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**Dame Meg Hillier**
**Chair of the Committee of Public Accounts**
*Sent electronically*

Dear Chair,

**DEFENCE INVENTORY**

I am writing to follow up the oral evidence session held on 13 November 2023, at which I gave evidence alongside Vice Admiral Andrew Kyte (Chief of Defence Logistics & Support), Mr Andrew Start (CEO Defence Equipment & Support) and Mr John Farrow (Director Logistics & Support Operating Centre). We agreed to provide further information on subjects outlined below which were raised during the session.

I would like first to apologise for the excessive delay in writing to you following the hearing. The Committee has now published its report on this topic and the Department will follow up your recommendations through the usual Treasury Minute process and the specific written updates at the six and 12 month points that you have requested. Although late, I think it worth responding here to the requests for follow up raised in the hearing.

Part of the reason for this delay is that it has now been brought to my attention that there is an error in our reporting of inventory stockpile holdings, which has been reflected in the NAO report that underpinned the Committee's work on this issue, despite my having agreed its accuracy as part of the clearance process. I apologise. I have wanted to establish the facts and be clear that updated data was accurate before coming back to you. Let me deal with this point first before the broader follow up.

In its key facts section and opening paragraph, the NAO report states that our inventory holdings on our system amount to some 740 million individual items of stock spread across 640k different line items. This data repeats information included in the Department's Annual Report and Accounts – specifically Note 8 on inventory holdings – and that was the basis on which the NAO report was judged to be fully accurate and so signed off. But the data in the Annual Report and Accounts on quantities is incorrect or more precisely has not been updated since 2017/18. The correct data, which demonstrates markedly more success in managing down our inventory holdings than we have claimed, is shown in the table below:

| Financial Year | Type of Items | Number of Items |
|---|---|---|
| 2022-23 | 517k | 457M |
| 2021-22 | 523k | 507M |
| 2020-21 | 528k | 550M |
| 2019-20 | 557k | 559M |
| 2018-19 | 598k | 559M |
| 2017-18 | 640k | 740M |

On my initial review, this looks to me like a reporting error in the Departmental accounts (and I see it as a Departmental error rather than one shared with the NAO), but it is important nonetheless and there is no real excuse for our not having spotted it much earlier. The Note to the accounts on volumes of inventory is essentially narrative and is not audited. The financial values of the stock that we hold are audited and I am confident in their accuracy in each set of accounts. These values have been reducing over recent years due to proactive action by the Department and as platforms and equipment have been withdrawn from service at the ends of their useful life. The reporting error highlights the point made by the Committee, the NAO and indeed MOD witnesses at your hearing that management of inventory is not yet as joined up as it needs to be, although we are making progress on addressing that legacy. Put simply, we have been actively managing the component parts of our inventory holdings rather than this overall quantity shown on our systems. Nevertheless it is important that we are both able to report this data accurately and to do so in a way that builds confidence in our management of inventory. Ensuring consistent and validated data is central to the approach we are taking under the Business Modernisation for Support programme.

We will respond to the Committee's request for targets for overall inventory holdings in line with your report's recommendations, but in the meantime I have asked the Comptroller and Auditor General to come back in to the Department to look at this error in our reporting and make recommendations on how we can tighten our processes in future. I will be happy to share that with you.

**Overlapping MoD contracts and associated logistics systems**

At the hearing, there was discussion on multiple MOD contracts and associated logistic systems and a request for us to explain more clearly how the key programmes, contracts and logistic systems relate to each other. As the NAO report states, there are two support transformation programmes running in MOD that will have a significant impact on the future of inventory management, these are Business Modernisation for Support (BMfS) and Future Defence Support Services.

**Business Modernisation for Support (BMfS)**

BMfS is a pan-Defence business change programme which aims to upgrade Defence's Support Information Systems and implement standardised processes across the Ministry of Defence including for engineering activity, demand, warehousing and transportation of inventory. Today the Armed Forces operate a common inventory demand system and we employ a common inventory pricing system across MOD, but there remain a range of different applications used across the Services for management of inventory supply, warehousing and engineering/ One of the aims of BMfS is to modernise these applications and also enable the transformation of the management of equipment availability and inventory through automation and advance analytics.

As a priority the programme, through the Boeing contract, is replacing the oldest inventory applications, which are used to manage Maritime and Land inventory, with essentially the same modern application that was introduced to manage Air inventory in 2016. Boeing is on track to commence the roll out of the new tri-service base inventory application in 2024 and complete the roll out by end 2025. Thereafter, a competition is underway now to introduce a common system across Defence for management of engineering and maintenance tasks on military equipment, replacing six legacy systems. This will be introduced first into the Land environment followed by Maritime and then Air.

The Committee asked about the decision to award a single source contract in 2020 to Boeing Defence UK to manage the MOD's Logistic Information systems. In 2010 Boeing Defence UK successfully won through competition a 10-year contract to manage the MOD Logistic Information systems. During that period, Boeing modernised the IT infrastructure to deliver consistently high levels of availability of these critical Logistic information systems. Furthermore, Boeing Defence UK helped MOD rationalise the number of Logistic Information System applications that MOD historically operated from 223 (in 2010) to 93 (in 2022), and with plans to reduce to 62 by March 2025. As the end of this contract approached the Department concluded that the lowest risk option to sustain for the short-term the high level of service required, including on some of the oldest applications, would be to extend this arrangement with Boeing Defence UK for a further 5 years during which time competitive procurements would be run under the BMfS programme to modernise and transform MODs logistic processes and applications. The first of these BMfS competitions are now underway. The commercial framework for the new 5-year contract with Boeing Defence UK followed single source pricing arrangements allowing the MOD to assure value for money through transparency of costs and rates.

**Future Defence Support Services (FDSS)**

The second Support transformation programme is Future Defence Support Services (FDSS) which will replace the current Logistics Commodities and Services Transformation (LCST) contract, delivered by Team Leidos and potentially a number of other contacts managed by MOD or its suppliers. This programme aims to identify the best commercial arrangements to deliver commodities procurement, inventory management and logistic storage and transportation solutions. As per Figure 4 of the NAO Defence inventory management report, there are multiple current logistics contracts across Defence that could be consumed or aligned with FDSS depending on the final scope of the programme. The programme is in its concept phase and will explore options and feasibility to enhance the delivery of commodities procurement, inventory managements and logistics solutions through commercial arrangements in the 2026-2028 window.

**Breakdown of the £2.5 Billion quoted in the NAO report (Figure 3 & 4)**

The £2.5 billion forecast spend is made up of the following:

- £515 million on the 5-year contract with BDUK to sustain and modernise current services and applications.
- £2.025 billion for the future Transform phase of BMfS.

**Medical Supplies and managing the risks to Service Personnel**

The Committee asked about how risks associated with medical supplies were managed within the Department. HQ Defence Medical Services Group own the policy on Competent Medical Authority (CMA) and Medicines, however the responsibility for managing the operational risks of medical supplies across Defence is administered by each Command individually. The Operational Chain of Command manages these risks using the advice provided by their CMA, who will advise on the risk of not having the medical material and what can be done to mitigate.

All inventory management issues that create risk are held and mitigated by the Operational Commander. Where the risk cannot be tolerated it is transferred up the Operational Chain of Command. Based on medical advice, the Operational Commander, in this case the Commanding Officer of the ship would either accept the increased risk in order to proceed to sea or delay until the medical inventory issue could be resolved. This is routine operational risk management. It should be noted that this process of managing risk is broadly the same across all three services. In this particular case, as reported by the NAO, the Navy also raised concerns at the 1* Defence Medical Operational Capability Group about medical inventory shortfalls resulting in units carrying increased risk and this was then escalated to the Defence Support Board by DG Defence Medical Services in March 2023.

MOD is funding improvements to the management of medical inventory through the LCST contract as agreed through that risk escalation process which will result in higher levels of availability of key medical equipment and stocks and thus less risk having to be managed by Operational Commanders. Team Leidos are on track to deliver these improvements by December 2024.

Yours sincerely,

**DAVID WILLIAMS**