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Public Accounts Committee

Defence Equipment Plan 2020–2030

Fiftieth Report of Session 2019–21

*Report, together with formal minutes relating
to the report*

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The Committee of Public Accounts

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Summary

The Ministry of Defence (the Department) has published its Equipment Plan (the Plan) each year since 2013, setting out its intended investment in equipment and support projects for the next 10 years. The Department assesses whether this is affordable within its future budget. The Committee remains extremely concerned that the latest Plan was again unaffordable, with the funding shortfall potentially as high as £17.4 billion between 2020 and 2030. The Department also faces significant additional cost pressures—estimated to be more than £20 billion—to develop future military capabilities that are not yet included in the Plan. This is highly destabilising for defence and must not continue. The Committee has highlighted serious affordability issues year after year and, while the Department has made some improvements, it has not yet established a reliable and consistent basis on which to assess the affordability of its equipment programme.

The Department remains stuck in a cycle of focusing on short-term financial pressures. For example, it has sought to balance its annual budget by again deferring or descoping the development of capabilities, resulting in poor long-term value for money, and the use of all its contingency funds in 2020–21 to help offset funding shortfalls, reducing its flexibility to respond to any in-year financial pressures. The Department’s assessment of the Plan’s affordability also assumes it will make significant levels of efficiency savings in the future. However, it has continued to include unrealistic savings in the Plan, including £3.7 billion of savings for which it has not yet implemented plans to deliver. The failure to achieve all of these savings—and find additional savings - will increase the financial pressures and make the Plan even more unaffordable.

In November 2020, the government announced in the Spending Review that it would provide an additional £16.5 billion of defence funding over the next four years. It intends that this funding will allow the Department to modernise and invest in new technologies, including its cyber and space capabilities. The Spending Review has given the Department an opportunity to address the funding shortfalls, even though the announcement of strategic defence priorities, to be set out in the Integrated Review of Security, Defence, Development and Foreign Policy (Integrated Review), has been delayed. However, as the existing equipment budget is not balanced, the Department must make tough choices to end the vicious circle of short-term financial management and delays in developing military capabilities. Once it has established a balanced equipment programme, the Department will need to develop a more sophisticated approach to assessing future funding pressures and managing its equipment expenditure. The Committee intends to scrutinise closely how the Department resets the Equipment Plan to ensure it can deliver future capabilities in a way that achieves value for money.

Introduction

The Department's 2020–2030 Equipment Plan (the Plan) sets out its spending plans for the next 10 years on projects to equip the Armed Forces. It shows that the Department has allocated a budget of £190 billion to equipment and support projects, 41% of its entire forecast budget. The Plan assesses whether its equipment and support projects are affordable. The Department needs to manage this expenditure effectively to ensure the Armed Forces can secure and maintain all the equipment that they need. The Department must also retain a level of flexibility to develop new high-priority capabilities and replace some existing capabilities as they go out of service.

The Department first published its Equipment Plan in 2013. Under the Department's delegated model, managing projects is the responsibility of the Front-Line Commands (Navy, Army, Air and Strategic Command), the Defence Nuclear Organisation and the Strategic Programmes Directorate. These organisations are known as Top-Level Budgets (TLBs) and are required to deliver their agreed defence outcomes within delegated budgets. The Department's Head Office aggregates the information provided by the TLBs to establish the departmental position on the affordability of the Equipment Plan.

Conclusions and recommendations

1. **It is very disappointing that the Department's latest Equipment Plan is unaffordable for the fourth year in a row.** The Department must get a grip on the serious affordability issues that this Committee has highlighted year after year, rather than accept this situation as normal. The Department's central estimate of the funding shortfall on equipment projects over 2020–2030 was £7.3 billion but this figure could be as high as £17.4 billion if certain risks materialise. The Department also faces significant additional cost pressures—estimated to be around £20 billion—to develop future military capabilities which are not yet included in the Plan, alongside wider financial pressures in maintaining the defence estate. We are extremely frustrated by the Department's inability to develop an affordable programme and break the cycle of short-term financial management. In 2020–21, the Department cut £1 billion of spending to balance its annual budget, but yet again did not address the fundamental problem with the long-term unaffordability of the Plan. Year after year, we have highlighted the serious affordability issues and criticised the Department's failure to take the hard choices needed to make the Plan affordable. It is very concerning that the Department seems to have resigned itself to there being a degree of inevitability about the financial problems facing the Department.

Recommendation: *In its next Equipment Plan report, the Department must demonstrate that its Plan is affordable and has the resilience to absorb financial pressures—like cost inflation—and respond to changing capability needs.*

2. **Because of the repeated delays to the publication of the Integrated Review of Security, Defence, Development and Foreign Policy, the Department was not able to provide details of how it proposes to use the £16.5 billion additional defence funding, or what capabilities it will cut to develop a balanced investment programme.** In November 2020, the government announced additional defence funding of £16.5 billion over the next four years. The Department's planning assumption that its budget will grow in real terms by 0.5% per year for the subsequent six years and, as a consequence, it estimated that the Spending Review settlement would result in an extra £30 billion over the next 10 years. This settlement provides—for the first time in many years—a crucial opportunity to tackle the longstanding unaffordability of the equipment programme. As the 2020–2030 Plan is not affordable, the Department needs to make tough choices to reduce the existing funding shortfalls, including disinvestment in capabilities that it decides it no longer needs. The Department also plans to develop new capabilities and establish a new Space Command, but was not clear what level of funding would be available for these initiatives. As ministers had not yet made final decisions, the Department could not provide us with details of how the £16.5 billion would be used, including how much would be allocated to the Equipment Plan or other areas of Defence expenditure. It referred to the forthcoming publication of the Integrated Review, although it could only confirm that this would appear in the 'spring'.

Recommendation: *Within three months of the Integrated Review being published, the Department should provide full transparency on its allocation of the additional funding, including: full details of disinvestment decisions; how the funding has been used to address existing shortfalls; and the investment in new capabilities.*

3. **The Department's failure to break the cycle of short-term financial management is preventing it from developing essential military capabilities in ways that achieve value for money and is restricting its ability to respond to new opportunities or threats.** The Department's continued focus on meeting the Treasury's requirement for it to balance its budget every financial year comes at a huge cost for equipment projects. The Commands have undertaken yet another re-prioritisation exercise to balance the budget for 2020–21, resulting in equipment projects being descoped or delayed. This results in higher costs in future years, with the Department now estimating a funding shortfall of £8.3 billion in the next five years. Furthermore, the Department allocated all its contingency funding at the start of 2020–21 to reduce the funding shortfall, restricting its ability to respond to any unexpected cost pressures during the year. It acknowledged this was not good practice. All funding in the 2020–2030 Plan is also allocated to existing projects, which means that the Department cannot develop new capabilities without further commensurate disinvestment or additional funding. We are deeply concerned at the Department's procurement practices, having seen examples of over-specifying capabilities, a 'salami slicing' approach to projects and a failure to achieve value for money; for example, when the original number of vehicles or ships are not procured on affordability grounds, driving up unit costs. There is a growing risk that the financial pressures and the Department's procurement approach are restricting its ability to exploit new opportunities, such as technological advances, and to develop capabilities to respond to new threats.

Recommendation: *After the Department has translated the decisions in the Integrated Review into a balanced investment programme, it should write to the Committee setting out the key principles of how it will make future investment decisions and manage its equipment budget to achieve value for money.*

4. **The Defence equipment programme is routinely jeopardised by factors that drive inflation in defence projects.** Defence projects are often long-term, complex and involve new technologies, which makes them vulnerable to cost inflation. This Committee has highlighted that inflation in equipment projects can result from factors specific to the defence sector; factors which the Department admitted are not fully understood. We therefore urge the Department to develop a better understanding of these factors, which would include: the availability of new and more expensive technology during the development and build phases; the ambition to maintain interoperability with the USA and other allies; the acquisition of leading-edge capability adding to unit costs instead of accepting more utilitarian specifications which would allow the acquisition of more units; relations with contractors who are in competition with each other to develop new technology; and the culture in Commands to have the best possible equipment at the expense of increased numbers of platforms.

Recommendation: *The Department should undertake a comprehensive study to better understand the drivers of defence costs inflation. This should not merely*

be a statistical exercise but should look at attitudes and behaviours within the defence acquisition system, and how commercial realities and competition with other nations drive up costs. It should report the results to the Committee.

5. **The Department has not established a reliable and sophisticated approach to estimating the cost of its future equipment programme, including setting realistic efficiency savings.** The Department acknowledges the risk of costs escalating on its equipment projects, which are often large, complex projects involving the development of new technologies. The Department’s approach to cost forecasting is likely to understate the risks, with some projects—such as nuclear and IT networks programmes—likely to be at higher risk of cost increases. The Department monitors these risks, including fluctuations in future foreign exchange costs, but has not explored whether its approach to assessing risk remains appropriate for all projects. It also continues to make over-optimistic and inconsistent judgements on future efficiency savings. The Department expects the TLBs to find £12.3 billion of efficiency savings from projects in the Plan and had high confidence in its ability to achieve £8.2 billion of these savings (66% of its target). However, despite our previous recommendations, the Department has again included £2.7 billion of efficiency savings for which it has not yet implemented delivery plans and £1.1 billion of savings with no delivery plans. It also needs to find another £0.4 billion of savings to achieve its savings target. Furthermore, past performance shows the Department has been over optimistic in its ability to achieve planned savings. However, the failure to deliver these savings and find new efficiencies, would mean that the Plan is even less affordable.

Recommendation: *The Department should strengthen its approach to assessing risk in long-term projects, liaising with other government departments to establish and draw on best practice. In the next Equipment Plan report, it should explain the improvements made and set out how it has tested confidence in its ability to deliver planned efficiency savings, including those for 2021–22.*

6. **The Department does not have all the necessary arrangements or qualified staff in place to provide assurance that its Equipment Plan is reliable and has been subject to rigorous quality assurance.** The Department has made some improvements to its production and presentation of the Plan in recent years. But shortcomings remain, particularly around the reliability and consistency of its adjustments to cost forecasts. The Department has also struggled to strengthen its financial capabilities, with no increase in the 41% of finance staff who have a professional finance qualification. The Department acknowledged the shortcomings of its delegated model. Head Office was not able to provide adequate quality assurance on the production of the Plan, with poor visibility of data used by the Top Level Budgets (TLBs), and struggled to challenge the inconsistency in their judgements. There have also been errors in the last three published Equipment Plan reports, raising further concerns over quality assurance.

Recommendation: *The Department should re-assess the role of its Head Office team in providing assurance on the affordability of the Equipment Plan and strengthen financial capabilities across the Department, ensuring that TLBs have adequate capacity and capability to make reliable and consistent assessments of future costs.*

1 Assessing the affordability of the equipment programme

1. On the basis of a report by the Comptroller and Auditor General, we took evidence from the Ministry of Defence on the Equipment Plan 2020–2030.¹

2. The Ministry of Defence (the Department) publishes its Equipment Plan report annually, setting out its intended investment in equipment and support projects over the next 10 years. It assesses whether this is affordable within its future budget. The Equipment Plan summarises the Department’s investment programme over a 10-year period because of the long-term nature of large, complex defence projects. It includes funding for equipment already in use, such as the Lightning II jets, and in development, such as the Type 26 global combat ship. It also includes budgets to support and maintain its military capabilities.²

3. The latest Plan covers the period from 2020 to 2030. It shows that the Department has allocated a budget of £190 billion to equipment and support projects, 41% of its entire forecast budget. It needs to manage this expenditure effectively to ensure the Armed Forces can secure and maintain the equipment they need to meet their military objectives. The Department faces financial pressures across its wider budget and must make choices about investment priorities, which can affect the money available for equipment procurement and support projects.³

4. Under the Department’s delegated model, managing projects is the responsibility of the Front-Line Commands (Navy, Army, Air and Strategic Command), the Defence Nuclear Organisation and the Strategic Programmes Directorate. These organisations are known as Top-Level Budgets (TLBs) and are required to deliver their agreed defence outcomes within delegated budgets. The Department’s Head Office aggregates the information provided by the TLBs to establish the departmental position on the affordability of the Equipment Plan.⁴

The affordability of the 2020–2030 Plan

5. For the fourth successive year, the Equipment Plan remains unaffordable. The Department’s central estimate was that equipment and support costs of £197.4 billion would exceed its budget of £190.0 billion, a shortfall of £7.3 billion over the period 2020–2030. The Department also sets out the best and worst case scenarios to take account of certain risks, and assessed that the shortfall could be as high as £17.4 billion if these risks materialise, equivalent to 9% of the budget over this period.⁵ The Department’s 2020–2030 Plan was based on financial information available at the start of the 2020–21 financial year and was therefore produced before the government announced additional defence funding for the next four years.⁶

1 C&AG’s Report, *The Equipment Plan 2020 to 2030*, Session 2019–21, HC 1037, 12 January 2021

2 C&AG’s Report, para 1

3 C&AG’s Report, para 2

4 C&AG’s Report, para 4

5 Q 64; C&AG’s Report, paras 9, 15

6 C&AG’s Report, para 5

6. The Department also faces substantial additional cost pressures to develop future military capabilities which are not yet reflected in the Plan.⁷ The 2020–2030 Plan excludes the full costs of buying equipment that TLBs will need to replace existing capabilities as they become obsolete, such as the Navy’s mine-hunting capability. The Department has also started major procurement projects, including new submarines and combat aircraft, but has not made full provision to fund them to completion.⁸ It told us that it still needs to make policy decisions on some capabilities, such as the number of additional Lightning II jets it will purchase, and that the Integrated Review will set out its judgements around the development of capabilities, such as Challenger and Warrior.⁹ The National Audit Office found that, based on TLB plans, the cost of filling these capability gaps would be at least £20 billion between 2020–21 and 2029–30.¹⁰

7. In our report on the Equipment Plan 2019–2029, we expressed our concern that the Department had still not established an affordable long-term investment programme in military equipment and had missed opportunities to take the necessary difficult decisions to develop an affordable plan. We urged the government to set a balanced defence budget that reflects new priorities and ambitions in developing capabilities to meet the evolving threats of modern warfare.¹¹ Yet we continue to see the damaging consequences of failing to address the unaffordability of the Plan.¹² The Top Level Budgets (TLBs) were again required to make savings on equipment projects—as they cut over £1 billion from their budgets in 2020–21—and were again restricted from entering into new contracts.¹³ We remain extremely frustrated that the Department has persisted with these practices while still not addressing the fundamental issue of the long-term affordability of its equipment programme.¹⁴

8. When asked if the financial problems with the Defence budget were ever likely to change, the Permanent Secretary pointed first to the Department not having a very good understanding of the drivers of inflation with defence projects. Second, and in his view probably most importantly, he highlighted the inherent difficulties of long-term and technical projects, where threats change, and where new capabilities come along that render as potentially obsolete equipment yet to be procured. He commented that “there is always going to be...a degree of flux, which is difficult to predict, in a defence procurement programme of this scale and tenor.”¹⁵ He also considered that, while the recently announced additional funding put the Department in a “much, much, much better position” to get the whole programme into balance, there would still be “tensions and flux” with which his successor would continue to struggle.¹⁶

9. The Permanent Secretary also explained that the Department has had to live with an annual budget cycle and plan its equipment programme without the certainty of funding over a 10-year period. He explained that this was very difficult to manage. The 2020 Spending Review has provided the Department with the certainty of funding for the

7 Qq 24, 29, 30, 36, 43, 44, 56, 65, 76

8 C&AG’s Report, para 13

9 Qq 31, 32, 72,73

10 C&AG’s Report, para 13

11 Committee of Public Accounts, *Defence Capability and Equipment Plan*, 10th Report of Session 2019–2021, 15 July 2020 paras 1, 7

12 Qq 24, 30, 31, 39,

13 C&AG’s Report, para 2.3

14 Qq 10 - 13,

15 Q 35

16 Q 36

next four years, providing it with a basis for planning and the opportunity to address the structural problems with the Equipment Plan.¹⁷ The Permanent Secretary told us that in 2010 the defence budget had been made affordable, but at the expense of capability. Then in 2015, capability shortfalls were addressed but without sufficient funding. The budget was, therefore, constantly unbalanced in one way or another. He told us that he hoped now to develop a coherent and sensible package of capabilities which are backed up by resources, allowing the Department to plan properly in the longer-term.¹⁸

Producing a reliable assessment of funding shortfalls

10. The Department acknowledged the risk of costs escalating on its biggest programmes—nuclear submarines and IT and communications systems—which are large, complex programmes involving the development of new technologies.¹⁹ It told us it assesses the risk of cost increases on projects and has embedded £13.5 billion in costings to enable senior responsible owners to manage risks that arise from delivering their projects. But the Department admitted that its independent cost assessors had estimated that there was £3.9 billion of risk over and above what is included in project budgets and the Department is also tracking £20 billion of cost increases that it judges, on balance, probably will not occur although at least some of these may materialise.²⁰ The National Audit Office’s report also concluded that the Department’s approach to analysing cost risk and uncertainty means it is likely to have understated the level of risk in the Plan’s central forecast.²¹ While the Department has taken a more prudent approach on some high-risk projects, including the Dreadnought submarine programme, it has not explored whether its approach to assessing risk remains appropriate for new, complex projects.²²

11. The Department acknowledged that its equipment projects are subject to uncertainties that affect their delivery and cost. It is responsible for managing the risk of cost increases within its annual budget. For example, as approximately 15% of the Plan’s forecast expenditure is in euros or dollars, the Department models the impact of foreign exchange movements on future equipment expenditure and reflects a possible 10% reduction in the value of sterling in its worst case scenario of the Plan’s funding shortfall.²³ The Department told us that it is paying very close attention to the impact of the global economic position on foreign exchange rates and is discussing with HM Treasury the effect of the fluctuations on sterling over the last year.²⁴ Furthermore, it monitors the impact on individual programmes as exchange rate fluctuations can create budgetary pressure; for example, it estimated that the costs of the Lightning II programme could increase by £0.8 billion if 2020 exchange rates persisted.²⁵

12. The Department’s adjustments to its cost estimates are still over-optimistic, including its assessment of the level of potential efficiency savings.²⁶ We have previously raised our concerns that the Department was including efficiency savings that it was not confident of

17 Qq 10,11

18 Q 12

19 Q 26

20 Q 41; C&AG’s report, para 1.14

21 C&AG’s report, para 14

22 C&AG’s report, para 14, 1.16

23 C&AG’s report, Figure 7

24 Qq 26, 42

25 Q 27; C&AG’s Report, *Carrier Strike – Preparing for deployment*, Session 2019–21, HC 374, 26 June 2020 para 1.17

26 C&AG’s report, para 14

achieving.²⁷ This year, we again sought assurances that its forecast savings were achievable. The Department told us that it had modelled the maturity level of its forecast savings and had high confidence in its ability to achieve £8.2 billion of efficiencies included in the Equipment Plan, 66% of its £12.3 billion savings target for projects in the 2020–2030 Plan.²⁸ However, despite our previous recommendations, the Department has again included £2.7 billion of efficiency savings for which it has not yet implemented delivery plans and £1.1 billion of savings with no delivery plans. It also needs to find another £0.4 billion of savings to achieve its savings target. If the Department fails to deliver these less mature efficiencies and find new efficiencies, then the Plan would be even less affordable.²⁹

13. The Department acknowledged that its plans for achieving efficiency savings—which are based on thousands of initiatives on equipment projects—did not always deliver the expected returns. It told us that it has introduced more rigorous scrutiny of savings proposals to help develop a better understanding of its ability to deliver future efficiencies.³⁰ However, the Department could not provide confidence it will achieve the forecast savings and accepted the need to continually identify and develop new initiatives.³¹ The Department told us that it needed to include challenging targets in its Equipment Plan to maintain the focus of Commands to drive through efficiencies.³² It also highlighted the need to invest in its approach for achieving efficiencies, such as introducing new digital processes.³³

Developing its financial capabilities

14. We have previously recommended that the Department should improve its financial skills and asked what progress had been made.³⁴ The Department had not increased the number of professionally qualified finance staff, and said it was unhappy that the proportion of finance staff with a professional qualification remained at 41%, the same as last year.³⁵ The Army, Navy and Royal Air Force also had staff shortages in their finance sections, with one third of Equipment Plan-related posts vacant. The Department said it is seeking to train and recruit staff with finance qualifications but acknowledged that these plans were not moving fast enough. Despite not having enough staff with a professional finance qualification, the Department told us that it still had confidence in its cost forecasts.³⁶

15. The Department admitted that its Head Office was not providing sufficient challenge on the financial judgements made by the TLBs when compiling the Equipment Plan.³⁷ Because of the way the Department is organised under the delegated model, Head Office cannot easily access the TLBs' financial information to identify the reasons for changes

27 Committee of Public Accounts, *Defence Equipment Plan 2018–28*, 77th Report of Session 2017–2019, 1 February 2019; Committee of Public Accounts, *Defence Capability and Equipment Plan*, 10th Report of Session 2019–2021, 15 July 2020

28 Q 58; C&AG's report, para 1.24

29 Q 66; C&AG's report, para 14, 1.24

30 Qq 58, 59

31 Q 60

32 Qq 66, 67

33 Q 60

34 Q 81; Committee of Public Accounts, *Defence Equipment Plan 2018–28*, 77th Report of Session 2017–2019, 1 February 2019

35 Q 82

36 Qq 81 - 83

37 Q 84

to the Plan's costs.³⁸ The National Audit Office also found that Head Office did not have the data, resources or remit to undertake the level of quality assurance we would expect.³⁹ The Department told us that it was actively seeking to address the ability of its Head Office to provide an appropriate level of leadership and challenge to the TLBs.⁴⁰ It is seeking to ensure that Head Office has the resource and capability it needs to understand what is going on in the Commands and make balanced investment decisions that take account of the full range of defence activities and priorities.⁴¹

16. The Department claimed it has fulfilled previous Committee recommendations, albeit that it accepted that some improvements were on-going.⁴² The National Audit Office has found that the Department has made improvements to its analysis and reporting, for example improving the presentation and transparency of its Equipment Plan report.⁴³ However, the Department could not demonstrate that its quality assurance work had ensured that the Plan was based on consistent and fully documented data and assumptions. In addition, the Department found errors in its 2017–2027, 2018–2028 and 2019–2029 reports after publication.⁴⁴

38 C&AG's report, para 2.13

39 C&AG's report, para 18

40 Qq 84, 92

41 Q 90

42 Q 9

43 C&AG's report, para 2.16

44 C&AG's report, para 18

2 Managing the funding shortfalls

Re-balancing the equipment programme

17. In November 2020, the government announced that it would provide an additional £16.5 billion of funding over the next four years, which represents a 10% increase in the defence budget over this period.⁴⁵ The Department said that HM Treasury has given it a planning assumption that its budget will grow in real terms by 0.5% per year for the subsequent six years and, as a consequence, it estimated that the Spending Review settlement would result in over £30 billion of additional funding over the next 10 years.⁴⁶ The government intends that this funding will allow the Department to modernise and invest in new technologies, including its cyber and space capabilities. The Integrated Review of Security, Defence, Development and Foreign Policy (the Integrated Review) will set out the strategic decisions on future capabilities that are needed to support the defence and security policy.⁴⁷

18. We have repeatedly urged the Department to take the difficult investment decisions needed to develop a balanced investment programme, highlighting missed opportunities to address fundamental weaknesses in its management of the Equipment Plan.⁴⁸ The Department acknowledged that the lack of certainty over long-term funding had prevented it from taking strategic decisions to address the structural imbalance in the Plan. The Spending Review settlement, announced in November 2020, now gives the Department more certainty of funding over a longer planning horizon and, for the first time in many years, provides it with the opportunity to take strategic decisions around future capabilities. The Department told us that it considered this was a turning point for Defence.⁴⁹ Drawing on the lessons from the strategic reviews in 2010 and 2015, it intends to develop a coherent and balanced 10-year programme of equipment expenditure.⁵⁰

19. The Department could not provide us with a detailed explanation of how it planned to use the additional £16.5 billion of funding as ministers have yet to finalise decisions.⁵¹ Given that the 2020–2030 Equipment Plan is unaffordable, it accepted that it would need to use some of the new funding to address the shortfalls on the existing equipment programme.⁵² The Department told us that, even after this, it will need to cut capabilities to establish an affordable programme and that Ministers faced some tough choices in deciding which capabilities to retire or reduce.⁵³ Furthermore, the Department has been clear that it faces funding pressures elsewhere, for example across its defence estate, and will need to assess how much of the additional resources will be spent on spending infrastructure, people and operations to address shortfalls in these areas. It told us it will set out its plan to manage the next four years and the equipment programme over the next ten years.⁵⁴

45 Q 57

46 Q 28, 40

47 C&AG's report, para 20

48 Committee of Public Accounts, *Defence Capability and Equipment Plan*, 10th Report of Session 2019–2021, 15 July 2020

49 Qq 10, 11

50 Qq 12, 13

51 Qq 14, 39, 54

52 Qq 24, 28, 36, 44 – 49, 56, 57, 102

53 Qq 11, 43

54 Qq 50, 51

20. The Department confirmed that the Integrated Review—which had not been published at the time we took evidence—would contain substantially different capability choices from the current Equipment Plan.⁵⁵ The government intends that the additional funding will be invested in capability enhancements and new technologies, and be used to help the Department to address the financial problems it has faced over the last five years.⁵⁶ As Ministers had not yet made final decisions, the Department could not set out what proportion of the additional funding would be used to develop new capabilities.⁵⁷ The Department told us that details of the specific new programmes and capability cuts will be set out when the Integrated Review is published, and it expected this to be in spring 2021.⁵⁸ We emphasised our intention to continue to scrutinise the outcome of the Integrated Review and the Department’s management of equipment expenditure.⁵⁹

21. The Department assured us that it has been closely involved in the Integrated Review and it had a clear view on the priorities and roles that Defence would need to play in the future. It highlighted the increasing threat from space and cyberspace, and the need to deter and defend against these threats.⁶⁰ The Department plans to prioritise investment in strengthening its capabilities in these domains, as well as continuing to renew the nuclear enterprise and develop the future combat air system. It also plans to develop its capabilities in autonomous systems, expand its global networks, and exploit new technologies by investing in science and technology, and research and development.⁶¹ Furthermore, the Department recognised the need to continue to invest in the support and spares that enable deployments around the world.⁶²

22. We are concerned that the Department has no flexibility in its 2020–2030 Equipment Plan budget, which limits its ability to respond quickly to new or emerging threats.⁶³ The National Audit Office report showed that the Department has only made provision for projects that it has already begun and has not allocated any funding to develop new high-priority capabilities or replace existing capabilities.⁶⁴ The Department allocated all of its 2020–21 contingency in response to the financial pressures that it faces but accepted that its approach was not best practice. It told us that it needed to build some margin back into the programme to avoid repetition of the short-term money saving measures that do not achieve value for money.⁶⁵

23. The Department also needs ‘headroom’ in its budget to keep up with the pace of change on new technologies.⁶⁶ It is therefore assessing how much contingency is appropriate for both the nuclear programme and more conventional equipment projects in the Plan.⁶⁷ The Department told us it also plans to invest in new capabilities for which

55 Q 14

56 Q 24

57 Qq 14, 24, 40, 79

58 Q 25, 53, 99

59 Q 102

60 Q 29

61 Qq 39, 55, 79

62 Q 30

63 Q 95

64 C&AG’s report, para 1.11

65 Qq 38, 42

66 Qq 78, 95

67 Q 41

future funding requirements are unclear. For example, the Department is establishing a new Space Command and seeking to build its capacity in this domain but has not yet set out its investment plan.⁶⁸

Responding to affordability pressures

24. We remain extremely concerned that the Department continues to manage a long-term spending programme on a year-by-year, cash-limited budget.⁶⁹ Faced with funding shortfalls, the Department took a range of measures to balance its 2020–21 budget, including introducing commitment levels on commands' budgets, restricting the introduction of new projects and closely monitoring in-year expenditure.⁷⁰ Furthermore, the Department once again allocated all of its contingency budget at the start of the year to reduce the funding shortfall in 2020–21, limiting its flexibility to respond to any unexpected cost pressures. It agreed with HM Treasury that this was the best way to manage its difficult financial position.⁷¹

25. The National Audit Office has also reported that the Department's continued focus on living within its in-year budget is affecting its ability to develop the military capabilities that are needed.⁷² The commands undertook yet another re-prioritisation exercise to balance the annual budget for 2020–21, either descoping equipment projects or delaying expenditure. This focus on living within its annual budget means the Commands must manage long-term projects within short-term expenditure approvals, which also leads to higher overall costs. The Department now estimates a funding shortfall of £8.3 billion in the next five years.⁷³

26. Faced with an unaffordable programme, we questioned the Department's ability to achieve value for money from its equipment expenditure. We have seen many examples of the Department not buying the quantity of kit or the number of capabilities that it originally intended to buy; such as Typhoons or destroyers.⁷⁴ The Department acknowledged that, historically, it has bought capabilities with sophisticated rather than utilitarian specifications, although it pointed to the Type 31 acquisition as an example of purchasing a more flexible capability.⁷⁵ It also acknowledged that in newer domains, such as cyber and space, its procurement procedures are too slow and have not allowed it to respond to the rapid pace of change on new technologies.⁷⁶

27. While pointing out that this was also a problem encountered by other countries, the Department acknowledged that it did not have a good understanding of the unique factors that drive inflation on defence projects, and that there was work to be done to better understand whether there are better ways of managing or predicting it.⁷⁷ Defence projects are often long-term, complex and involve new cutting-edge technologies. For example, it is likely to be buying Lightning II jets for another 20 years and will need to constantly

68 Qq 4, 74

69 Q 10

70 C&AG's report, para 19

71 Qq 10, 13

72 C&AG's report, para 16

73 C&AG's report, para 1.35

74 Q 35

75 Q 38

76 Q 95

77 Qq 35, 37

update the software in response to technological advances.⁷⁸ The Department accepted it needed to understand and anticipate the factors that affect the cost of projects in order to retain flexibility to manage the delivery of capabilities on the scale of defence projects.⁷⁹

78 Qq 34, 35

79 Q 35

Formal minutes

Thursday 11 March 2021

Virtual meeting

Members present:

Meg Hillier, in the Chair

Mr Gareth Bacon

Peter Grant

Olivia Blake

Craig Mackinlay

Sir Geoffrey Clifton-Brown

James Wild

Barry Gardiner

Draft Report (*Defence Equipment Plan 2020–2030*), proposed by the Chair, brought up and read.

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

Paragraphs 1 to 27 read and agreed to.

Summary agreed to.

Introduction agreed to.

Conclusions and recommendations agreed to.

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

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

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

[Adjourned till Monday 15 March at 1:45pm]

Witnesses

The following witnesses gave evidence. Transcripts can be viewed on the [inquiry publications page](#) of the Committee's website.

Thursday 4 February 2021

Stephen Lovegrove, Permanent Secretary, Ministry of Defence; **Charlie Pate**, Director General, Finance, Ministry of Defence; **Sir Simon Bollom**, CEO Defence Equipment & Support, Ministry of Defence; **Air Marshall Richard Knighton**, Deputy Chief of the Defence Staff (Finance and Military Capability), Ministry of Defence

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Published written evidence

The following written evidence was received and can be viewed on the [inquiry publications page](#) of the Committee's website.

DEP numbers are generated by the evidence processing system and so may not be complete.

- 1 Kiely, Mr Mike ([DEP0001](#))
- 2 Patel, Jag ([DEP0002](#))

List of Reports from the Committee during the current Parliament

All publications from the Committee are available on the [publications page](#) of the Committee's website.

Session 2019–21

Number	Title	Reference
1st	Support for children with special educational needs and disabilities	HC 85
2nd	Defence Nuclear Infrastructure	HC 86
3rd	High Speed 2: Spring 2020 Update	HC 84
4th	EU Exit: Get ready for Brexit Campaign	HC 131
5th	University technical colleges	HC 87
6th	Excess votes 2018–19	HC 243
7th	Gambling regulation: problem gambling and protecting vulnerable people	HC 134
8th	NHS capital expenditure and financial management	HC 344
9th	Water supply and demand management	HC 378
10th	Defence capability and the Equipment Plan	HC 247
11th	Local authority investment in commercial property	HC 312
12th	Management of tax reliefs	HC 379
13th	Whole of Government Response to COVID-19	HC 404
14th	Readying the NHS and social care for the COVID-19 peak	HC 405
15th	Improving the prison estate	HC 244
16th	Progress in remediating dangerous cladding	HC 406
17th	Immigration enforcement	HC 407
18th	NHS nursing workforce	HC 408
19th	Restoration and renewal of the Palace of Westminster	HC 549
20th	Tackling the tax gap	HC 650
21st	Government support for UK exporters	HC 679
22nd	Digital transformation in the NHS	HC 680
23rd	Delivering carrier strike	HC 684
24th	Selecting towns for the Towns Fund	HC 651
25th	Asylum accommodation and support transformation programme	HC 683
26th	Department of Work and Pensions Accounts 2019–20	HC 681
27th	Covid-19: Supply of ventilators	HC 685

Number	Title	Reference
28th	The Nuclear Decommissioning Authority's management of the Magnox contract	HC 653
29th	Whitehall preparations for EU Exit	HC 682
30th	The production and distribution of cash	HC 654
31st	Starter Homes	HC 88
32nd	Specialist Skills in the civil service	HC 686
33rd	Covid-19: Bounce Back Loan Scheme	HC 687
34th	Covid-19: Support for jobs	HC 920
35th	Improving Broadband	HC 688
36th	HMRC performance 2019–20	HC 690
37th	Whole of Government Accounts 2018–19	HC 655
38th	Managing colleges' financial sustainability	HC 692
39th	Lessons from major projects and programmes	HC 694
40th	Achieving government's long-term environmental goals	HC 927
41st	COVID 19: the free school meals voucher scheme	HC 689
42nd	COVID-19: Government procurement and supply of Personal Protective Equipment	HC 928
43rd	COVID-19: Planning for a vaccine Part 1	HC 930
44th	Excess Votes 2019–20	HC 1205
45th	Managing flood risk	HC 931
46th	Achieving Net Zero	HC 935
47th	COVID-19: Test, track and trace (part 1)	HC 932
48th	Digital Services at the Border	HC 936
49th	COVID-19: housing people sleeping rough	HC 934