (\$m)	Financial Year 2005/06 (\$m)	Financial Year 2006/07 (\$m)	Financial Year 2007/08 (\$m)	Financial Year 2008/09 (\$m)
Revenue from Rendering of Services	195.4	141.8	148.4	243.6	217.0	254.9	305.8	315.4	346.1
Financial Income	-	3.3	4.3	4.5	5.6	4.9	5.1	8.5	5.1
Other Revenues from Ordinary Activities	5.7	1.2	6.0	7.8	6.7	1.0	1.5	1.0	0.8
Total Revenue	201.1	146.3	158.7	255.9	229.3	260.9	312.4	324.9	352.0
Operating Profit before Tax	12.4	1.7	8.9	23.6	20.5	26.3	42.1	43.9	25.5
Operating Profit after Tax	7.1	0.1	5.9	16.1	16.1	18.5	29.6	29.7	18.4
Total Assets	206.7	196.7	236.7	243.5	283.9	245.9	276.6	308.2	446.4
Total Shareholder Equity	53.1	53.2	59.1	107.3	107.3	121.5	158.9	174.9	183.6
Total Fully-franked Dividend Declared	-	-	-	5.0	9.7	11.1	17.8	17.9	11.1
Return on Equity	13.4%	0.2%	10.0%	15.0%	15.0%	15.2%	18.6%	17.0%	10.0%

NO SUBMARINES AT SEA: At the time of the statement, apparently – of the six-boat ‘Collins’-class submarine fleet – two were in routine maintenance, and one was at ASC conducting an urgent defect repair. The remaining three were engaged in, or were awaiting, longer term docking cycles. The Navy was further said to have available only three crews for the six boats, whilst 119 trainees were awaiting to go to sea to achieve qualification.

Under heavy Opposition questioning at Defence SBE hearings, Defence Minister Faulkner conceded the operational status of the ‘Collins’-class submarine fleet as “far from ideal”. Dr Gumley similarly confirmed media reports that sustainment of the ‘Collins’ boats had been at the top of his projects of concern list for “probably the last three to six months.”

SBE Committee testimony revealed quite serious damage had been incurred to the Swiss-made ‘Hedemora’ diesel engines aboard HMAS ‘Collins’ shortly after it had completed a maintenance period, with an incorrectly executed bearing change at ASC fingered as the cause of a catastrophic engine failure, which occurred whilst the subject vessel was transiting the Great Australian Bight.

Officials described the ‘Hedemora’ diesels as having tracked ‘a complicated and difficult path’ since first being selected for the ‘Collins’ boats. The European manufacturer is understood to have closed its factory shortly after securing the Australian order, meaning that after assembly in Australia by the former ADI Limited, they needed to be stored for several years before being able to be integrated into the ‘Collins’ fleet.

The Chief of Navy, Vice Admiral Crane, went on to advise the Defence Foreign Affairs & Trade Legislation Committee that the same catastrophic failure experienced on the ‘Collins’ was not expected to occur on the other five boats in the production series. In light of an expensive costed study by ASC, the DMO’s Head, Maritime Systems Division, Rear Admiral Boyd Robinson, confirmed the RAN “had no plans to replace those engines ... because there was no evidence that that is even close to being required.”

Defence nevertheless went ahead to engage another diesel contractor to review ‘Hedemora’ engine experiences to date, and (along with ASC) prepare a report on required submarine propulsion repair options, which was to have been completed in December. Dr Gumley further confirmed the DMO had sufficient ‘routine maintenance’ money in its 4-year forward estimates to effect submarine repairs, but added, “we are not planning within our budgetary estimates to have the capital cost of replacing engines inside that period.”

Senator Faulkner advised the Committee he had recently directed the DMO to review all aspects of RAN submarine availability, with early changes involving increased DMO management oversight, and scheduling input on-site at ASC’s Osborne facility in Adelaide, along with improved logistic support to operational submarines and those that are in long-term maintenance. The Navy was also directed to place senior personnel in Adelaide to work with the DMO and ASC personnel.

Dr Gumley added, a further “commercial discussion is still

to be had” in regard to the application of penalties against ASC for defective work to date, noting “there are limited warranty provisions within the contract (which are) cost capped.” ASC self-insures against defective submarine work, with the 2008/09 annual report opening the year with a provision of \$8.9m, to which it drew down \$2.6m over the year.

Turning to the TLS Agreement re-negotiations, the DMO chief told the Committee, “over the last two or three years, the (cost-plus) contractual mechanism has not worked as well as it should have ... cost-plus contracts often drive the wrong behaviour.” So whilst the impact of all these changes is only now just hitting ASC’s 2009/10 accounts, the poor financial results for 2008/09 mark a clear watershed in the rosy financial performance recorded over the past five years, as well as future projections made of ASC’s likely future financial performance as the hype of the ASC sale program reached its peak in 2007/08.

PROFIT FALLS BY 32%: ASC’s 2008/09 Annual Report leads off with the declaration of a 32.8% fall in profit after tax over the previous year, with structural elements associated with the AWD build likely to push its fortunes further south over the next 12 months, due to start-up costs associated with the AWD and likely to affect both the 2009/10 and 2010/11 results. Instead of being able to pay an additional special dividend (*as boldly indicated on page 16 of the 2008/09 Directors’ report*), there are suggestions in some quarters that a harsh conclusion to the TLS Agreement re-negotiations this Easter, will set up the company for a loss in the next financial year, meaning it may well have to go back to the Minister for Finance to seek a capital injection in order to remain viable.

So what ended up being circulated to potential investors in a very colourful form (in terms of the presentation of ASC’s 2007/08 Annual Report) as the push for privatisation reached its peak – in light of the Rudd Government’s subsequent abandonment of the ASC sale process – has since been followed by an extremely late (ie: released just prior to Christmas) and bland 2008/09 mono/black type document, which has similarly been stripped of a large amount of information historically provided to readers in terms of providing needed transparency into the detailed operations of the company.

Accordingly, it’s easy to see why interests within the Government want external attention turned away from a focus on the abandoned trade sale, as the 2008/09 annual report delivers messages of falling

profit, dividend and return on equity outcomes – with potentially worse to come. Also stripped away is much of the hoopla stirred up through written statements by Directors the previous financial year, that the company, in effect, would have been fully privatised by now.

This privatisation quest, of course, came to a crashing end in parallel with accelerating falls in stock market values and onset of the global financial crisis. The downturn in economic fortunes led the Rudd Government to formally abandon the sale in February 2009, with Finance Minister Tanner – after having been told by leading privatisation contenders there



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deck. Small mast. Small – Medium length (generally 15 metres or less), Narrow Beam, Little or no superstructure) and Type 4 vessels (Motorised. Large (generally 20 meters or more in length), large beam).

In terms of supportability, each BCRV is required to be able to be maintained and supported at commercial facilities at various 'primary ports'. These are Adelaide, Albany, Brisbane, Broome,

Cairns, Dampier, Darwin, Eden, Fremantle, Geraldton, Gladstone, Gove, Hobart, Launceston, Mackay, Melbourne, Newcastle, Port Headland, Sydney, Thursday Island, Townsville, and Weipa. Secondary ports include Botany Bay, Bunbury, Burnie, Devonport, Esperance, Exmouth, Geelong, Henderson, Jervis Bay, Port Kembla, Port Lincoln, Portland, Warnambool, Western Port, Wollongong and Whyalla. **ADBR**

Cyber Security Centre – from page 12

Budget, and set to be fully operational by July.

CERT is to work in parallel with Defence's new CSOC to defend economic institutions, critical infrastructure, government agencies, businesses and home users from cyber threats. While more detailed plans for offensive cyber operations, to take an active role in influencing conflict outcomes, are highly classified, ironically no back up systems, or high level of redundancy has yet been built into the ADF's overall system-of-systems design.

Senator Faulkner told media that in 2009, the Department of Defence had investigated approximately 200 electronic security incidents on its own networks per month. Defence is said to have effectively responded to these activities, and no operations to date have been disrupted due to network invasion activities.

Offensive cyber warfare capabilities are already prevalent in most East Asian countries, with the finger regularly pointed at China as the source. Not wanting to directly confirm that Chinese activity was one of the principal drivers of the CSOC's establishment, Faulkner said, "it is true that the global community continues to experience an increase in cyber intrusions. We need to understand, that all systems that are connected to the internet are potential targets for hacking or cyber attack."

The Minister continued, "there has been speculation about nation states mounting cyber attacks, and there's also been specula-

tion about nation states mounting cyber attacks against Australian Government information networks. There is some evidence that electronic intrusion of Australian Government sites has been conducted from overseas, but I stress, the nature of the internet makes it difficult, perhaps impossible, to attribute those attacks to exact sources, and this comes back to again highlight the importance and significance of the establishment of this centre.

In moving to set up the CSOC, DSD has already transferred 51 of its staff into the Centre, with the number to grow to 130 over the next five years. At full strength it will comprise IT experts, engineers and analysts drawn from the Defence Intelligence Organisation, the Australian Defence Force, the Defence Science and Technology Organisation, representatives from the Attorney-General's Department, the Australian Security Intelligence Organisation and the Australian Federal Police.

Upon establishment of the CSOC, which has been armed with DSD's high-powered computing resources and advanced analytic techniques (for intrusion analysis, detection, threat assessment and incident response), the CSOC is ultimately expected to provide Defence with not only a comprehensive understanding of the cyber threat to government networks (as well as the private sector), but also a fully fledged cyber warfare capability. **ADBR**

ASC Stumbles – from page 20

was no longer any money left in their tin ... to relieve government of its awkward position where (in relation to naval warship construction, and in various guises), it remained owner, lead supplier and principal customer. Tanner's statement was short, citing "current uncertainty in global financial markets as presenting significant risks to a successful sale of the company."

Now on the verge of a decade-long AWD construction process that will similarly drive up costs across the enterprise and bleed off profits by way of a growing book of 'work in progress', the outlook for another stab at ASC privatisation is thus unlikely to improve until the next big shipbuilding contract comes around in 2015, with nomination of the prime contractor or alliance to build the 12 project Sea 1000 future submarines. Unfortunately for ASC, however, the Government has done little to underpin confidence that the company will walk straight into a contract on this project, with Ministerial comments on several occasions actually casting doubts on such a likelihood.

In a speech to the Sydney Institute on 4 November, Greg Combet noted project Sea 1000 would be "among the largest industrial projects ever contemplated in Australia ... (it is) perhaps at the margins of Australia's present scientific and cultural capacity. If managed properly, in addition to providing the Navy with 12 highly capable submarines, it will contribute to the modernisation of Australian manufacturing industry." Yet on the back of an estimated \$4 billion (of the initial \$5.1 billion project budget) spent in Australia, Combet noted, "we have found it difficult to maintain the industrial capacity built around this level of local content. Some of the ongoing maintenance problems of the 'Collins'-class are driven by this issue. Accordingly, we are giving serious thought to what industrial capabilities must be supported within country to sustain this project."

'COLLINS' LESSON LEARNED?: Turning to lessons learned from the 'Collins' project, Combet said, "project management performance during design and construction had been variable; the project management unit was split between Canberra and Adelaide; the location of the prime contractor in Adelaide led to poor communication and issues taking longer than they should to resolve; there was poor risk mitigation and inadequate contingency allocated; there was also insufficient recognition of the 'Parent Navy' challenge; and an underestimation of through life support costs. Moreover, the TLS contract was not in place early enough."

Moving forward, Minister Combet said the Government would need to consider for project Sea 1000 "a dedicated policy cell located in Canberra that could translate the strategic guidance into the actual detailed requirements of the future submarine. This would involve a deep understanding of the various trade-offs between desired capabilities and the impact on cost, schedule and risk. An appropriately resourced design and project management cell located in Adelaide, close to the builder, would also be needed. We have seen the benefits of this approach with the AWD project."

A study circulated at the close of 2009 by the Government-funded ASPI think tank, next went on to propose a series of models as to how the ASC could be restructured, in order to capture the company's submarine expertise for focusing on advancement of the new Sea 1000 program. It further noted, as have other studies, the remarkable quantum of investments made by various state governments (particularly South Australia & Western Australia) in common user facilities (CUFs), as part of a quest to invite new players into the market in order to drive down future platform construction and sustainment costs.

As this environment comes to pass, ASC's primacy – in terms of its incumbent status as Australia's principal submarine design agent & maintainer, as well as surface ship builder and maintainer – may end

up being severely undermined. Unencumbered by having to make substantive investments in facilities and infrastructure (as ASC just has in Osborne) to secure contracts, outsiders could package extremely competitive offers. In future, the WA AMC-CUF, the SA Techport CUF and potentially – Garden Island (Sydney), as Thales Australia's current lease comes to an end in 2013 – will all be owned and controlled by State Governments with full Commonwealth of Australia support.

On top of this, the ASPI report contained speculation as to the likely disposition of the ASC's submarine design and maintenance in terms of its provision of 'free' intellectual property, should the Government wish to be helped along the path of building a centre of excellence and expertise within the Department of Defence to help guide its deliberations on certain key thinking in relation to project Sea 4000.

In a sign of the times of where debate may go should ASC financial results remain depressed for an extended period of time subsequent to re-negotiation of the TLS agreement, ASPI toyed with the idea of the value of sustaining the ASC in its current structure (including all the GBE trappings), if it was considered the national interest would be better served by sucking such expertise out of the company and setting it up in a separate location. Presumably, the remnants of the extant ASC, along with its AWD consolidation contract could then be auctioned off, thus clearing the decks for reform of the acquisition/contracting model to be adopted for the future submarines.

NOT NEEDED NOW: The debate, and hence uncertainty created by such debate, could not come at a worse time for ASC AWD Shipbuilding Chief, John Gallagher, who – at his brand new AWD assembly site – is having to mould a workforce to make the best of an overseas platform whose build methodology was originally designed for a 200+ years old yard, whilst at the same time, never actually being sure where political interests in Canberra might wish to take his project (and the new shipbuilding facility), as the industrial development implications of the 2009 Defence White Paper's unprecedented emphasis on maritime warships and patrol vessels pans out.

Out of the frying pan (in terms of running the UK's nuclear submarine fleet) and into the fire (ie: the current debate over the most appropriate future for Australian naval shipbuilding) has just come former Rolls-Royce executive, Steve Ludlam, who spent his first day as MD on the ground at ASC on 18 January. Whilst there were sighs of relief at the confirmation of his appointment, that a six months recruitment drive had finally concluded, others were heard to observe that the battered (if not poisoned) chalice left behind in the last six months of turmoil would guarantee many long hours of ASC management burning the midnight oil before the new TLS agreement is properly concluded.

Interestingly, compared to previous years when Dr Gumley had regularly boasted his preparedness to pay a little more to secure good service from defence contractors, the mood within the DMO is now much bleaker. Like all who sail in the good ship 'Defence', a cash strapped Government which appears willing to stop at nothing – including purposeful manipulation of the Defence Capability Plan (*as established in analysis of ADBR's 'DCP at a Glance' spreadsheet*) – in its quest to restore the budget surplus, is looking to big savings from Defence – \$20 billion over the next ten years – and the impact of this will be felt from the highest levels of command through to the lowest – servicemen & women and defence-industry contractors alike.

NO ROOM LEFT FOR GOOD DEEDS: Perhaps the pity of the current story and situation with ASC, is that the former management led by now retired Chairman, John Prescott, appears to have believed they were truly running the enterprise in a manner that would be appreciated by the Government. As a GBE, successive annual reports through to 2007/08 claimed the company was being well run in delivering its services to Defence, albeit under GBE dictum, also being managed for profit and a regular dividend to government by way of

the Minister for Finance, concomitant with accumulating substantive retained earnings (now \$109.0m – or 60% of total equity of \$183.6m) to help fund further investments in future naval shipbuilding capacity, that would ultimately benefit the nation.

As it stands, this no longer appears to be the case. Profits generated by ASC and thenceforth returned to the Minister for Finance is in some way now viewed as not only over-charging the Navy for its task in sustaining the 'Collins'-class fleet, but also a direct extraction of wealth from the Defence portfolio (ie: into the Department of Finance's coffers), which must be stopped at all costs. The meat in the sandwich as a result of this change of heart is the ASC.

A view has thus been developed within the DMO that there is little utility for the nation as a whole in a situation where a 30c in dividend to the Department of Finance ends up costing the Defence Organisation, particularly the Royal Australian Navy, upwards of a dollar. The ascendancy of such thinking in dominating Defence's view of the ASC, in future, is likely to yield a much less profitable GBE, while its capacity to deliver incremental capacity to the RAN (as with ASC West), will be ultimately reduced.

In turn, those now likely to suffer a loss of utility from the above developments (ie: in future, they will have to fund their own infrastructure investments), are likely to start clamouring for ASC's disintegration, as each will see individual opportunity and gain from the demise of a company (in attracting work to themselves) given ASC's dominance of the market for so many years. That this may end up jeopardising the long-run success of the AWD build program (given ASC has never constructed a surface vessel before), may yet be considered acceptable given Government inclinations to open up the future submarine program to a larger number of players beyond ASC.

VULTURES GATHER FOR SEA 1000: True to character, those perceiving potential investment returns on sunk capital in naval shipbuilding facilities and related infrastructure might now change due to a pending further opening up of competition across the three prime contractor, shipbuilder and combat system integrator Tiers – with work being able to be undertaken at any one of the four state-subsidised CUF's – WA, SA, Victoria (potentially) and NSW (with the demise of Thales' tenure at Garden Island – are now advocating the industry should next be moulded into forms of systems specification monopoly at the highest tiers of integration.

A report by the DefenceSA Advisory Board (*see article page 7*) has kicked off this debate in the run up to Pacific 2010, and making a case for the creation of product and service monopolies through the interposing of an agent in the design process, who will be charged with dictating common specifications across all vessel designs, all in the good cause of achieving commonality of equipment and systems as part of a drive to reduce long-term RAN operating costs.

Rather than the undesirable monopolies of the private sector created by targeted Government business contract awards in the past, these good 'commonality-monopolies' are viewed as likely to cluster around state government-subsidised maritime precincts and common user facilities. The only problem is, if the Defence White Paper's quantum of new naval shipbuilding does not emerge as quickly as first anticipated (or contract awards are politically influenced to give 'a little bit to all' – as appeared to be the case with the initial decision to award module build work to NQEA), then states will end up being pressured to pour more money into such facilities, in order to increase their respective competitiveness in the quest to gain a greater quantum of work.

Such action risks a further duplication of assets already in place in other states (ie: how many 30,000t ship-lifts do we really need to build to maintain the LHDs), and hence, a free for all to secure the available work. Such a conundrum is now falling onto the plates of the two Defence Ministers – Faulkner and Combet. The turn of the decade into double digits – from 2009 to 2010 – will indeed be an interesting one.