



House of Commons
Defence Committee

**Defence Equipment
2009: Government
response to the
Committee's Third
Report of Session
2008–09**

First Special Report of Session 2008–09

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The Defence Committee

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The current staff of the Committee are Mike Hennessy (Clerk), Richard Ward (Second Clerk), Karen Jackson (Audit Adviser), Sara Turnbull (Inquiry Manager), Richard Dawson (Senior Committee Assistant), Christine McGrane (Committee Assistant) and Miguel Boo Fraga (Committee Support Assistant).

Contacts

All correspondence should be addressed to the Clerk of the Defence Committee, House of Commons, London SW1A 0AA. The telephone number for general enquiries is 020 7219 5745; the Committee's email address is defcom@parliament.uk. Media inquiries should be addressed to Alex Paterson on 020 7219 1589.

First Special Report

The Defence Committee published its Third Report of Session 2008–09 on *Defence Equipment 2009* on 26 February 2009, as House of Commons Paper HC 107. The Government's response to this Report was received on 27 April 2009. This is appended below.

Government response

Overview of DE&S progress

1. (Recommendation 1) DE&S was created on 1 April 2007 following the merger of the Defence Procurement Agency and Defence Logistics Organisation. Some 20 months after the merger, DE&S appears to have made good progress and is considered to be "heading in the right direction". The progress made has been achieved against a backdrop of supporting current operations in Afghanistan and Iraq. We commend the Chief of Defence Materiel and DE&S staff for their achievements to date. (Paragraph 10)

We are grateful for the Committee's recognition of the achievements of DE&S in its first year following the merger of the Defence Procurement Agency and the Defence Logistics Organisation. We also welcome the recognition for having achieved those successes in particularly challenging circumstances whilst supporting concurrent operations in Iraq and Afghanistan.

2. (Recommendation 2) While industry has generally welcomed the progress made to date by DE&S, it has also called for this progress to be accelerated and considers that the establishment of programme boards will be particularly beneficial. In its response to our Report, we expect the MoD to set out its plans for accelerating the progress achieved to date, the key changes it expects to see implemented in 2009, its plans relating to the establishment of programme boards, including the benefits expected from such boards. (Paragraph 11)

The move to a programme approach for managing the delivery of capability to the front line is the next step in embedding the MoD's Through Life Capability Management principles. The new programme arrangements are being implemented on a phased basis. The initial rollout was completed by the end of March 2009 with the formation of Programmes and Programme Boards to run them. The next phase of implementation covers the period up to March 2010 when the programme approach and underpinning ways of working will need to be sufficiently embedded across the MoD acquisition community. This is a major change to how MoD manages capability delivery and the implementation timescale represents a challenging target.

The next 12 months will see further development of how Programmes operate with the aim of achieving balance in the through life delivery of capability across projects and Defence Lines of Development by managing risk within programmes.

Performance in supporting current operations

3. (Recommendation 3) It is extremely serious that the A400M transport aircraft programme, which is to provide much needed new tactical and strategic airlift for our Armed Forces, is now running two years late and further delays cannot be ruled out. We expect the MoD to press the contractor for a new delivery schedule for the programme and examine closely the assumptions and estimates in the schedule to ensure they are robust. Once the new delivery schedule is confirmed, the MoD needs to

act swiftly to take the decisions which will prevent any capability gap emerging in the future relating to air transport. We expect the MoD, in its response to our Report, to provide us with an update on the forecast in-service date for the A400M programme and to update us on the action it is proposing to take once the new delivery schedule has been received from the contractor. (Paragraph 20)

We note the Committee's conclusions regarding delays to the A400M programme. Airbus Military has announced a series of delays in the development and production of the A400M programme, and has more recently indicated that first deliveries to customer nations will be three years after the achievement of first flight of the A400M prototype.

Airbus Military has indicated that first flight will occur no later than February 2010 and has also announced a slowdown in its production plans. Early A400M production aircraft will be delivered to some of our partner nations and therefore the first UK delivery would occur at least six months after Airbus delivers the first A400M. This suggests that initial UK deliveries could not start before 2013 and therefore the earliest in-service date of the A400M (defined as acceptance into service of the seventh UK aircraft) would be 2014.

When a new schedule is received from Airbus Military it will be evaluated by a joint Nations and OCCAR team and the information used to inform the way ahead for the programme.

4. (Recommendation 4) We consider that the Government has no choice but to consider the options referred to by the Chief of Defence Materiel. We call on the Government to set out its most up-to-date thinking on these options and to say whether it considers that there is a real risk that the entire A400M project might be so delayed that abandonment would be preferable. The costs and benefits attributable to any such decision should be clearly explained. (Paragraph 21)

The UK remains committed to A400M but not at any cost. We are currently considering all potential outcomes and are supporting actions within OCCAR and with Partner Nations that help inform our position.

We are considering a number of options as a contingency to mitigate any capability gap as a result of delays to or termination of the A400M programme. These include an extension to the life of the C-130K fleet and leasing or procuring additional C-17 and C-130J capacity.

The costs, benefits and timescales of each of the potential options form part of wider analysis work being undertaken to support decisions on the way forward. This work is ongoing and is being conducted with wide stakeholder involvement, including the C-17 and Hercules Integrated Project Teams and the military capability customer.

5. (Recommendation 5) The Minister for Defence Equipment and Support has assured us that all the A400M transport aircraft which will be deployed into theatre will be fitted with a full Defensive Aids Suite, a fuel inertion system and explosive suppressant foam. Given that risks to aircraft are not restricted to operational theatres, we consider it surprising that a decision has yet to be made on whether the A400M aircraft not earmarked to be used in operational theatres will be fitted with all three systems. The safeguarding of our Service personnel should be paramount and the equipment they

operate should have the maximum protection available. We note that the MoD considers that the risk of catastrophic fire on Chinook helicopters with pannier fuel tanks is low. We look to the MoD to ensure that its assessment about such risks is robust and is re-examined on a regular basis. (Paragraph 26)

Our intention is to fit the A400M fleet with a Portable Removable On-Board Inert Gas Generating System (PROBIGGS). The one exception is an early development aircraft, already under construction, that cannot be fitted with the necessary pipework. A retrofit to this aircraft in order to introduce PROBIGGS may be possible in due course, but if this is not possible, the aircraft would be used only in benign environments. The remaining 24 aircraft for the UK will all be equipped for FTI. The FTI system on A400M will use an on-board inert gas generation system; this is an alternative technical solution to explosion suppressant foam (ESF) which does not therefore need to be fitted to A400M.

The currently planned fitment of Defensive Aids Suites (DAS) for A400M covers a sub-set of the overall UK fleet but the numbers being procured are expected to be sufficient to cover the use of these aircraft in operational theatres. All of the UK fleet will be capable of being fitted with DAS equipment, ensuring operational flexibility and allowing optimal fleet management and asset utilisation.

The MoD's experts confirm that that the risk of catastrophic fire on Chinook helicopters with pannier fuel tanks remains As Low As Reasonably Practicable (ALARP) the remaining level of risk is Tolerable, and that appropriate mitigation action has been undertaken. As with all risks of this nature, they can rarely be removed entirely and we continue to explore mechanisms that might further improve the safety of operation of the aircraft.

Risks are considered in a detailed and methodical process as defined in the Chinook Safety and Environmental Management Plan which is fully compliant with existing Departmental guidance. The identification and assessment of all risks associated with the Chinook helicopter is conducted by subject matter experts (including industry) in conjunction with other key stakeholders including an external independent safety advisor. The assessments are carried out in accordance with guidance derived from the Health and Safety Executive's best practice principles.

An over-arching Airworthiness Review is conducted annually by the senior officer who has airworthiness responsibility for helicopters. This process was, and continues to be followed in the assessment of the risks associated with the use of the Chinook pannier fuel tanks.

6. (Recommendation 6) We note that the Urgent Operational Requirement process has continued to prove highly effective in enabling vital equipment to be provided in quick time to our Armed Forces in Afghanistan and Iraq. (Paragraph 29)

We are grateful for the Committee's recognition of our achievements in rapidly delivering battle winning equipment to troops on operations through the Urgent Operational Requirements (UOR) process.

7. (Recommendation 7) We welcome the announcement on 29 October 2008 that a substantial number of protected vehicles are to be procured as Urgent Operational Requirements. The protection of our Service Personnel against continuously evolving

threats must be the top priority. In its response to our Report, we expect the MoD to provide us with an update on its progress in acquiring these new vehicles and a breakdown of the procurement costs, including details of how much is to be funded from the MoD's budget. We also expect the MoD to provide us with details of which of the vehicles are expected to provide "longer-term benefit" beyond the current operations in Afghanistan and Iraq. (Paragraph 31)

We note the Committee's conclusion regarding the high priority of protecting service personnel on operations. The Secretary of State's announcement on 29 October 2008, which covered the procurement of a number of vehicles including a Protected Mobility package for Afghanistan, is evidence of our continued commitment in this area. The Protected Mobility package includes measures which will enable us to field Panther; upgrade Snatch; procure further Jackal vehicles; and deliver new well-protected logistics vehicles, to be called Tactical Support Vehicles (TSVs): Light (Coyote), Medium (Husky) and Heavy (Wolfhound). In the longer term, but as part of the same package, we are replacing the successful Viking vehicle with a better protected alternative (Warthog). Outside the package, but announced on the same day, is the procurement of Cougar training vehicles, and the development of a route proving and clearing capability known as Talisman. The latter capabilities are being fully funded from the Reserve as UORs. For the Protected Mobility package HM Treasury is providing £500M funding, with MoD contributing the remainder. The package was approved at £628M:

Costs of the package of Protected Mobility vehicles are:

Equipment	Original Estimate (Rounded)	Current Estimate (Rounded)
Additional Jackal	£75M	£75M
Warthog	£140M	£185M
Panther Theatre Entry Standard modifications	£20M	£20M
Snatch Vixen upgrade	£30M	£30M
Coyote	£65M	£65M
Husky	£170M	£180M
Wolfhound	£120M	£125M
TOTAL	£620M	£680M

Current estimated costs are based on signed contracts and current negotiations. Increases in estimated costs are principally due to changes in foreign exchange rates.

The MoD's financial contribution acknowledges the potential for long term benefit to defence of these vehicles beyond the immediate operation. Elements of the TSV fleet, for instance, are likely to offer a credible capability in a number of scenarios once operations in Afghanistan have ceased.

In terms of procurement progress, we are already on contract for Cougar Training Vehicles, Talisman, Jackal, Warthog, Coyote, Husky and the Panther modifications. Cougar is due to be fielded imminently, production of Jackal has started and the first tranche of Panther is currently in transit to Afghanistan. It is planned that Snatch Vixen and some of the TSVs will be delivered to training in Autumn 2009 with the majority of the TSVs to be delivered in time for the Spring 2010 deployment to take place.

8. (Recommendation 8) In November 2007 new arrangements for the funding of Urgent Operational Requirements (UORs) were announced. These new arrangements mean that, once the cost of UORs in a year have exceeded an agreed total with the Treasury, the MoD will have to contribute to half of the costs exceeding the agreed total and repay this two years later to the Treasury. In its response to our Report we expect the MoD to provide us with details of how the new arrangements have operated in practice, including its estimate of how much of the spend on UORs in 2008-09 will be funded from the MoD budget. We also expect the MoD to set out which of its programmes or activities will need to be re-prioritised in order to fund the cost of the UORs in 2008-09 which fall to the MoD's core budget. (Paragraph 36)

The arrangements outlined in the report reflect the agreement for Financial Year 2008/09. Expenditure in Financial Year 2008/09 has been contained within the estimate and therefore there is no excess to be repaid in 2009/10.

9. (Recommendation 9) While we are satisfied with UOR process, we remain concerned that the extent of UORs represents at least a partial failure by the MoD to equip adequately its forces for expeditionary operations which were anticipated by the Strategic Defence Review a decade ago. (Paragraph 37)

We do not accept that the level of investment in UORs represents a failure by the MoD to equip its forces for expeditionary operations. The Equipment Programme is designed to deliver long-term core capabilities that can be employed globally, to meet a range of potential future threats. MoD continues to invest heavily in equipment for expeditionary operations and significant quantities of new equipment will enter service in the next few years.

The UOR process, on the other hand, is designed to adapt and respond quickly to unforeseen requirements specific to particular operational environments and emerging threats, for example as a result of developing techniques, tactics and procedures of the enemy forces.

A requirement that aimed to equip our forces for generic expeditionary operations would not meet the UOR criteria and would not qualify for Reserve funding. Moreover, where UORs prove highly successful and have broader utility, the option exists for them to become part of the core equipment programme.

10. (Recommendation 10) We are concerned that the MoD appears to have made little progress with regard to its examination of the impact of current operations on equipment. While the MoD appears to have robust data on the cost of equipment procured through the Urgent Operational Requirement process, it does not have information on the cost of recuperating equipment returning from current operations nor on the impact of those costs on other areas of its budget. Such costs must be

substantial given the length of time that UK Armed Forces have been involved in current operations in Afghanistan and Iraq. The MoD must identify accurately the costs to date of recuperating equipment and the likely future costs of recuperation. Without such information, there is a real risk that these costs will fall on the Defence Budget, which is already under pressure, rather than on the Reserve as they rightly should be. (Paragraph 44)

We do not accept this conclusion. The MoD is aware of a variety of costs of recuperation where rolling recuperation has taken place (such as re-provision of munitions) or where equipment has returned from operations for recovery to stock or training use. For equipment not yet recovered, full costs can only be truly known once the equipment has been properly assessed. Since the Committee received evidence, MoD has now submitted a full assessment of recovery from Op TELIC to HM Treasury and the Committee has been briefed on the key findings of this work.

Equipment procurement performance

11. (Recommendation 11) We are concerned to learn that, once again, the Nimrod MRA4 programme has experienced further cost growth and in-service date slippage. In its response to our Report, we expect the MoD to set out the findings from its examination of the extent of further cost increases, to provide us with the latest position on the current forecast in-service date, and to outline the "mitigation measures" it has identified and what it expects these to deliver. We have not been satisfied by the explanations for these delays given by the MoD to date, nor by the Department's assurances as to how performance would be improved. We will return to this matter in the future. (Paragraph 48)

We understand the Committee's concern that the Nimrod MRA4 project has experienced further cost growth and delay to the forecast in service date, although it is worthy of note that the current In Service Date of late 2010 has remained largely unchanged since May 2006. Nimrod MRA4 is a complex and demanding project, where additional slippage and cost growth has principally been due to technical factors. Time and cost variations from the original project approval were largely caused by resourcing and technical problems at BAE SYSTEMS associated with the original fixed price contract that was let in 1996; these problems were exacerbated by the design and development, and production programmes being conducted concurrently. The agreement reached with BAE SYSTEMS in February 2003 placed a stop on MRA4 series production work until the design had reached adequate maturity and acceptable production costs were forecast. These criteria had been met when the contract for full production was placed in July 2006.

The cost increase of £102M and a slip to the in service date of 3 months reported in Major Projects Report 2008 largely result from a further extension to the flight trials programme, the effect of corrosion on the donor components from the Nimrod MR2 and a re-evaluation of the required financial risk provision. Means of mitigating these cost increases are being developed with BAE SYSTEMS based on a thorough re-examination of the content of the flight trials programme and remaining programme risk. A revised and robust flight trials programme has been produced and progress will be closely monitored until its planned completion towards the end of 2009. Despite these additional cost pressures for the extended flight trials programme, aircraft production at the Woodford

plant is progressing ahead of schedule with the first production standard aircraft expected in October 2009 and the in service date remains unchanged at December 2010.

12. (Recommendation 12) In its first year of operation, DE&S failed to meet its Public Service Agreement target to "Deliver the equipment programme to cost and time". We note that the National Audit Office examined the procurement performance relating to the 20 largest projects and found that the aggregate forecast cost for these projects increased by £205 million and the aggregate in-service date slippage increased by eight years in 2007-08. We are concerned that DE&S has failed to control delays on equipment projects with almost half of the 20 largest projects experiencing in-service date slippage in 2007-08. We have not been satisfied with the explanations given by the MoD as to what it intends to do to rectify this decline in performance, and we will be returning to this matter in the near future. (Paragraph 50)

The MoD notes the Committee's concerns about the cost growth and slippage reported in Major Projects Report 2008. The cost growth was confined to two projects, NIMROD MRA4 and the BEYOND VISUAL RANGE AIR TO AIR MISSILE, both of which were initiated (passed Initial Gate) before reforms to acquisition were introduced. Similarly around two thirds of the slippage reported was focused on three projects, TERRIER (27 months), NEST (19 months) and SOOTHSAYER (16 months). Of the projects reporting slippage only one (NEST) was initiated after the introduction of reforms to acquisition.

13. (Recommendation 13) Financial Year 2008-09 saw the introduction of new Departmental Strategic Objectives (DSOs) which include a Performance Indicator under DSO 3 covering "Procuring and Supporting military equipment capability through life". The MoD's performance, six months into 2008-09, has been disappointing with average in-year forecast in-service date slippage and average in-year forecast cost increases both exceeding the targets set. The MoD considers that exchange rate changes account for most of the forecast cost increases reported in 2008-09. In its response to our Report, we expect the MoD to set out its estimate of how much it anticipates exchange rate changes will add to the cost of equipment programmes in 2008-09 and what action it is taking to minimise the risk of such cost increases. (Paragraph 55)

Based on most recent forecasts of exchange rates over coming years, the MoD anticipates some £234M of additional future cost for the Departmental Strategic Objectives projects. While specific projects have recorded cost growth because of the exchange rate variance the overall impact on the Department, including during the course of 2008/09, has been mitigated by our forward purchase programme for euros and US dollars. Where the future impact is not fully mitigated, the pressures will be addressed as part of the annual planning cycle.

14. (Recommendation 14) In its response to our Report, we expect the MoD to set out what specific action it is taking to reduce the Demonstration and Manufacture timescales of equipment projects by 50% from 2009 onwards, a target set out in the DE&S Business Strategy 2008-12 and how such reductions will be measured and reported. (Paragraph 56)

A number of factors influence the time taken for Demonstration and Manufacture; these include industrial capacity, the level of available funding and the risk remaining at the Main Gate decision point.

The time taken for the Demonstration and Manufacture Phase has traditionally been measured from the Main Gate decision to the declaration of the In Service Date; often associated with initial deliveries.

The changes introduced as part of the reforms to Defence Acquisition were aimed, inter-alia, at providing greater certainty to Demonstration and Manufacture timescales. A key component is ensuring that adequate time and investment is made during the Assessment Phase to ensure delivery of the Demonstration & Manufacture phase following Main Gate to plan. Results from projects initiated since the introduction of acquisition reforms suggest improvement. There are, however, other factors that influence acquisition cycle times; the profile of available defence funds, the relative priorities that must be applied to these to deliver all defence outputs and the capacity available within industry; which can be subject to broader industry investment decisions.

When committing to a Demonstration and Manufacture phase of a project the MoD does so on the basis of best value for money and what can be afforded in the context of the delivery of overall defence capability. Such decisions will also take account of industrial capability and capacity as well as the wider defence industrial strategy for example is it reasonable for industry to invest in additional capacity for a short term faster production run and for MoD to pay for this if there is limited utility in the future.

15. (Recommendation 15) The MoD does not consider it possible to assess how, if at all, support to current operations has impacted on performance against its procurement targets. We consider that, while it would appear that only a small proportion of DE&S staff have been involved on Urgent Operational Requirement projects, support to current operations has had an adverse impact on its procurement performance, although we doubt that this factor alone is responsible for the state of parts of the equipment programme. DE&S staff involved in UOR projects have had to be transferred from longer-term equipment projects and, given the importance of UOR projects, more experienced project staff are likely to have been transferred. We would hope that as work supporting current operations begins to reduce, and staff are transferred back to the longer-term projects, that this will have a positive impact on procurement performance. (Paragraph 58)

The MoD notes the Committee's conclusion. We currently have some 750 personnel re-deployed to deliver Urgent Operational Requirements and continue to monitor numbers to protect delivery of Urgent Operational Requirements. This has caused significant pressures in some core project teams. The introduction of Flexible Resourcing, which is a key enabler of the PACE (Performance, Agility, Confidence and Efficiency) Programme, will provide DE&S with a system to manage the deployment of staff more effectively according to the highest priority and their skills. This should help us track more clearly the impact that moving resources to higher priority tasks has on the delivery of others.

16. (Recommendation 16) We note that the MoD considers that a key contributor to cost increases or delays on equipment projects is "the realisation of unplanned or low

level / high impact risk". The MoD states that it was placing greater emphasis on investment prior to Main Gate to address this risk. In its response to our Report, we expect the MoD to set out, for the current projects which have passed Main Gate, the proportion of such projects where 10-15 per cent or more of the forecast project budget was spent in the Assessment Phase. (Paragraph 61)

Of the 41 Category A-C projects that had passed Main Gate and had not declared an In Service Date at 1 April 2008; four are classified as Off the Shelf purchases and had no formal Assessment Phase (155mm Ballistic sensor Fuzed Munition, Non Signature Rotary Wing for Helicopters and two C17s). Of the remaining projects, nine (22%) have spent more than 10% of the total estimated project cost during the Assessment Phase. These are:

PROJECT	COST OF ASSESSMENT PHASE AS % OF FORECAST PROJECT BUDGET
Land Environment Air Picture Provision (LEAPP)	43%
Anti-Structures Munition	36%
Artillery Fuzing System (AFS)	30%
Chinook Mk.3 Reversion Programme	23%
HILDING	20%
Advanced Jet Trainer	14%
Seawolf MLU	12%
SOOTHSAYER	11%
FALCON	10%

17. (Recommendation 17) We note that DE&S has made good progress in improving the skills of its staff across a range of key acquisition disciplines. We note also that the Defence Commercial Director has recently been announced as the new Comptroller and Auditor General, but we consider it essential that the MoD build upon the progress he and the Chief of Defence Materiel have achieved to date. (Paragraph 66)

We welcome the Committee's acknowledgement regarding the good progress being made in improving the skills of those involved in acquisition and can confirm that the MoD remains committed to continuing to build on the achievements to date.

The funded DE&S Upskilling programme is being taken forward into Financial Year 2009/10 to continue the development and acquisition of required future skills. The Skills Directors have produced their skills plans which have translated into 71 separate skills interventions across the Commercial, Finance, Logistics, Engineering, Programme and Project Management, Information, Corporate Support and HR job families.

18. (Recommendation 18) Equipment programmes have often experienced delays at various points in their life cycle. We note that the MoD is looking at training programmes which focus on the "value of time". In its response to our Report, we

expect the MoD to set out what consideration it has given to such programmes and its future plans in this area. (Paragraph 68)

Within MoD, the Commercial Function is currently benchmarking the competences and skills of its commercial staff, taking fully into account the likely skills needs of the future. Based on the outcome of this exercise, a People and Workforce Plan will be developed, including the resulting training needs analysis which will enable the design of a comprehensive training programme aimed at closing identified skills gaps. It is anticipated that the training to be delivered by this plan will address time/value issues.

19. (Recommendation 19) By 2012, DE&S plans to have reduced its staff by 25% compared to the number in post at the start of April 2007. At the end of September 2008 the number of staff had been reduced by some 15%. Given that procurement performance declined in 2007-08 and that DE&S is supporting two operations, we find it surprising that DE&S is pushing ahead with its streamlining programme. DE&S must monitor closely the morale of its staff and recognise the uncertainty that such programmes create. In its response to our Report, we expect the MoD to provide us with its rationale for reducing staff at a time when procurement performance has declined and when DE&S remains busy supporting two overseas operations. We also expect the MoD to provide us with details of the costs incurred to date, including redundancy and early retirement costs, as a result of the streamlining programme. The response should also set out how many consultants have been employed to undertake work previously undertaken by DE&S staff who have left under the streamlining programme, and the costs of these consultants. (Paragraph 71)

We note the Committee's comments regarding the need to monitor the impact on staff morale of the restructuring programme. Changes within DE&S are being taken forward within a single framework; the Performance, Agility Confidence and Efficiency (PACE) Change Programme. We launched this programme not least to enable staff to understand our overall plans and the timescales for their implementation. In January 2008 we set out these plans in a "blueprint" for the future of DE&S and have since been undertaking a sustained communications campaign, including web-based and published material as well as face-face briefings for staff. Managing the necessary changes as a coherent programme enables us to explain how individual changes within the programme link together to deliver the single aim of PACE: the improved effectiveness of DE&S.

PACE includes specific efforts to improve leadership and skills across the organisation, to improve our ability to deploy the right staff to priority activities and to improve the means by which the MoD delivers capability to the Front Line, through-life. Each of these elements has been collectively and individually explained to staff, not least with the intent to reduce uncertainty to the maximum extent possible, though we accept that in any change activity of this nature, some uncertainty amongst staff is inevitable.

With the implementation of these changes, and taking into account the staffing implications of a number of planned individual future projects, our assessment of the number of staff needed in DE&S by 2012 is 20,000. With the necessary internal rebalancing to take into account, for example, the level of Urgent Operational Requirement activity being undertaken in some areas within DE&S, we expect this to be sufficient to meet the highest priority tasks, though this will be kept under close review. We need, for example, to

