

Twenty-Second Report of Session 2021-22

Ministry of Defence

Improving the performance of major defence equipment contracts

Introduction from the Committee

The Ministry of Defence (the Department) has been managing suppliers and delivering military equipment programmes critical to our national security for decades. There have been numerous reviews of defence procurement over the past 35 years, which have provided the Department with opportunities to take stock and learn from experience. We are therefore extremely disappointed and frustrated by the continued poor track record of the Department and its suppliers—including significant net delays of 21 years across the programmes most recently examined by the National Audit Office—and by wastage of taxpayers' money running into the billions. The Department is in a disadvantageous position because it relies on a limited specialist supplier base to meet its needs and at times lacks the skilled personnel to effectively manage the performance of these suppliers. Overall, we are very concerned that the Department—and ultimately the taxpayer—bears too much of the financial risks for failure.

Based on a report by the National Audit Office, the Committee took evidence on 12 July 2021 from the Ministry of Defence. The Committee published its report on 3 November 2021. This is the government's response to the Committee's report.

Relevant reports

- NAO report: [Improving the performance of major equipment contracts](#) – Session 2021-22 (HC 298)
- PAC report: [Improving the performance of major defence equipment contracts](#) – Session 2021-22 (HC 185)

Government response to the Committee

1: PAC conclusion: The Department's system for delivering major equipment capabilities is broken and is repeatedly wasting taxpayers' money.

1: PAC recommendation: HM Treasury and the Cabinet Office—with experienced external input—should review the Department's model for delivering equipment capabilities, including assessing:

- ***how the department holds suppliers to account for their performance.***
- ***the culture and relationships between Senior Responsible Owners, end-users and delivery agents.***
- ***how the Department undertakes technical risk assessments to arrive at cost and schedule estimates***

1.1 The government disagrees with the Committee's recommendations.

1.2 The Ministry of Defence (the department or MOD) recognises the challenges with delivering equipment capabilities, challenges which are not unique to UK Defence. There have been many wide-ranging reviews over the years culminating in the 2021 Integrated Review and Defence and Security Industrial Strategy. The department is clear that there is no single over-arching solution to the challenges but continues driving improvements across many areas which specifically include those the Committee has highlighted. This work is both

supported and assured by HM Treasury and Cabinet Office including in specific programme reviews through the Major Projects Review Group. The department believes that it is more appropriate at this time to drive forward these improvements and continue to learn as issues emerge. Therefore, instead of a fundamental review, the department will consider conducting targeted reviews where it will add value to existing change programmes.

1.3 There are comprehensive governance arrangements and robust measures in place to ensure that contractors meet their obligations. As standard, contracts contain management clauses which are constantly monitored to ensure compliance and enable corrective action if necessary. Reviews into the performance of the largest and most important projects are undertaken at senior level through multiple channels across the department, including the Strategic Partnering Team and the Sourcing Council.

1.4 The department acknowledges that some senior responsible owners (SROs) feel they want greater influence over the relevant delivery agents, who operate and are held to account through their own framework documents and governance. To continue to develop and support the role of the SRO, the department is reviewing model SRO activities and developing the Project Delivery function's operating model. This will articulate clear lines of accountability and responsibility between the SRO, Head Office, Commands (end users), and delivery agents.

1.5 The department's acquisition system has evolved significantly in the past decade, including improved Programme, Portfolio and Project Management, stronger functional management and project controls. Industry recognised, class leading Project Management tools and systems are in place, such as Primavera P6, Oracle Unifier, Business Intelligence, and Active Risk Manager, which provide an enterprise-wide view of project performance, underpinned by robust data, policies and procedures including a standard reporting drum beat and consistent Management Information dashboards. The department uses these tools to develop time and cost forecasts prior to procurement which are independently assured as part of the investment case and then monitored throughout the lifetime of the contract.

2: PAC conclusion: We are deeply concerned about departmental witnesses' inability or unwillingness to answer basic questions and give a frank assessment of the state of its major programmes.

2: PAC recommendation: The committee expects the Department to develop a more transparent approach to assessing value for money. In particular, the Accounting Officer Assessments letters—which come to this committee when significant changes occur on major programmes—should include a more detailed and frank assessment of how the changes impact on the value for money case as defined at the start of the programme.

2.1 The government agrees with the Committee's recommendation.

Target implementation date: Spring 2022

2.2 Although the department agrees with the Committee's recommendation it does not agree with the Committee's conclusion. The department assesses the value for money of all its investments. Value for money is evidenced and scrutinised at key approvals and assurance milestones and all programmes in the Government Major Programmes Portfolio must comply with HM Treasury's [Accounting Officer Assessments: guidance \(2021\)](#). Programmes are also considered against the accounting officer tests where the programme is in breach, or potential breach, of the agreed performance, cost, and time envelope.

2.3 The department has a well-documented and embedded accounting officer assessment process, whereby assessments and their accompanying letters are generated by the relevant SRO, before being considered by the Director General Finance and finally decided on by the Permanent Secretary. All four standards - regularity, propriety, value for money, and feasibility - are carefully considered as part of this process. In considering value for money, all assessments are based on evidence and in line with HM Treasury guidance "...make the most plausible projection available".¹

2.4 To ensure continuous review and improvement of activities to drive value for money, the department will ensure that in the future, letters to the Committee contain more of the detailed evidence provided to the Permanent Secretary on which value for money is assessed. The Permanent Secretary writes annually to all SROs as a reminder of this obligation to the Accounting Officer and to ensure the transparency of this process and will do so again by 31 January 2022.

3: PAC conclusion: The Department does not make enough demands of its suppliers to share the financial risks as well as the rewards of contracting for major equipment capabilities.

3: PAC recommendation: The Department should write to the Committee within six months with a clear plan on how it will ensure suppliers take on their fair share of the financial risk in contracts, and how it will take past performance into account when letting new contracts.

3.1 The government agrees with the Committee's recommendation.

Target implementation date: Spring 2022

3.2 Although the department agrees with the Committee's recommendation, it does not agree with the Committee's conclusion. The department recognises the importance of managing supplier performance including the apportionment of financial and programme risk. CAAS (Cost Assurance & Analysis Service) Approvals Team help define specific estimating and scheduling evidence requirements to underpin business cases in accordance with HMT Aqua Book Guidance². This is delivered throughout the lifecycle of programmes continually developing and improving the accuracy of estimates as the project becomes more mature, and its risks fully identified.

3.3 The department accepts that supplier underperformance has been a factor on some programmes, but the use of Firm Price contracts, Liquidated Damages, Single Source regulation reform and other measures have been effective in limiting exposure to cost increases. These measures have resulted in the financial liability for cost over-runs being borne by suppliers. Industry has posted significant losses on contracts (for example the development and production contract for A400M aircraft) as a result of work delivered by MOD programme teams to best understand where financial risk and liabilities rightfully sits between the department and supplier. The practice of government funding the development costs of new capability is well-established across the world. Demanding that most of the upfront development costs are funded by industry before a commitment is made to buy equipment would reduce investment in cutting-edge capability, damage UK industry competitiveness, and runs counter to the policy set out in the DSIS.

3.4 In addition to delivering military capability to the Armed Forces, Equipment Plan investment brings economic benefit, supporting over 200 thousand UK jobs and generating intellectual property (IP) that can be exploited by UK industry in exports. The generation of

¹ [HMT Accounting Officers Assessment Guidance \(2021\)](#), page 8

cutting-edge IP naturally leads to technically challenging and higher risk programmes as the Department strives to maintain operational advantage, while industry also seeks to offer market-leading equipment both for domestic export use.

3.5 The Department will write to the Committee by the end of May 2022 setting out evidence of how it holds its suppliers to account and fairly and responsibly apportions risk and reward across its contracts.

4: PAC conclusion: The Department continually fails to learn from its mistakes.

4: PAC recommendation: The Department should provide the committee with a clear plan on how it will draw on LFE and how its SPP and associated initiatives will generate the level of savings that would be expected from work that is intended to transform the procurement of hundreds of billions of pounds of equipment.

4.1 The government agrees with the Committee's recommendation.

Target implementation date: Summer 2022

4.2 Although the department agrees with the Committee's recommendation it does not agree with the Committee's conclusion. The department has a track record of delivering savings; the underlying cost of the Defence Equipment & Support (DE&S) managed element of the Equipment Plan has reduced by £5.4 billion since 2015, excluding Foreign Exchange or Front-Line Customer requirement changes. £5.7 billion of independently assured efficiencies have also been realised by DE&S since 2015.

4.3 Systems are in place to identify and share lessons as programmes are delivered and the department is working hard to ensure that Learning from Experience (LFE) information becomes increasingly standardised. The National Audit Office (NAO) report specifically commented favourably on some of the improvements that the department has made including the use of industry leading tools and processes for managing project delivery. DE&S, the MOD's principal project Delivery Agent, has recently successfully achieved ISO9001 certification and the independent national certifying body commented specifically on the strong business information that drives performance throughout the portfolio and the continuous improvements that the organisation undertakes.

4.4 The most complex programmes are subject to regular deep dives by the department's most senior staff, providing support and challenge to SROs. MOD executives also regularly meet with industry chief executives of some of the most demanding projects.

4.5 In 2018, the department established a Strategic Partnering Programme (SPP) which is based on good practice principles, transparency and sharing of data and lessons between supplier and commissioner. Category management, also mentioned positively in the NAO report, is in place to support the MOD to deliver £628 million of cashable savings through more efficient ways of working.

4.6 The department is also implementing an Acquisition and Approvals Transformation Programme to improve programme delivery and embed continuous improvement. Proportionate, tailored, risk-based approaches to acquisition are being developed to drive increased pace while maintaining rigour in investment decision-making.

5: PAC conclusion: The Department will not secure a step change in performance until it can recruit and retain the highly skilled staff that it requires.

5: PAC recommendation: The Department and HM Treasury should write to the committee within the next six months setting out how together they will address the gap in skills that it needs for effective contract and supplier management; making the Department competitive in specialist labour markets; and improving retention. In its letter, the Department should also set out what more it will do to get greater continuity in the SRO role, including where feasible a single SRO for the lifetime of a project, and to recognise the role's fundamental importance to delivering military capabilities effectively. The Department should specifically be clearer for military SROs about the scope and ambition for more back-to-back tours, and about how performance in the SRO role will be assessed and is relevant to career paths. For civilian SROs the Department should include specific comment on the scope for more use of fixed-term assignments to ensure that SROs are suitably invested for in the long-term.

5.1 The government agrees with the Committee's recommendation.

Target implementation date: Spring 2022

5.2 The department acknowledges that there is a highly competitive UK market for project delivery skills ranging from experienced project managers, project controls, commercial, and engineers and this is compounded by national shortages and a large UK infrastructure portfolio of work where both public and private sector organisations are in competition for this talent. Noting these challenges, the department has given some freedoms to the professional delivery organisations such as DE&S and the Submarine Delivery Agency (SDA) to help them compete in a demanding UK market for these highly sought-after skills.

5.3 Regarding Project and Contract leadership skills the department will build on its successful participation in the cross-government Cabinet Office sponsored Major Project Leadership Academy and Cabinet Office Contract Management training programme and its ongoing work to recruit and retain expert and specialist resource.

5.4 The department recognises the need to balance time in post for SROs and the need to match leadership with the phase of the project. The department is fully committed to Cabinet Office ambition of ensuring SROs spend at least 50% of their time on their GMPP projects and are working across Defence to increase capacity. The department's Project Delivery function is introducing specific talent and career management for MOD SROs, across both military and civilian postings, to ensure that the right SRO is in place for the right amount of time. The department is investigating a range of options to reduce SRO turnover, including minimum tour lengths aligned to the delivery of key project milestones, rank-range postings, fixed term contracts, retention allowances and the creation of a talent pool.

6: PAC conclusion: The Department continues to be unclear about what additional capability the taxpayer will get from the extra £16.5 billion in the 2020 Spending Review.

6: PAC recommendation: The Committee expects to see absolute clarity in the Equipment Plan 2021–2031 about what additional capability the Armed Forces is getting for the additional £16.5 billion and how it has secured the long-term affordability of the Plan. It should clearly distinguish between new capabilities and those already in development.

6.1 The government agrees with the Committee's recommendation.

Target implementation date: Spring 2022

6.2 Although the department agrees with the Committee's recommendation, it does not agree with the Committee's conclusion. The £16.5 billion extra funding from Spending Review 2020 will support the aims and priorities outlined in the Integrated Review to better counter developing and future threats. Further detail and a breakdown of the £16.5 billion will be provided in the upcoming equipment plan report for publication in February 2022, with a clear distinction between investment in new capabilities and managing the existing shortfall reported in our previous updates. As usual, this will be published alongside the NAO report.

6.3 Recognising the time taken to compile this significant edition of the Equipment Plan, the department has provided updates to the Committee following the publication of the Defence Command Paper in March 2021. The department wrote to the Committee on 22 June with detail of the investments and savings taken through the Integrated Review. The department [wrote again to the Committee](#) on 14 September 2021 in response to the Committee's report on equipment contracts and set out more detail on the new capabilities which will cover.