House of Commons
Public Accounts Committee


Twentieth Report of Session 2008–09

Report, together with formal minutes, oral and written evidence

Ordered by the House of Commons
to be printed 30 March 2009
The Public Accounts Committee

The Committee of Public Accounts is appointed by the House of Commons to examine “the accounts showing the appropriation of the sums granted by Parliament to meet the public expenditure, and of such other accounts laid before Parliament as the committee may think fit” (Standing Order No 148).

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The following member was also a member of the committee during the inquiry.
Mr Philip Dunne MP (Conservative, Ludlow)

Powers

Powers of the Committee of Public Accounts are set out in House of Commons Standing Orders, principally in SO No 148. These are available on the Internet via www.parliament.uk.

Publication

The Reports and evidence of the Committee are published by The Stationery Office by Order of the House. All publications of the Committee (including press notices) are on the Internet at http://www.parliament.uk/pac. A list of Reports of the Committee in the present Session is at the back of this volume.

Committee staff

The current staff of the Committee is Mark Etherton (Clerk), Lorna Horton (Senior Committee Assistant), Pam Morris (Committee Assistant), Jane Lauder (Committee Assistant) and Alex Paterson (Media Officer).

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Summary

The Major Projects Report 2008 provides information on the time, cost and performance of 20 of the largest military equipment projects being undertaken by the Ministry of Defence (the Department), where the main investment decision has been taken, as well as the top 10 projects in the earlier Assessment Phase.

In the last year, the 20 biggest projects suffered a further £205 million of cost increases, and 96 months additional slippage. This is the worst in-year slippage since 2003. The total forecast costs for these projects have now risen to nearly £28 billion, some 12% over budget. Total slippage stands at over 40 years, a 36% increase on approved timescales. The number of Key User Requirements reported as being “at risk” of not being met has also increased from 12 to 16 in the last year.

This is a disappointing set of results, particularly because the problems are being caused by previously identified failures such as poor project management, a lack of realism, not identifying key dependencies and underestimating of costs and timescales. The reoccurrence of these problems suggests that the Department’s latest acquisition reforms, introduced in 2001, are not yet resulting in the Department making better investment decisions or improving the execution of its defence projects. In particular, the main investment decisions for Terrier, Soothsayer and the Naval Extremely High Frequency/Super High Frequency Satellite Communications Terminals were made after 2001, yet these were the projects which suffered the largest slippages in 2007–08.

Project delays also have a detrimental impact on operational capability and costs. The Terrier and Soothsayer In-Service Dates have already been missed, forcing the Department to buy interim vehicles and continue using equipment suffering from obsolescence in Afghanistan. An additional 3–4 year delay to the A400M aircraft means that either older Hercules aircraft will have to serve beyond their planned Out of Service Date, or other transport aircraft will have to be bought or leased to address a growing gap in capability.

On the basis of the annual Report from the Comptroller and Auditor General,¹ we took evidence from the Department on the impact of time slippage and cost increases, on managing projects more effectively at the early stages, and on delivering projects successfully throughout their life.

Conclusions and recommendations

1. **Nine projects have been further delayed in 2007–08.** Delays to projects have caused gaps in front-line capability, or increased the risk that gaps may arise in future. In the case of the Terrier armoured engineering vehicle, these gaps have been filled by the purchase of interim equipment but in others, such as the Nimrod MRA 4 aircraft, existing equipment has been kept in service longer than originally intended. In order to better understand and adjust for the impact of delays, the Department needs to measure the full costs of delays to projects, including the costs of maintaining existing equipment in service for longer.

2. **The Department has recently announced delays to projects which have not yet reached their main investment decision point.** These projects include elements of both the Future Rapid Effect System and the Military Afloat Reach and Sustainability fleet auxiliary programme. Delaying projects to generate short-term savings can create future capability gaps and raise overall project costs. The Department should identify the financial and capability impacts of slipping projects, even if they have yet to pass their main investment decision point.

3. **On far too many projects the Department is over-optimistic and sets unachievable cost, time and performance objectives.** In future, when making the main investment decision on projects, the Department should develop quantified measures against which to assess how well it has:
   - understood the capability required and avoided over-specification;
   - assessed whether the technology can be delivered by industry within the agreed cost and time envelopes;
   - worked with industry to determine whether they have the right technical and project management skills to deliver the requirement;
   - identified any key interdependencies with other equipments and developed a strategy in case these impact on the project, and
   - assessed whether there is sufficient funding available to deliver the project.

4. **Recent fixed-priced contracts with industry, for example, on the Terrier and Soothsayer projects, have ensured cost overruns are borne by industry, yet the Department’s influence over these projects has correspondingly been reduced, eroding its ability to tackle project delays.** The Department should assess whether the risks to delivery inherent in the type of commercial arrangements it agrees with industry at the start of projects are appropriate. Further, before contracts are placed, it should routinely develop a joint strategy with industry for addressing these risks if they materialise, including, for example, if a gap in capability is created if the project is delayed.
5. Although recent progress has been made in licensing project managers, the Department admits that it needs to achieve more consistent skill levels across its procurement staff. The Department should introduce a more consistent approach across its own project management discipline, including further development of staff skills and the use of standardised project management systems.

6. Because many defence projects are very complicated and involve ‘cutting-edge’ technologies and complex commercial arrangements, the Department and industry must work together to solve problems that are likely to occur. Specific actions to encourage both parties to develop a common understanding of the challenges include sharing joint risk analyses and developing more common project and technical management training.

7. The Department is moving towards more incremental procurement strategies on some projects, with work broken into ‘bite-sized chunks’. If well applied in appropriate circumstances, this approach is sensible, but the existing two-stage approval process does not fit well with incremental projects or provide a sound basis for accountability to Parliament. The Department should:

- review whether the two-stage approach introduced under Smart Acquisition remains the most appropriate mechanism for delivering all defence projects, and

- ensure that publicly reported performance, measured from the decision points for each increment, meet the same rigorous accountability criteria as required for the current key decision point at Main Gate.

8. The Department is faced with some risks such as fluctuating exchange rates, which are hard to manage. The Department should take a portfolio view across its projects to make sure it is not committing to too many where it faces risks of similar magnitude, and where it has only limited ability to influence successful delivery.
1 The impact of delays and cost increases on projects

1. The Major Projects Report 2008 provides analysis on the cost, time and performance of the 20 largest defence projects undertaken by the Ministry of Defence (the Department), where the main investment decision to proceed with development has been taken, as well as information on the top 10 projects in the earlier Assessment Phase.

2. For the year ending 31 March 2008, total forecast costs for completing the 19 largest projects rose by £205 million to £27.6 billion. This represents a 12% (£3 billion) increase over the ‘most likely’ forecast costs when the main investment decision was taken. Projects were delayed by a further 96 months in-year, giving a total slippage of 483 months, representing a 36% slippage compared to forecasts made when the main investment decision was taken. This is the worst slippage reported by the Department on its Major Projects since 2003. Of the 20 projects, 15 are currently expecting to meet all their Key User Requirements, a worsening of the position that existed in 2007, when 17 projects were expecting to meet all of their Key User Requirements. In addition, 16 Key User Requirements on six projects are assessed ‘at risk’ of not being met, compared with 12 Key User Requirements ‘at risk’ on seven projects in 2007.

3. The Department has been unable to state what specific defence activity will be reduced to allow it to address the £205 million overrun in costs, but the Department is having to trade some capabilities to live within its budget. For example, it has trimmed the number of Future Lynx helicopters being bought from 70 to 62, and delayed a number of projects, such as Future Aircraft Carrier, Future Rapid Effect System and elements of the Military Afloat Reach and Sustainability fleet auxiliary programme. We remain deeply concerned that further cost overruns in projects will result in additional reductions in current defence capability and added delays to projects which have yet to pass their main investment decision. In particular, we are unconvinced by the argument that the Department has sought ‘coherence’ between the Future Aircraft Carrier and the delivery of the Joint Strike Fighter aircraft, as this has resulted in a delay to the carriers of up to two years only months after taking the main investment decision.

4. Cost overruns, slippage and reductions in performance can have a direct impact on current operations. For example, the Terrier mobile armoured engineering vehicle slipped by a further 27 months in-year and missed its In-Service Date of December 2008. The Department stated that had the Terrier been available it would have been deployed on current operations, as its predecessor vehicle had been taken out of service in March 2008. Although the fixed-priced contract on the Terrier project means that the direct costs of delays are borne by the contractor, the Department has had to address the resulting capability gap. Consequently, the Department has purchased a number of engineering

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2 Analysis of the costs of the Typhoon aircraft are currently excluded on commercial grounds
3 Qq 51–52
4 C&AG’s Report, paras 1.15, 2.17
vehicles for operations to cover the gap in capability, including 13 JCB excavators at a cost of £6.2 million.\(^5\)

5. Delays to projects are also creating looming gaps in capability which could impact on future operations. The In-Service Date for the A400M transport aircraft has already slipped from December 2009 to December 2011, and recent announcements suggest a further delay of three years. This will create an air transport capability gap as the existing Hercules C130K transport aircraft were expected to leave service by 2012. The Department has stated that it is considering a number of measures to close the gap, such as extending the life of the Hercules, buying more C17 aircraft or new Hercules, or bringing forward elements of the Future Strategic Tanker Aircraft.\(^6\)

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\(^5\) Qq 18, 21–22; C&AG’s Report, para 1.15

\(^6\) Q 11
2 Managing projects at the early stages

6. Many of the cost increases and time delays reported this year stem from the Department’s failure to start its projects properly. The Department has made unrealistic assessments of how much things will cost and how long they will take to deliver, taking decisions on the basis of what it would like projects to cost rather than what they should cost in reality. The Department agreed that it needs to inject greater realism into its procurement process. As evidence that it does take these issues seriously, it pointed to recent attempts to improve scrutiny of contracts, and work to estimate costs and timescales realistically. It believes, however, that it will take time for these efforts to be reflected in the Major Projects Report, as the failings described above will still be seen on its older projects.7

7. The Department has made unrealistic assessments of the risks involved with delivering technically complex projects. At the time the decision was made to take up a competitive bid from industry on Terrier, the Department accepted that the use of just one prototype vehicle was a reasonable level of risk, despite the important role the prototype plays in proving the reliability of a piece of equipment.8 Problems with this prototype vehicle have had a number of consequences, and contributed to the 27 month in-year delay to the project, although the Department believes that problems that the contractor, BAE Systems, has encountered with its supply chain have had a greater impact. The Department accepts it should have adopted a different approach and in future would consider reliance on one prototype vehicle to be an unacceptable risk. Despite the delays, the Department considers that Terrier will still deliver value for money as under the contractual arrangements BAE Systems will bear the costs of rectifying the problems.

8. The fact that technical risk was underestimated at the start of the Soothsayer project has been a major contributory factor to the 16 month delay reported this year. Components from the contractor’s supply chain proved not to be as technically mature as the Department and the contractor believed, and were delivered late.9 Soothsayer is a technically complex project, and the Department placed very demanding requirements on the contractor, which it believes contributed to the company producing schedule and technical risk assessments which were over-optimistic. The project team was based in the United States, but the Ministry of Defence team was in the United Kingdom, which made it more difficult for the Department to resolve these problems once they arose. Although the Department was aware of the potential issues associated with the location of the project managers, it did not consider this to be one of the key risks at the time the main investment decision was taken. The Department accepts that it underestimated both the technical risks, and the risks associated with the location of key staff overseas when the main investment decision was taken. The fixed price contract it agreed means that industry is now paying to rectify the problems.10

7 Qq 27–28, 63–64
8 Qq 21–22, 81–83; C&AG’s Report, para 2.11
9 C&AG’s Report, paras 2.21–2.23
10 Qq 23–24
9. The risks associated with procuring equipment from overseas are well known to the Department and yet the fact that the Naval Extremely High Frequency/Super High Frequency Satellite Communications Terminals project was so heavily dependent on the United States’ programme was not amongst the top twelve risks identified when the business case was approved. The Department was conscious of the high dependency on the United States, but considered that it was not realistic or affordable to develop a United Kingdom solution for this particular capability. As a result, it saw the risk of any delays to the United States programme as one it would have to live with. The project team judged that the fact that the Americans wanted the project delivered meant that the dependency was not a key risk in this case. The Department has successfully worked with the United States to bring in an interim solution to cover the delays to the Naval Extremely High Frequency/Super High Frequency Satellite Communications Terminals programme.

10. This Committee and its predecessors have reported year on year on the Department’s failings on delivering major equipment projects to time and cost. The Department repeatedly tells us that many of the projects suffering delays and cost increases pre-date the Smart Acquisition reforms it introduced in 2001, and so do not provide a fair reflection of progress it has made. We were, therefore, particularly unimpressed to note that the three projects reporting the biggest in-year delays (Terrier—27 months, the Naval Extremely High Frequency/Super High Frequency Satellite Communications Terminals project—19 months and Soothsayer—16 months) were all approved after that date. This suggests that these reforms have been ineffective. The Department’s argument that these are not truly Smart projects, as they were initiated (Initial Gate) before the reforms were introduced, is a weak one. The main investment decision (Main Gate) is the key decision point, as this is when the Department considers a project is sufficiently well understood such that defined time, cost and performance parameters can be set. The Department has been attempting to improve its processes for nearly 10 years and, even on long-running defence projects, we would expect to see signs of progress by now.

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11 Qq 107, 111
12 Qq 86, 109, 110–112
13 Qq 113–116
14 C&AG’s Report, para 1.20
15 Qq 114–116
3 Delivering successful projects

11. The Department needs to improve its record in the delivery of projects once they are under way. We were particularly concerned to hear that the Department was still failing on project management, with “Industry Project Management shortcomings and the Department failing to act as an intelligent customer” identified as a factor behind all four of the projects that have suffered significant delays and cost increases this year.\(^\text{16}\) In two instances, the Department has also failed to estimate costs and timescales to resolve emerging problems. For example, the heavily delayed Nimrod MRA 4 aircraft has seen a further increase of £102 million this year, largely because the Department’s initial estimates of the option to convert the development aircraft to production models, and the cost of resolving technical problems arising in flight testing, have proved to be inadequate.\(^\text{17}\)

12. Major Defence projects are by their nature technically and commercially complex, and it is likely that unforeseen problems will occur. The Department needs to improve its record on tackling such problems, and to work more closely together with industry. The Department should not wait until a project has gone badly wrong before carrying out a joint risk analysis with industry, as was the case on Soothsayer. Rather, this should be carried out as standard at the start of projects. The location of project managers in the United States hampered the delivery of Soothsayer, and affected the relationship with the contractor, but the Department has learnt the lesson from this, and the project manager is now based in the United Kingdom.\(^\text{18}\)

13. The Department only acted on the problems on the Terrier project in September 2007, when BAE Systems declared they were in default of the contract. We consider this shows a lack of grip on the Department’s part. The Department told us it was aware of the problems in April 2007, but the nature of the contractual arrangements meant it had to wait for BAE Systems to declare it was unable to meet a key milestone and therefore in default of the contract, before it could require them to come up with a rectification plan.\(^\text{19}\)

14. In response to our previous recommendations, the Department is concentrating its efforts on improving the skills of its staff in five key areas, including commercial and financial skills. The Department has now trained and licensed 500 project managers within its Defence and Equipment and Support organisation in an effort to raise skill levels across the project management discipline to the standards already achieved by the very best defence acquisition staff. The commercial area still needs to raise its skill levels, and the Department is prepared to bring in trained individuals from outside while it develops the skills and expertise it needs internally.\(^\text{20}\) The Department’s progress on improving the skills of its staff involved in project management is encouraging, but it also needs to make sure staff are equipped with the right tools to help them deliver projects to time and budget,
such as standardised systems for project management, and systems which are based on the right programmes and software.\textsuperscript{21}

15. The National Audit Office’s analysis of the projects in its report shows that in the early part of projects, procurement management is a major cause of time and cost delays.\textsuperscript{22} This suggests that commercial arrangements are not always sufficiently mature when the main investment decision is made. The Department is increasingly choosing to deliver its assessment phase projects in ‘bite-sized chunks’ in order to better understand the risks on projects before the main investment decision is taken. The Department’s two-stage Initial Gate and Main Gate approach to acquisition may not always be the most appropriate solution for the Department’s more technically complex projects. The Department is currently considering whether it is always right to agree the main investment decision at the start of the design and development phase, when many of the technical risks will not have been fully identified and understood. The use of increments is a sensible approach to project management, but should the Department choose to break projects down into smaller increments, for example, by having separate decision points for development and production, each must have defined time, cost and performance parameters, to maintain accountability. We would consider it unacceptable if there were any deterioration in the information reported to Parliament and the taxpayer as a result of the Department choosing to design and develop its projects differently.\textsuperscript{23}

16. There will always be some projects where the Department needs to work collaboratively with other countries, or where successful delivery is dependent on a related project or piece of equipment. The Department needs to get better at managing these interdependencies as these can lead to delays. The Beyond Visual Range Air-to-Air Missile has suffered delays and incurred an in-year increase of £55 million because of a lack of Typhoon aircraft for test firings. There are no special trial versions of the Typhoon aircraft available to integrate the missile because of delays to the overall Typhoon programme, and the other partner nations on the Beyond Visual Range Air-to-Air Missile project have been unable to commit to production of the missile. Given these problems, and a revised assessment of the threat, the Department has taken a deliberate decision to slow the delivery of the project by re-defining the In-Service Date so that it has two stages—the first, forecast for 2012 when the missile is ready, and the second, forecast for 2015, when it is integrated onto the Typhoon.\textsuperscript{24}

17. The current economic crisis and weakness of the pound against the Dollar and Euro mean that the Department is likely to see further cost increases on some of its projects in 2008–09. In line with its usual practice, the Department has entered into forward currency contracts for 80% of its expected foreign exchange requirements, so the impact of recent reductions in the value of the pound is less than it would have been had the Department purchased all its Dollars and Euros on the open market. For the remaining 20%, there will be impacts on individual projects, but the Department was unable to quantify how much

\textsuperscript{21} Qq 61–62
\textsuperscript{22} C&AG’s Report, para 9
\textsuperscript{23} Qq 30, 32
\textsuperscript{24} Qq 13, 72–74, 103
this would be across its Equipment Programme as a whole.\textsuperscript{25} Although there is a limited amount the Department can do to manage the impact of exchange rate fluctuations, as its ability to forward buy is currently under review with the implementation of international financial standards, the Department could do more to factor this in when making procurement decisions.\textsuperscript{26}

\textsuperscript{25} Ev 15
\textsuperscript{26} Qq 37, 41, 76–78
Formal Minutes

Monday 30 March 2009

Members present:

Mr Edward Leigh, in the Chair

Mr Richard Bacon    Rt Hon David Curry
Angela Browning     Rt Hon Alan Williams

Draft Report (Ministry of Defence: Major Projects Report 2008), proposed by the Chairman, brought up and read.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 17 read and agreed to.

Conclusions and recommendations read and agreed to.

Summary read and agreed to.

Resolved, That the Report be the Twentieth Report of the Committee to the House.

Ordered, That the Chairman make the Report to the House.

[Adjourned till Monday 27 April at 4.30 pm]
Witnesses

Monday 19 January 2009

Sir Bill Jeffrey KCB, Permanent Under Secretary, General Sir Kevin O’Donoghue KCB CBE, Chief of Defence Materiel, and Lieutenant General Andrew Figgures CBE, Deputy Chief of Defence Staff (Equipment Capability), Ministry of Defence

List of written evidence

Ministry of Defence
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Oral evidence

Taken before the Committee of Public Accounts
on Monday 19 January 2009

Members present:
Mr Edward Leigh, in the Chair
Angela Browning
Mr Paul Burstow
Mr David Curry
Mr Ian Davidson
Mr Tim Burr,
Comptroller and Auditor General,
Mr Jim Rickleton, Assistant Auditor General,
Mr Tim Banfield, Director, National Audit Office,
Mr Marius Gallaher, Alternate Treasury Officer of Accounts, HM Treasury,

Mr Tim Burr, Comptroller and Auditor General, Mr Jim Rickleton, Assistant Auditor General, and Mr Tim Banfield, Director, National Audit Office, gave evidence.

Mr Marius Gallaher, Alternate Treasury Officer of Accounts, HM Treasury, was in attendance.

REPORT BY THE COMPTROLLER AND AUDITOR GENERAL

MINISTRY OF DEFENCE: MAJOR PROJECTS REPORT 2008 (HC165)

Witnesses: Sir Bill Jeffrey KCB, Permanent Under Secretary, Ministry of Defence, General Sir Kevin O'Donoghue KCB, CBE, Chief of Defence Materiel, Ministry of Defence and Lieutenant General Andrew Figgures CB, CBE, Deputy Chief of Defence Staff (Equipment Capability), Ministry of Defence, gave evidence.

Q1 Chairman: Good afternoon. Welcome to the Committee of Public Accounts where today we are considering the Comptroller and Auditor General’s Major Projects Report, which we do every year, looking at the Ministry of Defence’s procurement in the year ended 31 March 2008. We welcome back to our Committee Sir Bill Jeffrey, Permanent Under Secretary of the Ministry of Defence, General Sir Kevin O’Donoghue, Chief of Defence Materiel and Lieutenant General Andrew Figgures, Deputy Chief of Defence Staff. Sir Bill, you are very welcome and, if I may, I will address my questions to you but if either of the generals wish to answer them that is fine by us. This is the worst slippage in-year since 2003. If we look at figure 7, which you find on page 13, you will see that the three projects with the biggest in-year delays were all approved after the introduction of Smart Acquisition. Does this mean that Smart Acquisition is failing?

Sir Bill Jeffrey: I do not think it does. For one thing Smart Acquisition is the label we use to describe changes that were made in the late 1990s and we have since then been pursuing a steady programme of trying to improve our capability in this area. It is a moot point whether three of these projects pre- or post-date it. The initial gate pre-dates the introduction of Smart Acquisition. Does this mean that Smart Acquisition is failing?

Sir Bill Jeffrey: I do not think it does. For one thing Smart Acquisition is the label we use to describe changes that were made in the late 1990s and we have since then been pursuing a steady programme of trying to improve our capability in this area. It is a moot point whether three of these projects pre- or post-date it. The initial gate pre-dates the introduction of Smart Acquisition, apart from one of them which is NEST which was a very specific case, as the Report brings out, because it is a project in which we are extremely reliant upon our American allies. I am not suggesting for a moment that we are other than disappointed that there has been this degree of time slippage in the year 2007–08 but I would not draw the conclusion from it that all the things we have been trying to do to improve our procurement performance have been unsuccessful.

Q2 Chairman: Others can come back on that. I do not want to delay because we have a lot to ask. Page 10, paragraph 1.1, we see that this year the overall forecast cost of the projects increased by £205 million. Last year, as you know, we were quite critical of you because you transferred £1 billion across between accounts. I have to congratulate you that you seem to have taken that on board. The fact is that we have this £205 million overall forecast increase so what is going to be cut? Presumably something will have to be cut or delayed.

Sir Bill Jeffrey: I am grateful for your comments about the re-categorisation of the past. Without being too recalcitrant, it really reflects the fact that we have done as much of it in the past as seemed justified but it does mean, without tempting the Committee’s ire and revisiting last year’s issues, that it is harder to interpret the significance of the £205 million than might otherwise have been. The £205 million very largely, as the NAO bring out in their commentary, is down to two projects, Nimrod and BVRAAM, both of which pre-date the main acquisition changes. Although we would prefer it to be zero it is worth bearing in mind that it compares with the total estimated value.

Q3 Chairman: I did not ask you that. That all may be true but what I am asking you is the fact that £205 million is now lost, what is going to be cut?

Sir Bill Jeffrey: It is hard, as it was when we went into this area last year, to be specific about that. The truth is that we revisit our equipment programme, and the costings of the entire programme, most years. We are in the middle of a planning round now and our ministers took some decisions a month or so ago.
Q4 Chairman: You either cannot or will not tell us. Sir Bill Jeffrey: We cannot point to specifics and say as a result of this cost increase we will not be able to do X. It is much more complicated than that.

Q5 Chairman: Let us look at Soothsayer for a second. If we read paragraph 2.23 on page 20, you can see the fact that project managers and key subcontractors were originally located in the United States. Soothsayer is in trouble. Was this not a mistake? Your eye was off the ball. They were in the United States, you were over here and you were not sufficiently in contact with Soothsayer.

Sir Bill Jeffrey: It is not unusual, where we do acquire equipment from the US, for many of those most heavily involved in the project to be US-based. I think we would accept the comment that the NAO make in their Report that we might have done more to monitor the project at earlier stages but what we have now done, and it has been in place for some time now, is to ensure that the project manager is UK-based.

Q6 Chairman: You have learnt the lesson on that failure. You accept it was a failure and you have learnt that lesson.

Sir Bill Jeffrey: The project, as a consequence, is in a much better place than it was.

Q7 Chairman: I have to run through these quickly as we have very little time. There are huge issues involved but the Committee can explore them in more detail if I lay the initial ground. Let us look at the A400M project. This continues to slip badly and there could well be a big capability gap, could there not? I think the Secretary of State made an announcement only last week saying we cannot accept a three- or four-year delay in delivery of these aircraft. What is going to happen?

Sir Bill Jeffrey: It is no secret that in addition to the nine months delay that this Report reveals in 2007–08, the company have relatively recently told us that we can expect further significant delay. We are still assessing the implications of that and putting the right defensive aids suites, and so on, on. There are a number of options which we are actively looking at which we could bring into play as necessary.

Q8 Chairman: I know what the Secretary of State said. I know it is a worrying situation. I want to know what you are doing about it. These things were going to be introduced in 2018. The original Hercules is not going to be operating after when?

Sir Bill Jeffrey: There is more than one.

Q9 Chairman: The present fleet will not be operating after when?

Sir Bill Jeffrey: They will be phased out over a period.

Q10 Chairman: I think 2012, so already these are aircraft flying very dangerous missions in Afghanistan. They were designed basically to get our troops from this country into theatre. They are now being used in very dangerous circumstances for short hops in Afghanistan. They are under tremendous pressure, they are running out of steam very quickly, certainly by 2012, and you have this appalling capability gap. What are you going to do about it?

Sir Bill Jeffrey: What we are doing is making it abundantly clear to the company that we cannot accept any significant further delay and we have discussed with them the implications of that.

Q11 Chairman: I am very interested in what you are making clear to the company but I want to know how you are going to cover this capability gap.

Sir Bill Jeffrey: And in the meantime looking at ways of covering the capability gap. The general himself, in evidence to the Defence Committee, gave an indication of it some time ago.

General Sir Kevin O’Donoghue: There are a number of options. We could buy more C-17. We could buy more C-130J. We could spend some money on the Ks to extend them; we are extending them anyway and we need to re-wing them to extend those. We could see whether we could bring forward the FSTA, the Future Strategic Tanker Aircraft, or some of them, and put the right defensive aids suites, and so on, on.

There are a number of options which we are actively looking at which we could bring into play as necessary.

Q12 Chairman: That is a fair answer. Thank you very much for that. Can I ask Sir Bill about the Nimrod. This is also seven year’s late. The relevant paragraphs where this is dealt with are at 2.2 and 2.3 on page 18. We have the MR2 variant; unbelievably it was introduced in 1969 and still flying. The MRA 4 is now seven years late. You have already lost one over Afghanistan, how are you going to ensure the present ones are safe to fly?

Sir Bill Jeffrey: There are two issues there: one is the safeness to fly of the existing MR2s, and at the moment this is a matter of which our air colleagues are satisfied that they are safe to fly. The problem has been, however, with the new generation MRA4. This does certainly pre-date Smart Acquisition. The main gate was as long ago as, I am ashamed to say, 1996. It has been one of our most problematic projects because early on we were definitely over-optimistic about the technical challenge that its construction would represent. We are now in a more settled position in the sense that we have a new production contract let in 2006 and we believe we are on course to introduce them in December 2010. It has not been a happy story, I entirely accept that.

Q13 Chairman: We can pursue that in more detail later. Can I now ask you about Beyond Visual Range Air-to-Air Missile. This is dealt in paragraph 2.35 if you want to look at that. There was some recent coverage about Jim Callaghan’s comments in the recently released documents on the 30 Year Rule. He said: “Has anybody worked out whether we can defend ourselves.” Apparently we did not have enough missiles at that stage. Perhaps you can reassure me that, in the light of what is going on here, we can defend ourselves.
Sir Bill Jeffrey: The BVRAAM story is about responding to a change in the strategic conditions. We are dependent on others. We are dependent on the pace of the Typhoon project and, as you may want to draw out in later questions, we feel we have responded pragmatically to the changes that we have faced. On the specific question of are we well enough placed to defensively—

Q14 Chairman: Can you assure this Committee, Sir Bill, that we have enough missiles to defend our airspace? It is a simple question.

Sir Bill Jeffrey: At the moment what we are doing with Typhoon is arming them with the Advanced Medium Range Air-to-Air Missile which is not as capable as the BVRAAM but will meet the immediate requirements.

Q15 Chairman: You can give me that assurance I just asked for.

Lieutenant General Figgures: Yes.

Q16 Chairman: My last question is about the Terrier. Frankly JCBs have been purchased at a fraction of the cost of what Terrier is costing us and it is still not ready. Again this is another area where “the best is the enemy of the good”.

Sir Bill Jeffrey: Because the Terrier programme has slipped as much as it has, we have acquired JCBs off the shelf and they are serving an important purpose on current ops. They are not as flexible as the Terrier will be cross-country and not as well-protected so we still think it is vital to persist with the Terrier programme.

Q17 Chairman: Is it better to have a solution which is far cheaper that actually works than something we have not even got?

Sir Bill Jeffrey: At the moment it is better to have JCBs because it is what we can acquire and we have used the UOR (Urgent Operational Requirements) process effectively to deliver them into theatre.

Q18 Mr Burstow: Perhaps I can start where you have just finished, the issue of the Terrier. The experience of purchasing JCBs is an interesting one. Looking at the Report on page 19, and as we go through paragraphs 2.11 through to 2.14, it seems to identify there a set of risks that unfolded as a consequence of the way in which the procurement was done in the sense of opting for just one prototype vehicle, which introduced additional risks, and then those sections document the various knock-on consequences of doing that. It then goes on to say in paragraph 2.14: “The full extent of the problems on the project became apparent in September 2007 when BAE Systems declared that they had missed one of the programme’s key milestones.” Why was it only then that this all came to light?

Sir Bill Jeffrey: It was identified as an issue earlier by the project team and in April of 2007 the project team instigated a major project review, but it was only in September 2007 that the company themselves concluded that they were not going to meet that milestone of bringing the thing to the state of being ready for production.

Q19 Mr Burstow: This was something that you were aware of earlier. What steps were taken then at those earlier stages to try and put the project back on track? We were told this was going to be in service in September 2008, we are now told the current forecast is December 2011 and we see that it is continuing to clock up additional months of delay.

Sir Bill Jeffrey: As I have said, the team did instigate the programme review in April 2007. I think that undoubtedly led to everybody addressing these problems but it was only in September that the company concluded it. That was the formal point when they notified us that they had to default on the contract to that extent, therefore under the contract we were able to essentially require them to come forward with a rectification plan which they did.

Q20 Mr Burstow: Given all of the experience with this particular project, a very important project in terms of appropriate hardware for construction work in dangerous and difficult situations, do you consider the way in which this has been procured represents value for money?

Sir Bill Jeffrey: I think it will represent value for money in the sense that the price is going to be what it started off as being.

Q21 Mr Burstow: But much later than expected.

Sir Bill Jeffrey: We accepted a bid which involved the use of only one prototype vehicle. That did introduce risk but I think it is fair to say that the problems in the supply chain that BAE Systems encountered are ones that would probably have led to the technical difficulties that delayed the project even if we had more than one prototype. We certainly agree that we might have, with the benefit of hindsight, adopted a proposal that involved more than one. Having said that, it was a competitive procurement. The other thing one can say for this project is that the contract was sufficiently robust and buttoned up for it to be clear that when BAE Systems did default it was down to them to rectify it at their own expense.

Q22 Mr Burstow: With that benefit of hindsight, were you to be involved in this sort equipment in the future, even if this company or another company came along with a very competitive bid this would be one of the key factors you would be looking at.

Sir Bill Jeffrey: We learn from experience. What went wrong in this case, and the General may want to say more about it because it is a project he has seen more of than I have, is more to do with the fact that, particularly through their supply chain, BAE Systems did hit quite serious technical difficulties.

General Sir Kevin O’Donoghue: That is right. I accept your point. If we were to do this again we would think very hard about doing it like this. The project team at the time after a competition judged the risk and believed that this was the best value for money.
Q23 Mr Burstow: Can I come onto another project, Soothsayer, which the Chairman has asked some questions about just to pick up on the experience from this. Again we were told it was going to be in service in December 2006 and it is now down to June 2009. The paragraphs on page 20 set out the background to this: again the technical problems with technical maturity and timeliness of delivery, software problems, further slippage as a consequence of that, then not being able to hit five out of the nine Key User Requirements on the project. At the end of all this, in terms of resolving the problems, it says “The Department is now working with Lockheed Martin to develop a joint risk analysis and to improve the customer-supplier relationship.” Why now and not at the beginning of the project?

General Sir Kevin O’Donoghue: This is technically a very challenging project and I am not surprised that technical risk was perhaps underestimated with hindsight, I concede that. I was perhaps underestimated. There have been risks registered. I think part of the difficulty in having the project team in the States and the MoD project team in the UK was underestimated and I accept your view on that. Mind you, we buy a lot of equipment from overseas where the project team is overseas and that has not always turned into a significant risk.

Q24 Mr Burstow: Presumably if it is an identified risk you manage it. The point I am making through this question, which is dealt with in paragraph 2.24, is that you seem to have been doing the joint risk analysis with Lockheed Martin only once all of the risks have been tripped over. Why was that not part of standard operating procedure to do the joint risk analysis at the outset or did all these things get missed?

General Sir Kevin O’Donoghue: There were risk analyses done by the MoD. There was a risk analysis done by the company. There are lessons to be learnt and I will accept that.

Lieutenant General Figgures: The answer is in that paragraph 2.24, in particular “the company underestimated the scale and technical complexity of the project, so the schedule and technical risk assessment were over-optimistic”. Working with them our assessment of risk would be suitably coloured. We placed some very demanding requirements on them and that over-optimism was a consequence of working with it.

Sir Bill Jeffrey: I would say, although I acknowledge that in the early stages we might have had a tighter grip than we had, the contract was fundamentally sound in the sense that Lockheed Martin, because of the fixed price nature of the contract, is investing its own money to rectify.

Q25 Mr Burstow: I am sure the users of the equipment would be reassured to hear that the contract is fundamentally sound but failed to deliver the thing on time.

General Sir Kevin O’Donoghue: May I come back on that. The user is very keen to get this equipment in service when it is right and would rather wait for it to be right than have it hurried and not right.

Q26 Mr Burstow: There are a lot of projects where perhaps that argument could be advanced but we are told in this Report that the overall delay on the 18 projects for which In-Service Dates are reported is now 483 months, 40 years and three months, a 36% increase on the expected timescales. I presume that not all projects have the requirement for reporting dates so is this just the tip of the iceberg in terms of the amount of delay that is accruing in projects?

Sir Bill Jeffrey: I do not think it is in the sense that the great majority of our projects, the smaller projects often more recent, deliver more to time. That dramatic headline figure of almost 40 years principally reflects some very serious delays in some of our much older projects at an earlier stage in their development. As I said to the Chairman earlier, we are disappointed that there was a further measure of slippage in 2007–08 but it does not compare with what we were experiencing some years earlier.

General Sir Kevin O’Donoghue: If you look at the UOR progress where we spent quite a lot of effort getting UORs into theatre, their delivery to time is very good. More than 80% of them are delivered to the original timescale and that timescale is very compressed anyway.

Q27 Mr Touhig: Following the Committee’s last session on the Major Projects Report there was a deal of to-ing and fro-ing between you and our Clerk. In particular, if I recall, I quoted from some briefing supplied to the Committee and I think you had the view that perhaps those quotes which I used did not reflect the Report. I am going to quote from the briefing again so doubtless you will let us know pretty soon if you do not think it reflects the Report. We are told there are several factors that have contributed to significant cost this year: the first is a worrying one because it says there have been shortcomings in project management; secondly, we are told there has been a lack of realism at the project outset; thirdly, there has been a failure to identify project dependencies; and, fourthly, there has been underestimation of costs. Those are four pretty key issues looking at any project. Do you accept those four points?

Sir Bill Jeffrey: I accept that these are four of the reasons for project failure that we need to address. We are constantly working internally on the issue of getting cost estimation right and not being over-optimistic at the outset because all experience here, and in other countries, is that time and resources spent investing at an early stage in making the hardest and most realistic possible estimates of how long things will take and how much they will cost is time well spent. I certainly accept that these four areas are where we need to address our activities. On project management we have done a great deal, and we can say more about it if the Committee wishes, to build the skills of our project managers.
Q28 Mr Touhig: On that point particularly, that does concern me about project management. Have you discussed with the NAO certain key instances they have given you where they said the project management has failed here or could be better and so on? Have you got examples you are using now to push through the system to say learning from best practice we could have done better?

Sir Bill Jeffrey: We have had a productive discussion with the NAO about all of this and we do try to learn lessons from these reports. I would say that we are doing much more these days to de-risk projects at the assessment stage and, in particular, to break them down into what we called in the past bite-sized chunks as the NAO recommend. We can point to examples of present projects, like the Indirect Fire Precision Attack project and the Search And Rescue Helicopter, where we have done precisely that and our project management is of the highest order. We are also doing more, particularly under the guidance of our present commercial director, to estimate the costs and timescales realistically and to really look hard at what projects should cost rather than what we would like them to cost. Over time we will be able to judge whether all of the measures we have taken make a difference. I certainly would not deny it is still possible to look at a population of projects like this and identify shortcomings but I would argue they are mostly in the past and we are gradually getting more effective at doing this work.

Q29 Mr Touhig: If project management is at fault then you are heading for trouble in any event, but when you have looked at the problems with project management you have discovered you have a lack of people with the right skills in the right place? Why do you think there has been a failure of project management? Here you have a project on XYZ and it has failed because of simple things. Is it just a lack of skills of the right people?

Sir Bill Jeffrey: The Chief of Defence Materiel might want to say something about skills in his area but I certainly feel that if I look at the period during which I have been responsible for these matters, trying, as we all do, to improve performance in this area, skills is the key to it. Our best people in the project management area are exceptionally good. Having been in more than one government department myself they compare with others elsewhere in government but we need to make the skill levels more consistent. We have made some progress, about which Kevin O'Donoghue may want to say something in terms of training and licensing of project managers.

General Sir Kevin O'Donoghue: As far as project managers are concerned, we have licensed 500 in the past year which is a huge step forward. You will recall last year I said that in the five professional areas we were looking at to get the skills and competencies up one was project management and others were commercial and financial and so on. We are progressing extremely well in getting the right level of competence of the staff into the right job. I think we are making huge progress.

Q30 Mr Touhig: The other area that the NAO flag up is the analysis of the projects in the Report shows that procurement management is the key reason for cost and timescale problems early on in the life of projects, with technical factors becoming the main cause later on. Is there a serious problem, because you mentioned Abbey Wood, with your procurement management? Are you again lacking skills in this area?

General Sir Kevin O'Donoghue: Again, the commercial area, which is what I believe the NAO are referring to, requires up-skilling and we are doing a great deal to up-skill our commercial people. Getting qualified commercial people is not something you do in a few months and that takes time. I have recruited staff, a director of commercial, from outside and we are progressing that quite significantly.

Q31 Mr Touhig: Is it your intention to bring in people from outside or because of the nature of defence you have to have a defence background?

General Sir Kevin O'Donoghue: I think that in the ideal world we would have our own people properly qualified to do the work. While we need to spend some time getting our own people up-skilled, I am bringing in people from outside as required.

Sir Bill Jeffrey: As a matter of fact, as the General says, the commercial director in the Defence Equipment and Support Organisation was recruited from outside. The current chief operating officer, who is effectively Kevin O'Donoghue's number two on the project management side of the business, was recruited two or three years ago from outside and promoted from the post to which he was recruited. We are very ready to look outside and it is helping us to gain strength and capability in this area.

Q32 Mr Touhig: The analysis suggests that commercial arrangements are not sufficiently mature when the main investment decision is made. Again, what do you put this down to?

General Sir Kevin O'Donoghue: There is a debate to be had here and we are looking at it as part of the Defence Acquisition Change Programme and in some projects we have changed it. It is always right to agree the main investment decision at the start of the design and development phase or should we go through the development phase, wait until a project is technically de-risked to a much greater degree and then go for the production major investment decision? Projects will vary. In simple projects perhaps going at the start of the development phase is right but with technically difficult projects perhaps it is not.

Q33 Mr Touhig: You came in to the Department in November 2005 and in December 2005 the Department adopted the Defence Industrial Strategy. Where is that? It was supposed to do away with a lot of these problems.

Sir Bill Jeffrey: The Defence Industrial Strategy is, at a higher level, the strategy we are still working to. The themes of that strategy—through life capability management, choosing the acquisition tool that best
meets the case, and clarity about what we think needs to be done and a closer and more open relationship with the industry—are still what is guiding us. We originally intended to reissue the Defence Industrial Strategy before now but the industry themselves would like us to be in a position to give more detail on our thinking on individual sectors before we do so. The short point, and I am glad to have a chance to make it clear, is that our overarching strategy is still the DE & S and will continue to be so.

Q34 Mr Touhig: Do you think the points I have just highlighted coming out of the Report are the key areas you need to address if you are not, year after year, to come before this Committee with the kind of problems that we have again this year?

Sir Bill Jeffrey: Yes is the answer to that. These are the areas we are addressing and have been. We feel that as we work through this we will have better results to show. These are long-standing projects in most cases, some of them of great technical complexity, and it is a never-ending task.

Q35 Mr Touhig: One final question following on from the Chairman’s questions about where we are with various projects and so on, the Financial Times, Sir Kevin, allegedly quoted a memo you sent out in November last year in which they allege you say “The default position is that no business cases are to be put to the approving authorities.” Does that mean everything is on stop?

General Sir Kevin O’Donoghue: No. The memo itself listed a series of criteria which would accept projects to go through to the approval authorities and current operations is one example. I am scrutinising with General Figures and with the finance director all the projects that meet the criteria to make sure that we are spending money effectively and sensibly, but, no, it is not a block on expenditure.

Q36 Mr Touhig: It did not necessarily say you said this but it says the department said it wanted to move away from purchasing equipment for the long-term, equipment that could be out of date by the time it comes into service. That is tongue-in-cheek in view of some of the things in this Report.

Sir Bill Jeffrey: I do not recognise that as an on-the-record statement by the MoD. There may have been people saying that. It may well reflect something we are trying to do which is where we can, within our programme, focus more attention on the requirements that have been thrown up in theatre as against the longer-term investments, but there are some very important longer-term investments that we are completely committed to.

General Sir Kevin O’Donoghue: It is a question of balance. Yes, we have to support current operations in theatre. Yes, we have to retain the seed corn for the future. It is getting those two in balance which is the answer to your question.

Q37 Mr Curry: Sir Bill, the pound which I with even greater reluctance give to the Prime Minister now barely buys me £1.72 EUR and very little short of S2. The pound which I with even greater reluctance give to the Prime Minister now barely buys me 1 EUR and buys me about $1.47. That is bound to have a huge consequence for the cost of procurement programmes. Can you quantify that for me and tell me where it falls hardest?

Sir Bill Jeffrey: Exchange rates do have an implication for us. We do what we can to manage them but some of the kit we do acquire in other currencies. I do not have a figure in my head of what the impact is but I can send the Committee as good a note as we can on the position.

Q38 Mr Curry: The reason I ask the question is because in the document in front of us talking about the A400M project it said that examples of savings were £26 million by deleting the requirement for one of two training simulators (I have no doubt it was put in there with the intention of deleting it) and then another £16 million through favourable exchange rates. Plainly there is going to be a significant adverse effect. Presumably American equipment is contracted for in dollars?

Sir Bill Jeffrey: Generally speaking, not invariably.

Sir Bill Jeffrey: Yes.

Sir Bill Jeffrey: I can certainly confirm that, as a general level, exchange rate movements are one of the financial issues that we are having to address in considering the budget for next year.

Q41 Mr Curry: You cannot buy forward, can you, because by definition the government can only buy forward if it then indicates what it thinks it is going to do with its own management of accounts. That is option excluded to you, is it?

Sir Bill Jeffrey: There is some scope but not as much.

Q42 Mr Curry: The Airbus project in euros?

General Sir Kevin O’Donoghue: Yes.

Q43 Mr Curry: Does the RAF buy fuel forward?

General Sir Kevin O’Donoghue: I do not believe we do.

Q44 Mr Curry: I appreciate that but the extent of the change is actually very considerable. The present exchange rate may move but the difference between what it was like last year and this year is significant.

Sir Bill Jeffrey: I certainly agree that at the moment it is more of an issue than it has been over my time; having said that, it is one of these variables that, when it comes to managing the budget in-year and prospectively a couple of years ahead, we have very much in mind.

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Q45 Mr Curry: The Committee would like a note on that as it is going to be a major factor. Can I come back to the Airbus? You told us when you talked to Airbus you said up to this we will not put. What did they say?

Sir Bill Jeffrey: I do not want to be unhelpful but we are at, for reasons that will be obvious to the Committee, quite a delicate stage in the discussions with Airbus and the A400M management team. I think it is right, as I stated last week, to say clearly on the record how dissatisfied we are with the present state of affairs but I would prefer not to be drawn into the commercial discussions.

Q46 Mr Curry: There are seven countries developing the A400M aircraft and there are some big purchases in there. What is their attitude, the other members of the consortium?

Sir Bill Jeffrey: The other partner nations who are acquiring A400M are as keen as we are to acquire the capability and are as disappointed as we are.

Q47 Mr Curry: Are they all operating Lockheeds at the moment?

Sir Bill Jeffrey: It is a mixture but most of them are operating C-130s.

General Sir Kevin O'Donoghue: Some nations have a greater problem than we do and some of their existing aircraft are older than ours.

Q48 Mr Curry: Is there any joint procurement with these nations of stop-gap aircraft? Would you get a better price?

General Sir Kevin O'Donoghue: We are not there yet. We are not yet at that stage.

Q49 Mr Curry: I thought we were going to have to buy more Lockheeds.

General Sir Kevin O'Donoghue: We may well have to; it is an option. I did not say we were going to have to but it is one of the options.

Sir Bill Jeffrey: Just at this moment what we are saying is discussions with AMSL, the supplying consortia, are going on and therefore, if you would allow us, we need to be a little bit careful what we say. Alongside that, we are looking hard at contingencies of the kind the General mentioned.

Q50 Mr Curry: Looking at it from the outside, Airbus seems to be less than enthusiastic about this aircraft than anything else basically on its stock. It does not radiate belief that this was a hugely urgent project.

Sir Bill Jeffrey: With respect, you had better ask Airbus that question.

Q51 Mr Curry: This is the impression one gets. Can I come to the carriers and can I have a little moan. I am fed up to the eyebrows with ministers telling me that it was very sensible to delay the arrival by two years because it would then have the aeroplanes to put on it. For years and years then presumably we had expected in-service dates knowing that the aircraft would not be there to put on it?

Sir Bill Jeffrey: I do not think it was years and years. We certainly set tentative in-service dates which were the ones we recently moved away from. The timescales for the Joint Strike Fighter itself have been somewhat in question over that period.

Q52 Mr Curry: You will accept that we have had ministers looking particularly smug as if it was some stroke of intellectual genius that they had actually managed to get the aeroplanes and the ships being delivered at the same time. I regard that as a rather commonsense sort of the thing given the activities which inevitably happen on complex projects. Could you advise your ministers to knock off that particular one, it is convincing nobody, and just admit that we have a delay on the damn thing? Making the worse appear the better reason may be good Milton prose but it is does not make good politics.

Sir Bill Jeffrey: It is nevertheless a fact that as a consequence of the re-profiling that the Secretary of State announced just before Christmas, we now have a more coherent one in the sense that we are planning to deliver the carriers at around the same time as the aircraft.

Q53 Mr Curry: If you were a betting man, and as a Scotsman you are a betting man, what money would you place on these carriers ever coming into existence?

Sir Bill Jeffrey: I will give you a more constructive answer than I did last time when you asked me if I was a betting man, which is no, I am not a betting man, but what I do know is the Government is committed to these carriers and intend to deliver them.

Q54 Mr Curry: If I may say so, that is the impeccable reply one would expect from someone in your position and leaves every possibility open. What bothers me is we have two very good aircraft carriers, we have the escorts for them but practically nothing else on the sea at all. Is that a reasonable situation? If the Astute is ever built that would go underneath it but would the whole of the rest of the Navy not be committed to escorting two aircraft carriers of doubtful use?

Sir Bill Jeffrey: There is a bit more on the sea than that. There is the Type 45 which is going ahead and there is Astute which is being built.

Lieutenant General Figgures: Could I just go back to the A400M. You mentioned the two training systems. Mindful that this really needed looking at, we did do a piece of work to work out how long it was going to take to train the crews, and so on and so forth, and in the light of the then proposed delivery programme we reinstated the second training solution. I think you have a fair point there, Mr Curry, and we are grateful for being invited to look again at it. Coming back to the carriers, the Navy, its size and so on, our plan is to build six Type 45s which will be sufficient to secure both the carrier group and the amphibious task group. We have in our plan a programme which will replace the Type 22 and Type 23 frigates and that is part of the Maritime Industrial
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Strategically, we believe that we will be able to address the military tasks required by the carrier strike group plus the other military tasks with the ships we propose to build and as they replace the ships that we have in service. Of course you cannot do everything. It is always a question of priorities but we believe that we will have enough cover for our high priority tasks. Just on the question of the value of the carriers, carrier strike, the ability to project power, equipped with very capable aircraft, this has considerably military utility.

Q55 Mr Curry: I do not doubt they are extremely good bits of kit, my doubts are whether we will find anything we want to use it for which is a different issue. Have you read David Loyn’s book called *Butcher and Bolt* which is a history of foreign involvement in Afghanistan since the 18th Century?

Sir Bill Jeffrey: I have not.

Q56 Mr Curry: Could I recommend it to you. What it demonstrates in great clarity is that every single attempt to intervene in Afghanistan has ended up in catastrophe. If President Obama says “Come on Gordon, old sunshine, if you want to demonstrate that you really want to work with me, more troops, more people into Afghanistan” what is that going to cost us in light of the argument about the equipment of the force in Afghanistan and even the recent post-retirement letter of the senior military, with which I agree, on the replacement of Trident?

Q57 Chairman: It has not much to do with the Major Projects Report although it is a very interesting question.

Sir Bill Jeffrey: Can I answer that or not?

Q58 Chairman: I do not see why not. It is topical and interesting, go ahead.

Sir Bill Jeffrey: Ministers’ attitude and approach to Afghanistan is well known. They are entirely committed to the campaign there and they are always looking at the level of troops that we commit to it. There may well be developments with the advent of a new President but beyond that I cannot say beyond the fact that so far the additional costs of deployments in both Iraq and Afghanistan have been met from the Reserve and I assume that if there were a decision by the Prime Minister and his colleagues to commit more troops to Afghanistan that would apply just as much.

Q59 Chairman: I would like to ask you about Afghanistan but I have to rule myself out of order so I will not. There is a question I must ask about the aircraft carriers which directly follows on from Mr Curry’s comments. This is very topical because on the 16 January the American State Department issued a statement saying that the cost of the Joint Strike Fighter programme is increasing markedly and the cost per individual aircraft is going up, and this relates to the cost of the dollar, from $50-60 million to $80-90 million, a 50% increase. How are you going to cope with this increase in cost?

Sir Bill Jeffrey: What was surprising us was that you were quoting a Department of Defense statement that none of the three of us could recognise.

Chairman: I have it here. It was given to me by the National Audit Office and I will pass it around to you and at the end of the session you can answer it.

Q60 Angela Browning: I have to say this is one of the most depressing and worrying reports I have read which have come before the Committee of Public Accounts. Really there is not a lot I have heard this afternoon that has encouraged me to think that you are actually going to get to grips with the core problems that the NAO have identified. I know you have spoken, and I take it as read, your own goodwill in wanting to learn from what has been identified here but when one reads this document it almost reads like a company that is new in the business. Some of the problems appear to be so fundamental that I find it extraordinary that it is actually a government department with the years of experience that you have had that is still grappling with some problems. If we could I would like to come back to the point Mr Touhig was making, I would like you to turn to page 6 because it is that table 2 which crystallizes the problems and I am still not sure we have answers that convince me that you have the right game plan, if I may say so, to sort these problems out. If I begin by looking at the first one here, and that is the industry project management shortcomings, you have talked about project management and you have said you have now recruited 500 certified new project managers. That sounds good but there are some things about project management that are key not just to the people who are the project managers. Could I ask you how much of your project management relies on appropriately written software?

Sir Bill Jeffrey: It is hard to answer in a quantified way. Of course in many respects the delivering of successful projects turns on the quality of software and in varying degrees software is an aspect of what we are acquiring. I do not know if that is what lay behind your question.

Q61 Angela Browning: If you use software for your project management strategy as well as the individuals who do the managing, the people involved, have you got the right programmes and the right software writers to make sure that your project management systems give those trained people the opportunity to deliver on time and to budget?

Sir Bill Jeffrey: It is certainly the case that we could do more to develop standard systems for project management which are software based, and that is something we are working on, but at the root of these problems, as I think I said earlier, it is partly to do with the standing guidance under which our staff are operating, in which we feel we have made progress, but principally to do with their own skills and that is where we are diverting a lot of our efforts.

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Q62 Angela Browning: Could I ask you to take a more holistic view of the problem you have with project management. I appreciate what you are saying about the individuals and skills and training but they are just one element of project management. If you do not bring them all together as a whole then there are problems. The most worrying thing that I read was to do with the Terrier project in that it demonstrated to me a real lack of grip, and that was that you only became aware of the extent of the problems on Terrier in September 2007 when BAE Systems declared they were in default of the contract. If the suppliers are the people who generate the information and it is only when they supply that information to you that there is a significant problem that you recognise it, that is a very serious situation to be in, is it not?

Sir Bill Jeffrey: In the particular case, as I said earlier in response to Mr Burstow’s question, the project team did spot that the Terrier project was in difficulties and did set up a review some six months earlier. The September 2007 point was the point at which BAE Systems themselves felt that they had got to the position where they had to declare they could not pass an important milestone and we were then into more formal contractual territory. We have to work hard at improving our project management but I would say the best of our people are doing very well. If you look at the headlines in this Report on the cost side, all but two of these projects kept pretty well to cost over the year that we are talking about. On the time slippage side it was a less good performance but it reflected some very difficult technical challenges in a number of our projects, and in particular some dependencies with other countries and partners which are always going to be quite hard to manage. I do not doubt that we still have a lot of work to do but I feel we are heading in the right direction.

General Sir Kevin O’Donoghue: May I just come back as perhaps I was not very clear. I have not recruited 500 extra project managers. We have qualified 500 of our own people. Of course project management is a combination of qualification and experience and so I am satisfied that we are heading in the right direction there.

Q63 Angela Browning: I am glad you said experience and qualification because one of the problems that we encounter in many of the things we look at in the House of Commons, particularly where there are large complex issues, is that, although you need a framework, the experience of the individual not just to tick boxes but to see beyond the boxes is key to things being done well and that experience coming into play. Although I was interested to know about your use of software, I also think that is a very important point. Could I now come to procurement itself, and Mr Touhig touched on this, because clearly there was a lack of realism from the outset. You have said a little bit about these projects and Soothsayer which was procured through the USA. Procuring projects from abroad in any business should not be that much of a difficulty today. After all, it is not as if people have to send letters. There is Cardcam if there are technical difficulties, things like that, where things are conveyed over a computer in a matter of seconds. Why should procuring from abroad lead to these sort of problems?

Sir Bill Jeffrey: We are not saying it does. We are saying that we do acquire from abroad. There are some issues that it is up to us to manage effectively. In the Soothsayer case we probably did not manage that as effectively as we could. We had difficulties in our relationship with Lockheed Martin which are now largely behind us. The point I would strongly agree with is that the initial procurement and the nature of the contact on the deal, as it were, is of crucial importance here. One of the things we have been trying to do in recent years under our commercial director is to improve our central scrutiny of commercial assurance and due diligence around contracts with a view to looking independently from the centre, and the Chief of Defence Materiel is doing the same thing within his area, really looking hard at is this the right deal, are we being over-optimistic, are we assuming this can be done more quickly given how technically challenging is likely to be the case. I strongly feel that one of the things we have to do as a team is to inject realism into this process because where these projects go badly wrong, and many of them go back a decade or more, is where the initial prospectus and the initial deal with the supplier was simply unrealistic.

Q64 Angela Browning: Is that to do with the way these original specifications with the supplier were drawn up?

General Sir Kevin O’Donoghue: I think in some instances it was in the past. In some of those projects perhaps the clarity of the specification was not there. Sometimes I think the projects are over-specified such that the technical risk of delivering them becomes a huge challenge. My previous chief operations officer, David Gould, would have said the way to get projects right is in the project initiation right up front. If you get that right and you have, as you said quite rightly, proper project managers with qualifications and experience then you stand a very good chance of delivering the performance on cost and time.

Q65 Angela Browning: The project managers, the 500 you have qualified, what would their involvement be at procurement stage when the specification and negotiations are going on initially?

General Sir Kevin O’Donoghue: The requirement is drawn up by General Figgures and my project teams will translate that into a proper specification. It is an iterative process. Is that deliverable? Do we think the company can deliver to that specification? Can they deliver in the time and the cost? If we believe that the project is over-specified, then there will be an iterative process. This is the trade-off that the Committee has talked about in the past.

Q66 Angela Browning: I am pleased to hear your advice but I do think this is very worrying. One of the reasons it worried me when I read it was because, as
a Member of Parliament. I have, over my years in parliament, had a little bit of tangential involvement in companies who are in my constituency who supply to the MoD. They are probably much smaller projects. Some of them are quite hi-tech but smaller projects. It has been my experience that the MoD is much more particular on those sorts of projects in their project management process and in the procurement side than these. I appreciate these are bigger more complex projects but nonetheless there does seem to be a difference between the qualities and the experience that you bring to smaller projects and not being able to translate it into these bigger more complex projects. I wonder whether that is something you might look at.

**General Sir Kevin O’Donoghue:** I am not sure that is true. We are post-Smart Acquisition bringing in a much greater degree of scrutiny to the projects than we did pre-Smart Acquisition. I am not sure you could look at small or big projects. I know we have talked about the aircraft carriers but that is a project, notwithstanding the announcement recently, that is extremely well defined.

Q67 **Angela Browning:** I used to run a business which ran training courses on procurement but not at this level of procurement I have to say. I always used to say when it came to project management the reason why things slip is one week at a time. If you are 92 weeks over, it has slipped 92 weeks one at a time and it is getting in at the beginning. I hope you will get to grips with what you have promised us to do before we see you again next year.

**Sir Bill Jeffrey:** I appreciate these comments. If I may say so, I regard the Committee as an ally because we try to keep ourselves up to scratch on this. One of the things I fear about this process, the Major Projects Report, is that year by year a lot depends on the projects that happen to be in the top twenty and how they get reported but under the surface we feel we are making some progress.

Q68 **Chairman:** We are allies and that is why we want you to be as open as you possibly can, but you seem to be enormously skilled, as all the best Permanent Secretaries are, in saying as little as possible to us. Am I being unfair to you?

**Sir Bill Jeffrey:** I try to. **Chairman:** Let us be more and more open because we are your ally.

Q69 **Mr Mitchell:** In our Report last year, the Major Projects Report advised against delays to projects to do with short-term funding difficulties. You have had a lot of short-term funding difficulties in your department. Has that led to any delays in the major projects this year?

**Sir Bill Jeffrey:** The Secretary of State before Christmas on the 11 December made a statement about the outcome of our examination of the equipment programme which included, in particular, the information that we were delaying the carrier programme to match the time when the Joint Strike Fighter was accepted. There are certainly some cases of projects being phased over a longer period and that is something we occasionally have to do.

Q70 **Mr Mitchell:** That kind of juggling process does increase costs overall.

**Sir Bill Jeffrey:** It can do; it does not invariably.

Q71 **Mr Mitchell:** I see that there is one project where there has avowedly been a deliberate decision to slow the delivery, the Beyond Visual Range Air-to-Air Missile. I am always suspicious when people give two reasons for delaying a project. One is in response to a revised assessment of the threat, in other words it is not necessary. Does that mean it is not necessary?

**Sir Bill Jeffrey:** It does not mean that it is not necessary.

Q72 **Mr Mitchell:** It will not be a threat for five years?

**Sir Bill Jeffrey:** Among other things it means we are content that by arming Typhoon with the Advanced Medium Air-to-Air Missile we will meet the immediate requirements but we do need the BVRAAM. The problem there has been two things. Our partner nations on the Eurofighter programme have not been able to commit to production of these missiles as early as we have.

Q73 **Mr Mitchell:** You have to keep your fingers crossed and hope there is not a threat.

**Sir Bill Jeffrey:** No, it is not a question of keeping fingers crossed. This is about how capable is the missile capability we need.

**Lieutenant General Figgures:** We have done a lot of work. Clearly in having been told how the programme is developing we went back and said what is this going to do to a threat. We did a lot of work with the Defence Intelligence Service about the possible threats. Just as we have some issues, so do our threats. We believe that this will now come into service at a time such that we will have it before the threat ramps up so I think we are safe.

Q74 **Mr Mitchell:** It is a fact that threat that will materialise. The other reason given is so the missile can be integrated with the Typhoon aircraft more cost effectively. Why can it not be integrated more effectively now?

**Sir Bill Jeffrey:** Because it has not yet been made available by the suppliers in order for the integration to take place. The problem we faced was, first of all, that our partner nations had not been able to commit to production of the missile; secondly, because the Eurofighter project itself was slipping we were unable, a year or so ago, to agree on the availability of Typhoon for test firings and that in itself led to some delay. It is one of these complicated cases where the dependencies with other people have contributed to the delay. What we think we have done is the sensible thing, which is to make Tornados...
available as a test platform for the missile, re-define the In-Service Date so that it has two stages, one when the missile is available and the other when it is actually integrated on Typhoon, and in the meantime arm Typhoon with the Advanced Medium Range Air-to-Air Missile. It is a pragmatic, sensible approach I would argue.

Q75 Mr Mitchell: We will probably discover later on this week to be in a recession and, in my view, it is going to get worse. When I go around Grimsby all the shops are saying 50% off, 75% off, which makes 2.5% off VAT look small. In that intensified competition is that going to benefit you? Are your costs going to escalate in the way they have done in the past?

Sir Bill Jeffrey: Most of what we are doing is contractually committed. Whether this will have an impact on the deals we are able to do going forward is harder to judge.

Q76 Mr Mitchell: Are we in a position to drive tougher bargains?

Sir Bill Jeffrey: In some areas.

General Sir Kevin O’Donoghue: The sort of areas you are talking about are what I would call commodities. Yes, we will be able to drive better bargains in the commodity area.

Q77 Mr Mitchell: Things like rifles.

General Sir Kevin O’Donoghue: No, they are not commodities; they are developed and designed.

Q78 Mr Mitchell: The only commodities you are buying is uniforms.

General Sir Kevin O’Donoghue: Food, clothing and so on, there we might be able to drive a better bargain when the current contracts run out. Where we will not be able to drive a harder bargain is where we have a contract, a nuclear submarine design and build, for example. I do not see that getting cheaper.

Q79 Mr Mitchell: Because there is only one supplier.

General Sir Kevin O’Donoghue: Yes.

Q80 Mr Mitchell: It seems to me as a layman you are spending a lot of money on an obsession with hi-tech. You are like a greedy kid wanting more and more hi-tech equipment. All the Forces are like that. Since the only wars we fight are against men with beards in mountains, why do we need all this hi-tech junk?

Sir Bill Jeffrey: I am tempted to say do not underestimate the sophistication of the men with beards. I spent last Friday talking to General O’Donoghue’s team who deal with protection against improvised explosive devices. In that area, in a very inspiring way, we are getting more and more effective. We have some very clever people working on it. If you look into the future of course some of our longer-term investments are very much the leading edge of technology. As I said earlier, to the extent we can within our budget, we are very keen to find ways of responding to some of the less elaborate and high-end requirements that current experience is throwing up.

Q81 Mr Mitchell: Something that is not terribly hi-tech, the Terrier. The industry bidder’s contract only had one prototype vehicle. This is not a terribly sophisticated thing. Why was that? Did it seem to be so simple you did not need extensive testing on prototypes? Why did they get away with only one prototype when in the long run it has caused a lot of problems?

General Sir Kevin O’Donoghue: It was a competitive bid and at the time that seemed the best value for money.

Q82 Mr Mitchell: The requirement was yours for only one prototype?

General Sir Kevin O’Donoghue: No, the requirement was delivering the outcome of the Terrier engineer tractor. The bid came in with the proposal they only needed one prototype and at the time that seem to offer best value for money than another bid.

Q83 Mr Mitchell: It has turned out to be more expensive.

General Sir Kevin O’Donoghue: The cost has not gone up. The time has gone up but the cost is marginal. The company are bearing the extra cost for putting right what they got wrong.

Q84 Mr Mitchell: They are now employing JCB engineering vehicles which look to me to be OK for the job. Who pays the cost of that, the contractor or you?

Sir Bill Jeffrey: The JCBs that we are deploying in theatre, the cost of these, is met from the reserve as an Urgent Operational Requirement.

Q85 Mr Mitchell: Since the contractor is now in default with the Terrier and the JCB things look pretty satisfactory, why do you not just cancel the project and use JCB kit?

Sir Bill Jeffrey: The military judgment, and General Figures may want to add to this, is that the Terrier when delivered will still provide us with more flexibility and more capability and will be a better product. We are getting good service from the JCBs and it was the right thing to do to get them into theatre because we need them there.

Q86 Mr Mitchell: The high frequency things, we are dependent there on the USA. Why did you not anticipate long delays because of the usual relationship with the USA where delays are built in and you have very little opportunity, as the minor purchaser, to influence the contract?

Sir Bill Jeffrey: Of course we were conscious from the outset that this was a project on which we were dependent on the Americans. It would not have been realistic for us to invest ourselves on our own account. The consequence of that is when the main US project suffers delay we have to live with it. We have kept pretty close to the Americans and our project team meets the US project manager very
regularly indeed. We have developed some interim solutions, which paragraph 2.30 of the Report mentions, which are sensible steps to take in the meantime.

Q87 Mr Mitchell: Having contracts with the USA brings up what the Chairman was talking about. When it was agreed it was £1 to $2, now it is £1 to $1.50 so the expense of all that goes up.

Sir Bill Jeffrey: There is the point that Mr Curry was on that some of the quite substantial exchange rate movements we are seeing at the moment do have an impact on us, yes.

Q88 Mr Mitchell: Why was there no Typhoon available to test the Beyond Visual Range Air-to-Air Missile?

General Sir Kevin O'Donoghue: There are only a limited number of Typhoons which are test-bed Typhoons with all the wiring and the instrumentation to do this job.

Q89 Mr Mitchell: You could not get one of them?

General Sir Kevin O'Donoghue: They were being used to develop Tranche 2. You will recall that Typhoon itself is late and so the Typhoon test aircraft were being used to develop further the Typhoon.

Q90 Mr Davidson: Would it be fair to see yourselves as one of the few beneficiaries of the economic crisis inasmuch as it has diverted attention from what is a pretty poor Report when it indicates that things seem to be going backwards?

Sir Bill Jeffrey: A lot of Committee's earlier questioning was on this point of whether we are making progress or not. I would simply mention that the NAO themselves in the Report acknowledge the fact that we are making progress, and I think we are. It is worth bearing in mind that all but two of these projects kept their costs pretty steady during the year that we are looking at and the two were well-known problematic cases for a long time.

Q91 Mr Davidson: We have a report which indicates this is the worst slippage record since 2003. You are saying that is simply focused on only a couple of projects?

Sir Bill Jeffrey: Time slippage, there are obviously more projects affected by that. I said earlier in the hearing I am disappointed by that. Again if you look under the surface of the individual projects that have suffered time slippage it is predominantly to do with quite serious technical problems that these projects have faced as they have been delivered and, in some cases, the consequence of complex interrelationships with other partners.

Q92 Mr Davidson: I understand that. Given one of the other initiatives that the government has been picking up on opportunities, is it still the case that 90% of top generals are from the 4% of the population who went to private schools?³

³ Ev 15

Lieutenant General Figures: No. I did not go to a private school. I went to a grammar school, and then attended Welbeck Sixth Form College.

Q93 Mr Davidson: You could be one of the ten.

Lieutenant General Figures: I can think of a number of others who were apprentices.

Q94 Mr Davidson: The figure of 9 out of 10 is actually from the Department, which is infallible and therefore must be correct.

Sir Bill Jeffrey: We can certainly update that figure. The other thing I would say, as I did when we responded to you earlier, in some ways an equally interesting figure is the percentage if you look at the main command course and that is quite different.

Q95 Mr Davidson: It would be helpful if you updated us on that, in particular as well as the top generals also the point I did not pick up with you before as to whether or not the bursaries to Sandhurst are disproportionately taken by those from the minority of the population who went to public schools.⁴

Sir Bill Jeffrey: There is another development that I am sure you will be aware of and be interested in and that is the establishment of Mr Millburn’s group on which there will be a two-star General with an army background as a member of the group.

Q96 Mr Davidson: I think that is welcome. As ever, where the Committee of Public Accounts leads the Government follows and picks up these sorts of things at a later stage. I am glad to see that the Type 45 Destroyer is running, as I understand it, to apply no further delays and no further costs. Can I say that given the point that was made earlier on about economic difficulties, I can probably offer you another two at a reduced price compared to the price that you have got the existing ones for if you wanted to discuss this after the meeting!

General Sir Kevin O'Donoghue: How much reduced?

Q97 Mr Davidson: I do not want to discuss it in front of all these other people in case they want to buy them and I would not like to offer them at a worse rate than yourselves! Could I ask about the impact of delays on front-line services. The only one I can see identified clearly is the question of Terrier. Clearly what you have in the field now is inferior to Terrier otherwise you would keep it. I am not entirely clear whether or not there are other delays or cost overruns which are impacting directly upon the troops that we have in the field in both Iraq and Afghanistan and I would grateful if you would clarify that. If you cannot do it now, maybe you would let the Committee have a note on it.

Sir Bill Jeffrey: I think Terrier is the example where if we delivered earlier it would be in theatre earlier and we are using JCBs instead. I do not think any of the other slippages have a direct impact on theatre,

⁴ Ev 16
Q98 Mr Davidson: Maybe you can reflect upon that and if there is something you can come back. I want to pick up the NEST point about the delay and the position of the UK as a junior partner to the US in these circumstances. I think it is this point that is made in the Report at paragraph 2.29, that the Department has only limited ability to influence its progress. What worries me is in the context of the Report we had a little while ago about the submarines, this really confirms the position in spades in a sense. Am I right in thinking that the bald statement we have in this document goes a bit beyond the assurances that you were giving us in relation to the procurement of nuclear submarines and the other elements of nuclear missiles?

Sir Bill Jeffrey: It does but I would argue they are different cases. The successor deterrent project is our project. There are some significant respects in which we are working on it with the Americans; indeed, as in your earlier hearing, there are significant respects in which we are moving ahead of the Americans in collaboration with them. This NEST project is quite different. It is essentially a core US project onto which we piggy-back.

Q99 Mr Davidson: My understanding was there were quite a number of elements of deterrent replacement where essentially we were simply buying into the United States’ project and were very much the minority partner and some of these elements were critical to the success of the deterrent project.

Sir Bill Jeffrey: There are some areas where we are working very closely with them in partnership but the partnership on the nuclear issue is of very long-standing and two way.

Q100 Mr Davidson: I understand all that point but we are still quite clearly the minority partner in those relationships.

Sir Bill Jeffrey: Of course we are.

Q101 Mr Davidson: Does 2.29 not apply to those, having very limited ability to influence its progress?

Sir Bill Jeffrey: In the end the Vanguard successor project is our project. There are significant respects in which it is dependent on the United States but in this NEST project what we are essentially doing is acquiring something that the US were acquiring anyway and if their programme slips in time, although we keep very close to it and we are in close contact with the programme manager, there is not anything we can do about it. I think it is different.

Q102 Mr Davidson: I am not sure I accept that.

Lieutenant General Figgures: If I may, it is not that we do not have the capability that they have. Because this is a programme which is suffering some technical delays which they are penalised by, they have enabled us to equip the Astute submarine with the Super High Frequency Terminal, and the Trafalgar class submarine they have released the Enhanced Ship Submersible Nuclear system. We can provide the necessary information exchange. We know the Trafalgar class submarines when they get the Extremely High Frequency we will have a better capability but it is a capability sufficient to do the job at the moment and it is comparable to the capability that the United States has. Although we may be a junior partner, we are enjoying the same capability benefits.

Q103 Mr Davidson: I do understand that. That was exactly the same as applied to the deterrent replacement which means that essentially we are in the same position: if there is a delay for them there is a delay for us as well and that is the point I was making. I am grateful to have that confirmed. Given the difficulties of our relationship with the United States, given the difficulties that we have in the relationship with the Europeans and the A400M, we have not really got reliable allies that we can trust to develop anything and we cannot afford to do it ourselves. Things do not look all that bright in a sense, or have I misunderstood?

Sir Bill Jeffrey: Any project that is cross-national involving a number of different countries joining together to create capability is more complicated because of that fact than doing it ourselves would be, but as this list of projects illustrates it will very often make sense in the modern world for us to do things with other countries and we just have to get skilful at doing them. It is a degree harder because sometimes in big programmes, especially if there are two or even three countries involved, the thing can move little better than the pace of the slowest.

Q104 Mr Davidson: The final thing I want to pick up relates to the transfer of risk in relation to Terrier. As I understand it there are no costs being passed on to the Ministry of Defence except where they are related to the contract amendments vis-a-vis Bowman. What I am not clear about is the cost of the JCB purchase and everything else, whether or not that is being picked up by BAE or whether or not that got transferred to the MoD to pay for.

General Sir Kevin O'Donoghue: That is not being picked up by BAE Systems but is a charge to the MoD.

Q105 Mr Davidson: In those circumstances the full risk was not transferred to the contractor if you end up paying the bill for whatever you have got to do while they are delayed.

Sir Bill Jeffrey: It was not, as I understand it, part of the original contract that if there was default of that kind the contractor would pay for the supply of an equivalent capability in the meantime.

General Sir Kevin O'Donoghue: There are three risks: one is operational which always rests with us, it has to; one is financial risk, and that very much depends on the way the contract was originally drawn up; and the third is a risk of unreliable equipment, which is what we had in the Terrier example and that is what we are driving back into industry, the reliability of that equipment to do what was said.

Q106 Mr Davidson: In the context of the Report we had seen and the material I had seen before about transfer of risk, I was not entirely clear how much of the risk had actually been transferred. If you leave
you yourselves open to having quite substantial costs as a result of non-delivery or in time lots of reliability standards of a piece of kit, that is a risk that is not transferred and it is not quite as it has been projected to us in the past.

Sir Bill Jeffrey: I certainly think it is true that we must not kid ourselves that we are transferring risk that we actually can’t. That is one of the great lessons of this business that I believe we are learning. In the Terrier case, as I said earlier, the project was such that we did not suffer what we have sometimes suffered in the past which is a cost increase because it was not delivered and more work had to be done on it. BAE Systems are meeting the cost of that but it does not extend to supplying us with something equivalent in the meantime.

Q107 Mr Williams: Going back to the point just raised about NEST communication terminals. Why was it that the risk known to exist in relation to American procurement was not even amongst the first 12 risks identified when the project was being developed?

Sir Bill Jeffrey: It should have been.

Q108 Mr Williams: Why was it not?

Sir Bill Jeffrey: It was self-evidently part of this project and it is certainly the case that since the main investment decision in 2003 the project team has treated --

Q109 Mr Williams: I am not asking what has happened since. I am asking why it was at the time. You said it should not have happened. How did you do it happen?

Sir Bill Jeffrey: I cannot answer that question but I think it may well have been seen by those who were drawing up the project at that stage as a self-evident feature of a project of this kind.

Q110 Mr Williams: The same applied to Soothsayer. It was not recognised as a hazard there as a key risk, why not?

General Sir Kevin O'Donoghue: On NEST, if I may, it is slightly different. NEST is a project that the Americans wanted and they were driving it and, therefore, we did not, but perhaps we should have, necessarily considered it a high risk that it would not be delivered simply because it was American.

Q111 Mr Williams: Not in the top 12 suggests it is a very low risk, otherwise the others must be appalling risks of dealing with the Americans and we should not go near them at all.

General Sir Kevin O'Donoghue: A400M is not American. I suppose you could argue that we should put in every risk register of any product we are buying abroad that this is a risk as we are buying it from abroad but there is a judgment to be made?

Q112 Mr Williams: Slippage of 27 months in one year should represent a high risk and should be identified. It is staggering.

General Sir Kevin O'Donoghue: I think with NEST in particular, because that is a project the Americans wanted delivered, the balance of judgment at the time that it was not put in the risk register was probably reasonable at the time.

Lieutenant General Figures: It comes back to Angela Browning’s point. This is all about understanding the environment in which you are operating. It could be said that there are some impacts of certain risks which we were suffering today and might well have been anticipated are now blindingly obvious in the light of this hindsight.

Q113 Mr Williams: That would be all right if this did not apply, according to our briefing, to the longest delays having been in the three most recently approved projects, if you look at table 7, the Terrier, NEST and Soothsayer. In the case of Terrier, last year alone it was falling behind at a rate of over 2 months a month. 27 months over a year it fell behind. Did that not worry you? Did anyone notice it?

Sir Bill Jeffrey: Yes, it was noticed. Of course it was noticed but the fact is that when projects with this high technical content hit technical problems it sometimes does create very substantial delay.

Q114 Mr Williams: The three most recent projects, according to our briefing, Terrier, NEST and Soothsayer, last year there was an extra 27 months delay in the case of Terrier, 19 months extra delay in the case of NEST, and 16 months extra delay in the case of Soothsayer. Coming back to the original question you were asked by the Chairman, where is Smart Acquisition if our three most recent projects are trailing behind that appallingly badly?

Sir Bill Jeffrey: Terrier was initiated in 1998 and it is back to project initiation.

Q115 Mr Williams: When was it approved?

Sir Bill Jeffrey: It went through main gate in 2002 but it was initiated in 1998.


Sir Bill Jeffrey: Soothsayer was in August 1999, around the time when the changes we are discussing were beginning to be introduced.

Q116 Mr Williams: All three were introduced after Smart Acquisition.

Sir Bill Jeffrey: All passed through main gate after Smart Acquisition but they went through the initial gate either earlier than Smart Acquisition or very close to its introduction.

Q117 Mr Williams: I have a genuine puzzlement. If we go to table 3 on page 8 where it has all the projects listed, if you go down to Typhoon, the fighter aircraft, when it comes to “In-year change on cost to completion” it says “Commercially sensitive”. It does not say it about any of the other projects listed. When you come to “Current forecast cost to completion” again it says “Commercially sensitive” but it does not apply to any of the others on the list. When you come to “Total (historic plus in-year)
Variation” again it says “Commercially sensitive” but that does not apply to any of the others on the list. Why?

Sir Bill Jeffrey: We have been for some time, and continue to be, in close negotiations both with our Eurofighter partner nations and the company themselves about the next tranche of Typhoon. It is a judgment on the Department’s part that it would be unhelpful to these negotiations if we were to publish some of these estimates.

Q118 Mr Williams: In what way would it be unhelpful?

Lieutenant General Figgures: If I may, General Kevin’s predecessor, Sir Peter Spencer, gave an in camera briefing on Typhoon, I seem to recall two years ago, and it has always been addressed privately to the Committee.

Sir Bill Jeffrey: We would be happy to do that again if the Committee wishes to do that.

Mr Williams: I want to get the answer to it so we will do that. I am happy to finish there and let us find out what it is about in private.

Q119 Chairman: You were going to answer my question on Joint Strike Fighter.

Supplementary memorandum from the Ministry of Defence

Question 37 (Mr Curry): Sir Bill, the pound that I reluctantly handed to the Prime Minister when we last met here bought me about 1.72 EUR and very little short of $2. The pound which I with even greater reluctance give to the Prime Minister now barely buys me 1 EUR and buys me about $1.47. That is bound to have a huge consequence for the cost of procurement programmes. Can you quantify that for me and tell me where it falls hardest?

MoD’s practice is to enter into forward currency contracts for a proportion of the Department’s expected foreign exchange requirements, to provide a measure of certainty in the planning process. For 2008–9, that proportion was 80%. The impact of recent reductions in the value of Sterling is less than would have been the case had the Department purchased all US Dollars and Euros on the open market. In relation to the remaining 20%, the impact of currency movements is managed at project level and cannot be identified precisely for the Department as a whole.

Question 59 (Chairman): I would like to ask you about Afghanistan but I have to rule myself out of order so I will not. There is a question I must ask about the aircraft carriers which directly follows on from Mr Curry’s comments. This is very topical because on the 16 January the American State Defence Department issued a statement saying that the cost of the Joint Strike Fighter Programme is increasing markedly and the cost per individual aircraft is going up, and this relates to the cost of the dollar, from $50–60 million to $80–90 million, a 50% increase. How are you going to cope with this increase in cost?

The statement drawn up by the Chairman was made by Major General Davis, Joint Strike Fighter Programme Executive Officer and focuses mainly on support for the programme within the new Congress and the potential impact on the cost of aircraft if fewer are ordered. We do not recognise the unit costs quoted by the Chairman—and certainly not the 50% increase which his question implies—but our cost model and budget reflect current assumptions about the cost of STOVL aircraft based on when they are likely to be purchased on the production curve.
Question 92 (Mr Davidson): Given one of the other initiatives that the Government has been picking up on opportunities, is it still the case that 90% of top generals are from the 4% of the population who went to private schools?

Question 95 (Mr Davidson): . . . I did not pick up with you before as to whether or not the paths that lead to Sandhurst are disproportionately taken by those from the minority of the population who went to public schools.

As at 4 February 2009, nine of the Army’s 10 most senior officers were privately educated. As these figures reflect the educational background of those joining the Services up to 30 years ago, some additional work has been done to look at comparable data for Army officers attending the Advanced Command and Staff Course, which trains middle ranking officers assessed as having the potential for promotion to the highest ranks. This shows the following proportions:

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<th>2007</th>
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<th>2008</th>
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<tbody>
<tr>
<td></td>
<td>State School</td>
<td>Private School</td>
<td>State School</td>
</tr>
<tr>
<td><strong>Army</strong></td>
<td>58%</td>
<td>42%</td>
<td>56%</td>
</tr>
</tbody>
</table>

The following table shows the most recently available data in terms of Royal Military Academy, Sandhurst’s intake from state and private schools. It demonstrates that, for five out of the last six quarters for which figures are available, the majority of recruits were educated at state schools:

<table>
<thead>
<tr>
<th></th>
<th>2007</th>
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<th>2008</th>
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<tbody>
<tr>
<td></td>
<td>State School</td>
<td>Private School</td>
<td>State School</td>
</tr>
<tr>
<td><strong>January</strong></td>
<td>59%</td>
<td>41%</td>
<td>59%</td>
</tr>
<tr>
<td><strong>May</strong></td>
<td>66%</td>
<td>34%</td>
<td>70%</td>
</tr>
<tr>
<td><strong>September</strong></td>
<td>62%</td>
<td>38%</td>
<td>44%</td>
</tr>
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*6 February 2009*