SPECIAL REPORT

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Improving Defence Management

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Background

In August 2006 the Minister for Defence The Hon Dr Brenden Nelson commissioned a *Defence Management Review* led by Ms Elizabeth Proust. The Review is expected to take around six months and will report directly to the Minister.

The terms of reference for the Review direct an examination and assessment of 'organisational efficiency and effectiveness in the Defence organisation'. Particular issues to be covered include; decision making and business processes, the role of military personnel in executive positions, the management of information and the adequacy of IT systems.

This is the first major external review of Defence in almost a decade. As such, it represents a rare opportunity to bring in outside perspectives to improve the performance of the organisation. There is much at stake. Not only does Defence spend almost $20 billion of taxpayer's money each year, but it plays a critical role in Australia's security.

This *Special Report* presents a range of perspectives and ideas that may be of interest to the Review.

Introduction

Despite recent improvement, Defence management remains imperfect.

This *Special Report* outlines the author's view of problems with Defence management and suggests solutions. Consistent with the Review's terms of reference, no attempt is made to examine the Defence Materiel Organisation (DMO). Nor have the internal management of the Services or their supporting agencies been considered in any detail. Instead, the focus is on the central management and leadership of Defence.

Defence management is of a scale and complexity unparalleled in Australia below that of the state and federal governments themselves. Not only is Defence one of the largest employers in the country—comparable with the Coles and Woolworths retail chains—but it maintains a diverse range of technologically sophisticated military equipment valued at more than $32 billion. Defence is also the country's largest single land owner with more than 30,000 buildings spread across the length and breadth of the continent. In addition, Defence undertakes complex operations at short notice ranging from disaster relief through to peacekeeping and conventional war-fighting. No other entity in Australia has to deal with the diversity and complexity of missions allocated to Defence.

Critically, the ADF is entrusted with the use of deadly force in defence of Australia and, under the Constitution, within Australia when in aid to the civil power. This demands highly effective military command and absolute control by the Australian Government, two factors that greatly complicate the management of Defence.

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Given the criticality, complexity and diversity of Defence, no simple or foolproof arrangement for running the organisation is possible. Nonetheless, substantial improvement is possible both in the short and the longer term.

The situation today

Apart from a series of major reforms to the DMO between 1999 and 2006, Defence's overarching management framework largely reflects that put in place through the 1997 *Defence Reform Program* (DRP).

At the risk of oversimplification, the DRP sought to achieve three things: (1) boost efficiency by consolidating (and where practical outsourcing) support, training and logistics activities previously undertaken by the individual Services, (2) enhance management effectiveness by fusing previously separate, and partially duplicated military and civilian headquarters functions, (3) generate one-off savings by selling Defence-owned properties rendered surplus by geographical consolidation.

The extent to which the DRP actually succeeded in its aims is a matter of debate but its impact on the structure of Defence is unquestioned. As a result of the DRP and some subsequent adjustments (not to mention the important constraints imposed by legislation) the organisation is broadly set out as follows:

The Secretary and Chief of the Defence Force (CDF) sit atop the organisation jointly responsible for the administration of the Defence Force but with the CDF exclusively responsible for the command of the Defence Force [*Defence Act 1903, Part II, Section 9A (1)*]. This arrangement is called the diarchy. Notwithstanding the apparent complexity of the Defence wiring diagram, there are really just three broad organisational components below the diarchy:

- An Australian Defence Headquarters (ADHQ) that formulates policy advice and (in a limited way) administers the remainder of Defence. The ADHQ also includes the direct operational command of the ADF through the Vice Chief of the Defence Force (VCDF) on behalf of the CDF.
- Three military services—Navy, Army, Air Force—and an Intelligence Group that maintain and provide capabilities for, and in support of, military operations.
- Several support agencies including; the DMO that acquires and maintains equipment for the Services, the Defence Support Group (DSG) that provides lodging and base support, and the Defence Science and Technology Organisation (DSTO) that provides scientific and technical support.

One consequence of this broad organisational arrangement is that the Services exercise limited control over many of the inputs to the military capabilities they are nominally responsible for—a direct result of the DRP consolidation of support activities. In this sense, the 1997 DRP sacrificed accountability in pursuit of efficiency.

Effectiveness

Planning and budgeting

The largest single problem facing Defence is the failure to properly plan over the medium to longer term. Despite ferociously complex planning processes, coherence between strategic guidance, capability development and the budget remains elusive.

The current forward estimates do not have enough money to operate the equipment planned under the *Defence Capability Plan* in the years ahead. The *People Plan* does not take account of the personnel that the Services judge necessary to meet current demands let alone those imposed by new equipment. And the much-lauded *Defence Financial Management Plan* appears to encapsulate both of those shortcomings and consequently provides scant forewarning of the financial impact of future plans.

A persistent failure to take account of the cost of operating new equipment lies at the heart of this problem.

Rather than a coherent planning process, Defence is in a constant state of financial crisis. Government is asked—budget after budget—to provide additional money for logistics, personnel, estate and acquisitions. Ad-hoc internal exercises like the *Defence Capability Review* of 2003 and the recent *Review of Defence Logistics* show that Defence's routine planning/business processes do not work. It is noteworthy that the latest logistics review is the third major exercise since 2000 (outside of the budget process) to try and baseline the cost of maintaining ADF capability.

A persistent failure to take account of the cost of operating new equipment lies at the heart of this problem. In fact, analysis of the latest budget papers shows that over the next several years the Defence budget is insufficient to operate existing equipment let alone the new equipment to be delivered by the *Defence Capability Plan*. As a result, notwithstanding recent strong growth in defence spending, Defence cannot afford its current plans and will have to ask the government, yet again, for more money.

There also appear to be problems with the setting of priorities for investment in future capability. Specifically, it is unclear how much strategic discipline is exercised within current planning. The recent initiative by Army to expand by two battalions is an example. Rather then work through the central capability development process, Army prepared its own $10 billion submission to government. Irrespective of the merits of the case to expand the Army (which appear strong) the task of planning the size and shape of the ADF should be done centrally so that the merits of proposals can be judged against the alternatives in a strategic long-term context. The same applies to the unplanned and surprise acquisition of four C-17 aircraft this year at a cost of $2.2 billion.

What makes the current piecemeal approach to planning disappointing is that six years ago the government set out a framework for a coherent rolling ten year planning process in the 2000 White Paper [Chapter 11]. As envisaged, the *Defence Capability Plan* was to encapsulate a holistic approach to the cost of investment, personnel, logistics and all the other components of military capability. Today, the *Defence Capability Plan* has degenerated into a list of future investment projects.

The current approach could easily become unsustainable. If threat perceptions fall or the government's strong fiscal position erodes, Defence will be left with a much-expanded

inventory of equipment and insufficient funds to operate it. Defence planning needs to give the government a clear vision of future costs so that it can make an informed commitment to sustaining the defence force under development.

It is tempting to conclude that the solution is to improve Defence's internal processes for planning and budgeting. This is a necessary, indeed crucial, step and should focus on strengthening financial and operational analysis in Defence. But while this is a necessary step it is not sufficient. As long as the government remains willing to fund ad-hoc capability development proposals (as opposed to formulating a long-term plan) and continues to entertain bids for 'unanticipated' operating and personnel costs, Defence will have no reason to be more disciplined or to plan properly for future costs.

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Accordingly, the government should develop a clear plan for the size and shape of the ADF and give Defence a long-term funding envelope to deliver that plan. Because the government has shown minimal interest in developing a new Defence white paper, a more limited *Force Structure and Sustainability Review* should be undertaken to create a fully costed long-term plan for the ADF. While annual adjustments to the plan will be inevitable and necessary, Defence should be required to deliver the resulting plan within budget as far as possible including anticipated productivity improvements over time.

Governance

The governance of Defence presents a unique problem. The three Services are legislatively constituted institutions rather than subdivisions of a single force, and despite significant progress from the fractious days of the 1980s, a degree of tension remains between military and civilian executives over control and influence. As a consequence, Defence displays all the characteristics of a federation of disparate groups—each operating with its own distinct culture and, at times, its own agenda.

The diarchy

Many critiques of Defence management begin and end by lamenting the complexity and clouded accountability wrought by diarchic leadership. But while other arrangements are possible within the Westminster construct—as New Zealand's separate ministry and defence force demonstrates—one must be careful not to simply exchange one set of problems for another.

If the diarchy were to be abandoned, the legal demands of command authority would mean that the CDF would have to be given pre-eminence, either as head of a single Defence organisation or by relegating the Secretary to a separate (easily marginalised) policy advising rump. Neither arrangement recommends itself. To give the military an effectively exclusive role in advising the Defence Minister on defence matters would be as flawed as having the Health Minister advised solely by doctors or the Education Minister advised solely by teachers. For this reason the Secretary plays an essential role in advising the government on policy matters. This is especially important today when the new security environment increasingly blurs the line between 'policy' and 'operational' issues—a distinction that has always been subtle if not arbitrary.

Thus, while not discounting completely that a better arrangement might be possible, on the available evidence the diarchy is probably no worse than any of the alternatives that are consistent with Westminster style Government. Accordingly, hasten slowly to abandon the diarchy and be very sure that any mooted alternative does not bring with it even greater drawbacks.

Australian Defence Headquarters

In 2006, the previously disparate headquarter functions of strategic policy, capability development, finance, personnel policy, operational command and public affairs/ ministerial liaison were brought together to form the ADHQ in Canberra. (Actually, the DRP created an ADHQ back in 1997 but that turned out to be a short-lived experiment that ended in 2000).

As far as it went, the formation of ADHQ was a good idea. There was an undoubted need to bring together and more closely coordinate these six activities. The only problem is that no one has yet been put in charge of the headquarters, presumably because of the political difficulty of giving a military or civilian pre-eminence below the diarchy.

Someone needs to be put unambiguously in charge of the day-to-day management of the ADHQ.

While a position nominally called 'Chief of Staff' exists in the ADHQ, the responsibilities do not fully encompass the orchestration of the various activities in the ADHQ—let alone those of the three Services and support agencies external to the Headquarters. What's more, the Chief of Staff is of subordinate rank to four of his five colleagues. Someone needs to be put unambiguously in charge of the day-to-day management of the ADHQ. Not only would this improve the administration of Defence but it would free up the Secretary and CDF to concentrate on pressing near-term and strategic long-term issues. This could be done by appointing a civilian *Under Secretary* reporting directly to the Secretary and CDF to oversee the coordination of the headquarters and the administration of the department more generally.

In any such arrangement, care would be needed to ensure that the direct command link between the CDF and VCDF remained unambiguously intact. Having said that, the legal exercise of command should not be confused with formulating broader advice on military operations. The unavoidable overlap between policy and operational matters demands that civilians are directly involved in operational issues. In particular, the Secretary has a responsibility to advise the government on the policy aspects of operational deployments, and any change to the senior management arrangements in Defence must facilitate this.

Finally, the relationship of the ADHQ and the Services warrants mention. The three Services and the Intelligence Group are conspicuous by their exclusion from the ADHQ. There is a respectable argument that they should be involved more closely—perhaps by having the deputy chiefs participate in ADHQ meetings. The counter-argument is that the Services and the Intelligence Group are best kept at arms length from the corporate centre so that they can concentrate on delivering the capability outputs they are responsible for. Noting that the present arrangement does not prevent consultation between the ADHQ and the Services/Intelligence Group, I believe that no further change is called for.

Decision making and committees

A decade ago the *Defence Efficiency Review* observed that 'Defence appears to have too many committees with too many members.' There is no sign that things have changed. The Review should look closely at the number and size of committees with a view to rationalisation. For example, with the Secretary and CDF jointly responsible for the administration of the ADF, and the CDF now supported by a dedicated and extensive Joint Operations Command, what is the role of the Chiefs of Service Committee?

Nonetheless, given the federated structure of Defence it has to be accepted that some decision making will occur in committees. This acceptance must be tempered by two disciplines:

- **More delegation:** The effective governance of an organisation like Defence requires a careful balance between central control (including via committees) and delegated authority (hopefully exercised by individuals). Currently, the balance is skewed towards the former at the expense of the latter. To redress the imbalance, the issues rising up to senior committees (and being pushed back down for speedy resolution at lower levels) needs to be actively managed. The present ADHQ Chief of Staff has some responsibilities in this regard but, once again, a higher ranking Under Secretary would be more effective.
- **Clear accountability:** Committees should act as advisory forums for individual decision makers (as opposed to seeking a lowest common denominator consensus or majority position). From the outside, it is difficult to judge the decision making dynamics of the many committees in Defence. One way to encourage committees to act as advisory forums would be to designate them explicitly as such. The Defence Committee, for example, should be recast as the *SEC/CDF Advisory Forum*.

Contestability

Prior to 1997, contestability was built into Defence structurally in the areas of strategic guidance, capability development and personnel policy. In practice, this involved tension between counterpoised civilian and military elements. Nowhere was this more apparent than in the force development process where the *Force Development and Analysis* division scrutinised equipment investment proposals.

This has now been lost and the only real contestability comes from the various 'central agencies' external to defence, including especially the Department of Finance and Administration. While this is proper, it is also inadequate. No external body can hope to fully understand the issues let alone mount compelling arguments from afar—especially with Defence tightly controlling access to information and data.

Robust internal contestability is particularly important for Defence because group-think is a default in hierarchical organisations.

Robust internal contestability is particularly important for Defence because group-think is a default in hierarchical organisations. Accordingly, while a return to the extensive organisational dualism of the 1980s and 1990s is unwarranted, active and robust contestability needs to be reinstated within Defence. This can most effectively be accomplished by creating an expanded and

independent secretariat function to provide critical analysis of proposals brought forward to senior committees including, but not limited to, capability development.

In the current organisational framework the secretariat would be the responsibility of the ADHQ Chief of Staff, or if the position existed, the Under Secretary in charge of the ADHQ. In either case, accountability for the quality of the analysis produced would rest with the person in charge.

Accountability

One of the unintended consequences of the 1997 DRP (or rather the inevitable consequence of not taking the program to its intended conclusion) is that the Services have been separated from the direct control of many of the resources necessary to manage the delivery of the capabilities for which they are nominally responsible. Put simply, below the level of the Secretary and CDF no single person controls all the inputs (such as logistics, base support, personnel management etc) to ADF military capabilities.

Under the current financial framework, DMO sustainment funding flows through the individual Service budgets, the theory being that the Services are the 'purchasers' of sustainment services. However, there are two problems with the purchaser analogy. First, a conventional purchaser has the scope to make trade-offs and benefit from the resulting savings. This ensures that resource use decisions are made with a view to the benefits that those resources can provide, including in alternative use. Second, a conventional purchaser can consider a range of sources, including self-supply. Absent these conditions, the 'buyer/seller' analogy is strained.

In other areas (such as scientific and corporate support) the Service Chiefs receive support effectively as a 'free good' over which they have limited influence. As a result, the Service Chiefs cannot make the sorts of trade-offs intrinsic to optimising the cost-effective delivery of capability, nor can they be accountable for doing so.

The aim should be for the Services to fully control the resources needs to deliver the capabilities for which they are responsible. This would entail purchasing the goods and services they need from responsive service providers including (but not limited to) DMO, DSG and DSTO. Such a change would be a major shift for defence and would need to be pursued progressively and incrementally in tandem with the development of management information systems necessary to support internal transfers. This is not a change to make quickly, but a vision of the end result needs to be captured early to allow migration to that end state. The current arrangement between DMO and the Services is a good model to build on.

Ultimately, the Service Chiefs should be responsible for the cost-effective delivery of military capability and able to make the decisions inherent in exercising that responsibility.

Ultimately, the Service Chiefs should be responsible for the cost-effective delivery of military capability and able to make the decisions inherent in exercising that responsibility. This would include holding them accountable for the efficient management of the multi-billion dollar capital stock they are entrusted with—a capital stock ultimately owned by taxpayers. Like any other managers, they should be personally accountable through incentives and sanctions for the results they achieve.

Personnel

The performance of Defence can only ever be as good as the calibre of the people it has working for it. For this reason, the effective employment of both civilian and military personnel underpins the organisation's capacity to manage itself. Although the vast majority of Defence personnel are dedicated and hardworking, there are systemic problems with the way Defence manages and uses its people.

Bring in the professionals

One of the key problems compromising Defence management is a lack of professionally qualified and appropriately experienced people in senior and middle ranking positions. There are several reasons for this:

Firstly, the military posting cycle imposes severe constraints. On one level the military posting cycle ensures the orderly professional development of personnel through on-the-job experience. It works particularly well at lower levels where individuals move through a series of progressively more challenging jobs within their Service.

But there are drawbacks to having people change jobs every 18–36 months. At higher levels, and especially away from the core activities of the Services, the posting cycle results in individuals often being posted into specialist positions for which they have neither the experience nor training. This is true in critical areas including human resource management, strategic planning, capability development and other central corporate functions. One of the great paradoxes of military culture is that the Services (quite properly) take a very conservative approach to the development of individual skills in the area of core war-fighting, but assume (quite incorrectly) that corporate and policy roles can be discharged by individuals with no substantive experience or qualifications.

Secondly, on the civilian side of the house, the corresponding malady is the cult of the generalist public service officer who—by writ of broad education—can supposedly undertake any task without subject matter expertise or professional qualification. This belief is most acute at the more senior level where the Senior Executive Service maintains a generic 'capability framework' that reads like a faddish management text. More generally, the increased mobility of public service officers between agencies has seen an erosion of the development of subject matter experts within Defence. This has been further exacerbated by the accelerated promotion of individuals in recent years as a by-product of the rapid growth in civilian numbers. Similar to the military posting cycle, rapid changes from job to job prevent the accumulation of skills and expertise in civilian staff.

The result is that a good number of key senior and middle ranking jobs are held either on a transitory basis by military personnel without the qualifications (nor sometimes even the inclination) for the task, or by civilians who are equally ill qualified.

If Defence is to perform as a world class organisation in these areas it needs to employ individuals of the calibre employed in major corporations.

The problem is further exacerbated on the military side by the deliberate policy of churning through senior officers at the star rank level. As a rule, a star-ranked officer can expect only one or two postings before promotion or retirement. In contrast, civilian Senior Executive Officers have the

opportunity to grow and develop their skills over time. While the frequent turn-over of senior military officers has the happy by-product of maximising the number of officers below them who can look forward to promotion, it effectively prohibits the accumulation of expertise at senior levels. The argument that rapid promotion and short tenures for senior military officers is necessary to ensure retention at lower levels is completely at odds with experience in the private and broader public sectors.

The solution to this problem is three-fold:

1. Use the flexibility already built into the *Public Service Act* to recruit professionals into key leadership positions in areas including, but not limited to; financial and economic analysis, information technology, personnel management, investment analysis and logistics planning. In practice, this will mean meeting market rates of remuneration. If Defence is to perform as a world class organisation in these areas it needs to employ individuals of the calibre employed in major corporations. Once in place, these individuals need to be given the flexibility to trickle-down professional appointments within their areas.

2. Increase the tenure of military personnel in senior positions. The extended tenure recently accorded to the Chief of Capability Development shows that this is possible. Where an appointment requires military experience, make sure that the individual has the other requisite professional qualifications and experience to do the job.

3. More actively develop the skills and expertise of civilian staff in specific areas pertinent to Defence. While a senior military officer can look forward to two or three years of dedicated training and education within their career (excluding the initial three to four year tertiary qualification often also provided at taxpayer expense), dedicated further education for civilian personnel is very much an exception rather than a rule.

Performance management

Consistent with the professionalisation of the workforce, Defence should employ private sector style rewards and sanctions to manage performance. This means a move away from the old public service style of a 'job for life' towards a model where remuneration and continued employment is contingent on performance. Defence, like much of the Australian Public Service, lumbers on with a system that makes it overly burdensome to terminate the employment of underperforming individuals.

If Defence wants to move its performance beyond that of a staid bureaucracy it will need to manage its people accordingly.

The 1999 rewrite of the *Public Service Act* gave agency heads considerable latitude to move towards more flexible employment practices, and the DMO has taken some tentative steps in this direction. Nonetheless, as a whole, Defence civilian employment is locked into an anachronistic model whose time is long past. If Defence wants to move its performance beyond that of a staid bureaucracy it will need to manage its people accordingly.

This is not to ignore or understate the practical difficulties such a move involves. A crucial role of the public service is to provide independent advice, and there can be a considerable tension between ensuring independence and a managerial approach

that rewards and sanctions individual performance. Moreover, if individual officers are asked to bear greater risk, then they will naturally expect greater reward. These are real and difficult issues, but it should be possible to strike a better balance than is struck today.

Information systems

The long and sorry history of Defence's faltering attempts to put in place effective management information systems needs to be seen against the intrinsic difficulty of the task. Nonetheless, it is of little surprise that the results have been so poor given that the projects have often been conceived and run by individuals with little or no project management or IT experience.

Unfortunately, it is in the area of information technology that the tendency to try and make-do with underqualified personnel has been most acute. If Defence is to have any chance of developing and implementing the complex management information systems it aspires to have, it needs to employ a Chief Information Officer of world class calibre and with the scope to create an appropriately staffed organisation for the job.

Financial management

Much has been made of the heroic efforts to satisfy the auditors that Defence has its balance sheet in order, and it is to Defence's great credit that they have been able to improve their accounting of assets over the last several years. It is a big and difficult task.

Regrettably, it's unclear that much of real substance has been delivered for the very substantial effort and cost incurred in doing so. The valuation of assets is simply not that important—especially since the strategic value of many military assets is unrelated to their market or replacement value. Nonetheless, the *tracking* of assets is important and to the extent that the trials and tribulations with the auditors have caused improvements in this area it will have been worthwhile.

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However, the key problem facing Defence financial management has nothing to do with the entrails of the balance sheet. It is, instead, the optimal allocation of resources towards results. Here, it must be said, good progress has also been made over the last five years. In 2001 Defence's internal financial management was in crisis as the confluence of accrual accounting and organisational reform coupled with poorly conceived and inadequately implemented management information systems hit home. Since then, the annual budget has been put on a firm basis and the estimation of operational funding supplementation has become a refined art.

Yet further improvement is possible and necessary. Key problems include:

- The inability to understand the cost-drivers of existing capability and project 'what-if' estimates of changed rates of effort.
- The lack of credible estimates of the future operating costs of new capabilities, or at least the lack of their input into forward financial planning.

In part, further improvement depends on the ongoing development of appropriate and effective Management Information Systems (MIS). More important still is the development of business analysis capabilities within the Chief Financial Officer group and across the organisation including especially the

Services. No MIS solution can substitute for experienced and trained personnel dedicated to understanding and modelling the cost and benefits of capability. As in other technical areas of Defence, this is not a job for junior staff officers or recent graduates but rather for trained professionals of the highest calibre.

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Efficiency

The Review's terms of reference mention efficiency. This is an encouraging sign because it's been almost a decade since the government last looked seriously at the value for money aspect of the almost 2% of GDP invested in Defence each year.

It is important to recognise that, at some level, the distinction between efficiency and effectiveness is moot. Within a fixed budget, increased efficiency delivers more output and, therefore, greater effectiveness. Equally, greater effectiveness frees resources that can then either be used to provide more defence output or redirected, for given defence output, to other purposes. Moreover, efficiency is not simply a matter of minimising administrative overheads, it is also about finding ways to increase operational effectiveness at fixed cost, or maintain operational effectiveness at reduced cost.

While there have been a series of internal efficiency and savings programs since 2000, these have done little more than constrain the growth of overheads. In fact, in many cases nominal savings have been redirected back to address growing administrative costs elsewhere in the portfolio. One clear exception is the harvesting of savings from a refinement to ADF command arrangements. On the whole, however, Defence has had six years of generous funding that has provided a limited incentive to find ways to deliver capability more cost effectively. Since 2000, the pattern has been one of asking for more and usually getting it.

Civilian staffing levels

One of the consequences of the recent period of generous funding has been a continuing high number of civilians in Defence. The 1996 *Defence Efficiency Review* (which preceded the DRP) estimated that, between 3,075 and 3,400 positions could be done away with and a further 5,903 positions should be 'market tested' for outsourcing. Thus, if the recommendations of the DRP had been taken up, the Defence civilian workforce would have fallen by somewhere between 3,075 and 9,303 depending on the results of market testing. Nonetheless, the budgeted civilian workforce for 2006–07 is 18,768 representing an overall fall of only six positions compared with the 1996–97 total of 18,774. Over the same period permanent ADF numbers fell from 57,028 to 51,253 (of which only around 1,500 reflect a failure to recruit and retain personnel).

While government initiatives in the intervening years (in the intelligence sector for example) account for some of the extra civilian positions, as does the recent 'civilianisation' of some military positions, it is difficult to explain why civilian numbers remain so high. This is specially the case given that the last decade has seen significant investment in IT by Defence that should have resulted in productivity gains that would have allowed staff numbers to fall.

The civilian workforce has also undergone significant 'level enrichment' over the last decade. For example, prior to the cuts due

to the DRP in 1996 there were 3,008 senior officers at the EL1/2 level in Defence. However, by 2006–07 the number has grown to 4,591, representing an increase of around 50%. Corresponding figures for military personnel are unavailable but over recent years the increase in numbers at the equivalent military ranks has been modest. (All figures include DMO personnel.)

The Review would do well to closely examine the number and level of civilians in Defence and try to understand why current levels far exceed those judged as necessary by the *Defence Efficiency Review* a decade ago.

The sprawling (and still expanding) bureaucracy that inhabits the crowded complex of offices on Russell Hill is a concern independent of the cost.

The growth in civilian numbers in the last decade is not simply a matter of efficiency but also one of effectiveness. The sprawling (and still expanding) bureaucracy that inhabits the crowded complex of offices on Russell Hill is a concern independent of the cost. More is not better when it comes to bureaucracy. The simple arithmetic of networks shows that the number of internal lines of communication increases dramatically with the number of nodes (~ n^2 for large n). As a result, large bureaucracies can easily become ineffective due to large amounts of time spent on internal communication.

Teeth-to-tail ratio

The key determinant of efficiency in the ADF is the demarcation between full-time and reserve uniformed personnel, civilians and private sector support. Over the past decade good progress has been made in a number of areas:

- The DRP outsourced a range of tasks previously undertaken by military personnel including many equipment maintenance and base support activities
- Legislative changes have enhanced the government's ability to use the Reserve and closer integration with the permanent force is under way
- A number of non-deployable ADF positions have been replaced by civilians
- A rationalisation of ADF command and control arrangements delivered a saving of around 240 personnel.

While these specific steps are encouraging, it is unclear whether the ADF as a whole is delivering as much capability as it could with the personnel it has. It has been a decade since the structure of the ADF was last put under external scrutiny (by the *Defence Efficiency Review*). And official reporting by Defence, though voluminous, carefully avoids disclosing the number of uniformed personnel in training, administrative and non-combat support roles. There is no way of knowing how many uniformed personnel are employed as bureaucrats, cooks, musicians, clerks, bar stewards, waiters and personal staff to senior officers.

Opacity extends to even the most basic measure of efficiency…

Opacity extends to even the most basic measure of efficiency; the ratio of combat to non-combat personnel in the ADF. The 2001 *Defence Annual Report* claimed that the DRP had allowed 7,400 additional combat force positions to be created in the ADF resulting in an increase in the teeth-to-tail ratio from 42% to over 60% of the permanent force.

Or to put it another way, around 1,850 new combat positions were created in each of the four years following the DRP.

This claim is very difficult to credit. The number of ships and aircraft in the ADF only changed marginally over that period. And while an additional two full-time battalions and a 500 strong deployable Air Force component were added to the force in 1999–00, these were both funded separate from the redirection of DRP savings. Curiously, notwithstanding a number of subsequent initiatives to create new capabilities in the ADF, the most recent quoted official figure from mid-2006 puts the combat proportion at 62%—exactly where it was in late 2001!

The sad reality is that there is no credible measure available to the public of whether the Defence organisation is using its people—military and civilian—cost-effectively. Both areas bear close examination. In the case of the ADF, the obvious avenue would be to use the aforementioned *Force Structure and Sustainability Review* to examine the efficiency of the ADF including especially the demarcation between full-time, reserve, civilian and contractor personnel.

Defence efficiency is not something that can be achieved through a one-off action.

Improving efficiency

Defence efficiency is not something that can be achieved through a one-off action. Instead, it needs to be an ongoing process that not only exploits new technology and business processes, but periodically applies liposuction to the inevitable fat that accumulates in an organisation isolated from market pressures.

As already argued, in the long-term, responsibility for the cost-effective delivery of capability should be devolved to the Service Chiefs, and with it the responsibility for improving efficiency. But that transfer of responsibility has not yet occurred, and even after it does the Secretary will continue to bear ultimate responsibility under the *Financial Management and Accountability Act 1997* (FMA Act) for ensuring that taxpayer dollars are spent efficiently within the Department of Defence. To better discharge this responsibility, the Secretary needs high quality advice and analysis focused directly on increasing the productivity of the Defence workforce and improving the efficient delivery of capability.

This task must be independent of the Services albeit undertaken with expert military input. It should focus both on securing better measures of output, at all levels of the Defence organisation, and of the costs necessarily involved in securing that output. It should provide the Secretary with the ability to independently examine trade-offs and advise government on those trade-offs.

Progress in this respect is not only essential to improving government decision-making with respect to Defence; it is also crucial to successful devolution to the Services of greater direct control over the inputs they need to provide capabilities. Without a clearer framework for determining the desired levels of those capabilities, and for assessing the efficiency with they are being delivered, any such devolution would be perilous. In short, what is needed is to strengthen Defence's ability, at a policy level, to define (and where useful, measure) its outputs and understand the costs and trade-offs associated with producing those outputs.

Arguably the best way to achieve this would be to create a position of Chief Defence Economist reporting directly to the

Secretary. Assisted by a small professional staff, the Chief Defence Economist would be responsible for developing:

- indicators of Defence outputs, and defining the quantitative and qualitative indicators relevant to monitoring those outputs
- methods that can be used to understand the costs of those outputs
- a database of historical financial, personnel and performance data that can support the implementation of those methods and that advance understanding of Defence's delivery of those outputs.

Additionally, the position would be responsible for monitoring and benchmarking:

- the cost of acquiring and maintaining military capabilities
- the cost of services purchased by Defence under contract
- personnel costs and productivity
- administrative overheads.

On the basis of this work, the Chief Defence Economist would advise the Secretary on how to improve the efficiency of Defence.

The largest single problem is a failure to align planning and budgeting.

Summary of recommendations

Despite recent improvements Defence management remains imperfect.

The largest single problem is a failure to align planning and budgeting. The only way to improve Defence planning and budgeting is to force Defence to live with the results of those processes. Accordingly, a *Force Structure and Sustainability Review* should be undertaken to deliver a costed long-term plan for the Australian Defence Force (ADF), and Defence should be required to deliver the resulting plan within a pre-determined budget.

Other initiatives to improve the effective management of Defence are:

1. Streamline administration and enhance accountability by reducing the number of committees and re-establishing those that remain as 'advisory forums' for individual decision makers. Wherever practical delegate responsibility to an individual.
2. Create a new civilian position of Under Secretary reporting directly to the Secretary and Chief of the Defence Force responsible for:
   - running the Australian Defence Headquarters
   - coordinating Defence's committees/ advisory forums and decision making
   - overseeing the day-to-day administration of Defence.
3. Reintroduce contestability within Defence through an expanded and independent secretariat function to provide critical analysis of proposals brought forward to all committees/advisory forums.
4. As a long-term goal, make the Service Chiefs responsible for the cost-effective delivery of military capability and able to make the decisions inherent in exercising that responsibility. Like any other managers, they should be personally accountable through incentives and sanctions for the results they achieve.
5. Revamp Defence's approach to personnel management by:
   - recruiting professionals from the private sector into key positions in areas like financial management, information technology, personnel management, investment analysis etc

- making remuneration and continued employment contingent on performance
- increasing the tenure of military personnel at senior levels and in senior positions
- more actively developing the skills and expertise of civilian staff.

6. Develop a cadre of business analysis professionals to properly understand the cost and performance of military capability.

It has been a decade since Defence was subject to a comprehensive review of its efficiency. To ensure that taxpayers receive value-for-money:

1. The aforementioned *Force Structure and Sustainability Review* should include a comprehensive examination of the efficiency with which Defence delivers military capability including the demarcation between full-time, reserve, civilian and contractor personnel.
2. The recent growth in numbers and rank enrichment among civilians in Defence should be examined closely and the numbers cut to the level consistent with effective administration.
3. A Chief Defence Economist should be appointed to advise the Secretary on ongoing improvements to efficiency, effectiveness and productivity within Defence.

About the Author

Prior to joining ASPI, **Mark Thomson** held a number of positions in Defence working in the areas of capability development and resource management. In 1999 he was Political Military Adviser to Major General Peter Cosgrove during the INTERFET operation. Prior to his time with Defence, Mark held a series of academic research and teaching positions in theoretical physics.

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