29 October 2014

Defence White Paper 2015
Department of Defence
Canberra ACT 2610

Dear Sir/Madam

We write in response to the Defence Issues Paper released for public consultation.

Executive Summary

Over the past 25 years, South Australia has cemented itself as a leader in defence capability, particularly naval shipbuilding. Our defence industry has delivered the Collins class submarines and is in the process of delivering the $8 billion Air Warfare Destroyer project, both of which are being supported by the world class Techport Australia facility.

We preface our submission by acknowledging that a key consideration for the Federal Government in deciding where to build Australia’s next fleet of submarines is that it obtains value for taxpayer dollars while providing effective and affordable equipment for the Australian Defence Force. Business SA is a broad business membership organisation and we advocate for Government policy and programs which promote sustainable economic growth across industry sectors. We do not advocate for industry protection, but rather for governments to facilitate an environment where local businesses are able to be competitive against international companies.

In relation to the future submarine project tender process, our primary consideration is that South Australian based companies are given equal opportunity to at least compete against any other interstate or international option that the Federal Government may be considering.

Business SA has been actively participating in the Harper Review of competition policy on the basis that effective competition is in the best interests of local business, particularly small business. South Australian businesses increasingly need to compete in international markets, particularly considering the pending void left by the end of Australian auto-manufacturing. The Federal Government’s engagement of stakeholders during the Harper Review shows a genuine commitment to competition as a key plank of Australia’s future economy and any decision on the future submarine project should be aligned with the Government’s mantra of promoting competition.
Background

Business SA’s comments in relation to the Defence Issues Paper are largely centred on the tender process for the future submarine project. We also make general observations regarding the need for defence procurement to be appropriately structured to accommodate small business:

1. Business SA acknowledges comments made by the Australian Industry & Defence Network Inc that Australian SMEs are finding it much more difficult to be involved in ship building projects because more often than not, the Defence Department’s value for money (VFM) criteria only considers the short term acquisition costs which often drives procurement to an overseas supplier.¹

Considering that Australia’s defence industry is increasingly characterised by the presence of multi-national companies, often supported by SMEs, the Federal Government must have appropriate consideration for how it can help facilitate growth in those SMEs to enable them to be the next multi-national companies.

There are already small South Australian businesses successfully supplying into globally supply chains, a prime example being for the Joint Strike Fighter program, but Federal Government defence procurement policy needs to facilitate further growth of SMEs, particularly those which are export orientated.

Business SA was a driving force behind the South Australian Government establishing the Industry Participation Advocate (IPA). Although only formed in February 2013, the IPA has already had significant success with its ‘Meet the Buyer’ events, bringing hundreds of local businesses and government procurers together to discuss opportunities for Government tenders. Not only do these forums help smaller businesses better understand how to participate in the tender process, but they showcase local business capabilities and emerging technologies to inform Government procurers about innovative possibilities to address their purchasing and contracting needs.

The IPA has also been successful in achieving practical change to open up tender opportunities to small businesses by reducing red tape through:

- Setting limits of liability for low-risk contracts valued up to $1 million at 5 times contract value;

- Removing prequalification fees from 1 July 2014;

- Streamlining prequalification to ensure that a business who prequalifies for one agency is to be prequalified across other agencies in key categories of supply – to commence 1 July 2014; and

¹ Australian Industry and Defence Network Inc, Submission to 2014 Senate Inquiry into Naval Shipbuilding in Australia, P3
- In conjunction with Business SA, establishing a tender ready program to help small business access State Government contracts. As part of this program, Business SA has developed a tender ready handbook as a practical guide for small business.

2. We acknowledge comments made by Dr John White, a member of Defence SA’s Advisory Board, that through-life costs for submarines can be three to five times the initial cost of acquisition, taking into account mid-life updates. If Australia’s future submarines are built overseas, locking the navy into that overseas supply chain, any savings from the overseas build versus an Australian build may be quickly negated by higher through-life costs.2

We understand the Federal Government must consider all options in making a decision on where to acquire Australia’s next submarine fleet, but proper consideration needs to be made for whole of life costs, particularly if Australian industry will not be part of the building process. Furthermore, as highlighted by the Submarine Institute of Australia, if the submarines are assembled overseas, there is an increasing risk that certain technology that can only be installed during the assembly phase will not be made available.3

3. Dr White also pointed out that it is essential for such a long-term, high-value procurement, with so many overseas government, military and industry dependencies, that a prudent and comparative process be implemented to solicit and negotiate the best offers of support in all areas of overseas dependency in the future submarine project. Australia has experience in successful implementation of this approach, but it depends on competitive tension between at least two feasible sources.4

Business SA echoes Dr White’s concerns about the need for competition in the tender process, particularly as it relates to the Federal Government’s clear stance on strengthening Australia’s competition policy. In the Competition Policy Review Draft Report, the Expert Panel stated that previous competition reforms were “not an exercise in driving competition further into the Australian economy for its own sake, but for the longer-term benefits that would flow for Australian living standards.”5

It is important to note that Australian industry, including the workers that support it, have had to adapt to major economic structural adjustments over the past three decades on the basis of successive Governments’ drive to increase competitiveness. Business SA welcomes continued reform to increase Australia’s competitiveness, but business needs to be assured that the Federal Government is also subjecting its processes to competition to the same extent it expects the private sector to adapt to the realities of competition.

4. We refer to the Department of Finance’s submission to the Senate Inquiry into Naval Shipbuilding in Australia which states that “Paragraph 2.6 of the Commonwealth

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2 Dr John White, Submission to 2014 Senate Inquiry into Naval Shipbuilding in Australia, P3
3 Submarine Institute of Australia, Submission to 2014 Senate Inquiry into Naval Shipbuilding in Australia, P4
4 Dr John White, Submission to 2014 Senate Inquiry into Naval Shipbuilding in Australia, P2
Procurement Rules (CPRs) provides an overarching exemption removing the need to apply the CPRs where an Accountable Authority has determined it necessary for the maintenance or restoration of international peace, to protect human health or for the protection of essential security interests. In practice, this allows an entity to undertake an alternative form of procurement, such as a limited tender, should they choose, including for procurements above the relevant procurement thresholds."

According to the Defence Procurement Policy Manual, Defence Exempt Procurements are made on the basis that Paragraph 2.6 of the CPRs permits the Accountable Authority of an entity to determine that a measure is necessary for, among other things, the protection of ‘essential security’ interests. The Secretary and CEO of the Defence Material Organisation (DMO) have determined a measure for the procurement of submarines to be categorised as Defence Exempt Procurements.

Despite this caveat, Business SA cannot see why a limited tender for the future submarine project needs to necessarily exclude any bid centred on building in Australia on the basis that it is for the protection of ‘essential security interests’.

Accordingly, the tender process should be open to multiple bidders assuming other relevant ‘essential security’ criteria are met.

5. Business SA does not purport to be qualified to provide advice to the Federal Government on its geopolitical strategy. However, we do have a very clear understanding of how important our trade relationship is with both Japan and China. During the 2013/14 financial year alone, South Australian exports to China increased by 42%.

We are very cognisant of the significant growth in two way trade between China and New Zealand, most notably in dairy products, since the two countries signed a free trade agreement in 2008. Any potential future submarine purchase from any international country needs to be properly considered in terms of its impact on Australia’s present and future trade potential. We have already waited far too long for a free trade agreement with China, and with South Australia already facing a significant structural adjustment following the end of auto-manufacturing, we cannot afford further delays on measures which will greatly assist growth in export sectors where we have a comparative advantage, including agriculture and associated food and beverage manufacturing.

6. While we support a fully competitive tender process for each defence procurement project which may sometimes result in off-shore involvement, the Federal Government needs to provide more certainty to local industry in relation to its actual procurement requirements over the longer term. This is not to say that industry needs guarantees over where projects will be ultimately delivered, but the on and off commitments for the future submarine project have created a significant degree of uncertainty for local industry which is counterproductive to productivity.
Like any industry, businesses in the defence sector understand they need to remain competitive to stay in business. However, considering Australian industry is largely reliant on Federal Government projects, predictability of future defence requirements is a must if local businesses are to be able to position themselves to compete on price with international companies. Local businesses can only make future investments in staff, plant and equipment if they at least know what the actual demand from the Federal Government will be. Whether or not individual businesses win contracts is a business risk that any business faces and is factored into initial investment decisions.

Who we are

As South Australia’s peak Chamber of Commerce and Industry, Business SA is South Australia’s leading business membership organisation. We represent thousands of businesses through direct membership and affiliated industry associations. These businesses come from all industry sectors, ranging in size from micro-business to multi-national companies. Business SA advocates on behalf of business to propose legislative, regulatory and policy reforms and programs for sustainable economic growth in South Australia.

Should you require any further information or have any questions, please contact Rick Cairney, Director of Policy, Business SA on (08) 8300 0060 or rickc@business-sa.com.

Yours sincerely

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