

The Auditor-General
Audit Report No.11 2009–10
Performance Audit

Garrison Support Services

Department of Defence

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of Australia 2009

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Canberra ACT
17 November 2009

Dear Mr President
Dear Mr Speaker

The Australian National Audit Office has undertaken a performance audit in the Department of Defence in accordance with the authority contained in the *Auditor-General Act 1997*. I present the report of this audit and the accompanying brochure. The report is titled *Garrison Support Services*.

Following its tabling in Parliament, the report will be placed on the Australian National Audit Office's Homepage—<http://www.anao.gov.au>.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Ian McPhee', is positioned above the printed name of the Auditor-General.

Ian McPhee
Auditor-General

The Honourable the President of the Senate
The Honourable the Speaker of the House of Representatives
Parliament House
Canberra ACT

AUDITING FOR AUSTRALIA

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Contents

| | |
|--------------------------------------------------------------------------------------|-----------|
| Abbreviations..... | 8 |
| Summary and Recommendations | 11 |
| Summary | 13 |
| Introduction | 13 |
| Audit objective and scope | 15 |
| Overall conclusion..... | 16 |
| Key findings by Chapter | 18 |
| Defence's response | 24 |
| Recommendations | 25 |
| Audit Findings and Conclusions | 29 |
| 1. Introduction | 31 |
| Background | 31 |
| Defence's Garrison Support Services management arrangements and resourcing | 35 |
| Audit approach | 39 |
| Report structure | 40 |
| 2. GSS Procurement – 2008 North Queensland Base Services tender | 41 |
| Introduction | 41 |
| Approach taken with the Request for Tender for North Queensland..... | 43 |
| Tender evaluation | 51 |
| Advice to tenderers of evaluation outcome..... | 57 |
| Contract negotiation | 59 |
| 3. Contract management framework..... | 62 |
| Introduction | 62 |
| Regional Contract Governance Plans..... | 62 |
| Risk management | 64 |
| Communication and relationships | 67 |
| Training and guidance..... | 75 |
| Centralising the availability of communication, training and guidance material | 77 |
| 4. Contract performance management and measurement..... | 79 |
| Introduction | 79 |
| Contractual provisions for monitoring progress and assessing performance..... | 80 |
| Application of the GSS performance management framework | 81 |
| 5. Administration of GSS payments and contract amendments | 102 |
| Introduction | 102 |
| Expenditure related to GSS | 102 |
| GSS Budget Management Review | 105 |
| Contract amendments..... | 106 |

| | |
|----------------------------------------------------|-----|
| Payment arrangements..... | 114 |
| Savings related to GSS contracting | 119 |
| 6. The GSS Procurement and Contracting Model | 123 |
| Introduction | 123 |
| Issues identified by the audit..... | 123 |
| Options for changing the base support model | 125 |

Appendices 131

| | |
|---------------------------------------------------------------------------------------------------|-----|
| Appendix 1: Defence comments..... | 133 |
| Appendix 2: First round of GSS contracts: announced dates and actual savings..... | 137 |
| Appendix 3: Second round of Garrison Support Services contracts and Base Services contracts | 138 |
| Appendix 4: Efficiency dividends and other savings initiatives | 139 |
| Appendix 5: Tools and systems related to Performance Management Framework..... | 140 |
| Appendix 6: Definition of service type categories..... | 142 |
| Series Titles..... | 143 |
| Current Better Practice Guides | 144 |

Tables

| | |
|------------------------------------------------------------------------------------------------------------------------------------|-----|
| Table S 1 Categories of Garrison Support Services..... | 13 |
| Table 1.1 Categories of Garrison Support Services..... | 31 |
| Table 1.2 Changes to DSG regional structure | 36 |
| Table 3.1 GSS communication between DSG, contractors and service recipients | 68 |
| Table 4.1 Assessment tiers for ongoing performance in GSS contracts..... | 83 |
| Table 4.2 An illustrative example of the Performance and Risk Reward Remuneration Model linkages for Access Control Services | 86 |
| Table 5.1 Payments made by service type – 1 March 2008 to 28 February 2009 | 103 |
| Table 5.2 Timeliness of the contract amendment process..... | 111 |
| Table A 1 Defence's full comments in relation to the ANAO's recommendations | 133 |
| Table A 2 First round of GSS contracts | 137 |
| Table A 3 Second round of GSS contracts (let under ITRI arrangements) | 138 |
| Table A 4 Base Services contracts (let under open tender arrangements)..... | 138 |

Figures

| | |
|----------------------------------------------------------------------------------------------|----|
| Figure 1.1 GSS expenditure (\$ million), 2001–02 to 2008–09 | 38 |
| Figure 2.1 Criteria applied in the evaluation of tenders for NQ Base Services contract | 44 |
| Figure 4.1 Operation of the Defence GSS Performance Management Framework..... | 82 |

Figure 4.2 Percentage of relevant performance indicators across all regions
for which CAPMAN source data is considered adequate—May
2008 to May 2009 92

Figure 4.3 Average access control performance ratings over the period
January 2008 to January 2009 94

Figure 4.4 Average stores management performance ratings over the
period January 2008 to January 2009 94

Figure 4.5 GSS CAPMAN Performance Indicator scoring frequency—July
to December 2008 97

Figure 4.6 GSS CAPMAN Compliance Indicator scoring frequency—July to
December 2008 98

Figure 5.1 Key stages in the GSS contract amendment process..... 107

Abbreviations

| | |
|--------|-------------------------------------|
| ADF | Australian Defence Force |
| APS | Australian Public Service |
| AQT | Agreed Quality Target |
| BAM | Base Accountabilities Model |
| BSM | Base Support Manager |
| CAO | Contract Amendment Order |
| CAP | Contract Amendment Proposal |
| CAPMAN | Contract and Performance Management |
| CAR | Contract Amendment Request |
| CDF | Chief of the Defence Force |
| CEO | Chief Executive Officer |
| CI | Compliance Indicator |
| CMS | Comprehensive Maintenance Services |
| CMT | Collaborative Management Team |
| CNNSW | Central Northern New South Wales |
| COO | Chief Operating Officer |
| CRB | Contract Review Board |
| CSA | Customer Supplier Agreement |
| CSB | Collaborative Strategy Board |
| CSP | Commercial Support Program |

| | |
|---------|---------------------------------------------------------|
| DEMS | Defence Estate Management System |
| DMO | Defence Materiel Organisation |
| DPPM | Defence Procurement Policy Manual |
| DS-NQ | Defence Support – North Queensland |
| DSG | Defence Support Group |
| DSO | Defence Support Operations |
| E2 | Economy and Efficiency |
| FMA Act | <i>Financial Management and Accountability Act 1997</i> |
| GDP | Gross Domestic Product |
| GEWM | General Estate and Works Management |
| GFE | Government Furnished Equipment |
| GSO | Garrison Support Officer |
| GSS | Garrison Support Services |
| GST | Goods and Services Tax |
| IDCR | Interim Defence Contract Register |
| ITRI | Invitation To Register Interest |
| KPI | Key Performance Indicator |
| MAB | Management Audit Branch |
| Max QT | Maximum Quality Target |
| Min QT | Minimum Quality Target |
| MRU | Members Required in Uniform |

| | |
|-------|-----------------------------------------------|
| NQ | North Queensland |
| DPC | Directorate of Procurement and Contracting |
| PCM | Professionalising Contract Management course |
| PI | Performance Indicator |
| PMF | Performance Management Framework |
| PVF | Price Variation Formula |
| RCGP | Regional Contract Governance Plan |
| RFT | Request For Tender |
| RMV | Riverina Murray Valley |
| ROMAN | Resource Output Management Accounting Network |
| RRRM | Risk Reward Remuneration Model |
| SME | Small and Medium Enterprise |
| SOW | Statement of Work |
| SRP | Strategic Reform Program |
| SSDS | Serco Sodexo Defence Services Pty Ltd |
| TDR | Tender Deliverable Requirement |
| TEP | Tender Evaluation Plan |
| TET | Tender Evaluation Team |
| TEWG | Tender Evaluation Working Group |
| WA | Western Australia |

Summary and Recommendations

Summary

Introduction

1. Garrison Support Services (GSS) describes a range of services provided by contractors to Defence sites around Australia. In 2008–09, total annual expenditure under Defence’s GSS contracts was \$454.77 million. This represented an increase of 58 per cent over expenditure on GSS in 2001–02. The majority of this increase relates to the impact of price indexation arrangements over time, although there have also been increases in the scope of services delivered under GSS contracts and some of the increase in GSS expenditure can be attributed to the higher Defence tempo of operations in recent times.¹ The following categories of GSS generally generate the highest contract payments (in order): hospitality and catering; access control; cleaning; grounds maintenance; fire fighting and rescue; and transport. Table S 1 lists all of the categories of services that may be provided under GSS contracts.

Table S 1
Categories of Garrison Support Services

| | | |
|-------------------------------------------------------|------------------------------|---------------------------------------------------------------------------|
| access control | fire fighting and rescue | range and training area management |
| accommodation management | grounds maintenance | reprographics and printing services |
| airfield and runway maintenance | hospitality and catering | sports and recreation services (e.g. gym operation, sport field markings) |
| cafeteria services | laundry and dry cleaning | transport services |
| cleaning | management of Defence stores | waste management |
| ensuring availability of petrols, oils and lubricants | pest and vermin control | workshop services |

Note: The majority of these services are delivered in all Defence regions, although not all services are delivered in each region.

Source: GSS contracts

¹ For an explanation of the significant scope changes see paragraph 5.61.

2. GSS contracts have been in operation for some 10 years and there are currently 10 GSS contracts which are regionally based. In 2008, Defence moved to a revised model for the procurement of GSS. This model involves contracts for the provision of what are called 'Base Services' where contractors provide both GSS and Comprehensive Maintenance Services (CMS).² Tenders for the two Base Services contracts so far in place, for the former Tasmanian and North Queensland regions, were conducted in 2008 with the contracts commencing in December 2008 and January 2009 respectively.³

3. Overall responsibility for the procurement and contract management of GSS (or Base Services) lies with the Defence Support Group (DSG), which has regional staff throughout Australia. Each DSG regional manager (the Contract Authority for the regional contract) reports to the Head of Defence Support Operations (DSO). The Business Services Procurement and Contracting Branch within DSG has a key role related to GSS as it is the 'process owner and technical authority' for procurement, contracting and commercial advice, and develops DSG policies and processes in these areas.

4. Currently, Defence is undertaking management reforms that affect GSS. One of these involved the implementation of a restructure of the DSG regions. Until 1 July 2009, the DSG regional structure was made up of 12 regions and the 10 GSS and 2 Base Services contracts currently in place relate to that structure, that is one contract per region.⁴ However, from 1 July 2009, the number of DSG regions has been reduced to five.⁵

5. In addition, DSG is introducing a 'contracting hub model' which involves establishing a 'hub'—essentially a high level management team—for each contractor involved in delivering GSS, CMS and/or Base Services contracts. Defence's aims in adopting this model include improving

² CMS involves, amongst other things, the maintenance and repair of Defence fixed plant and equipment, and provision of engineering and other specialist advice. For the second round of GSS contracts, which were let on a rolling basis from 2004, the rules of the tender allowed tenderers to submit a combined GSS/CMS bid, however a combined bid was only successful in the case of the South Queensland region.

³ Defence restructured its regional structure for the delivery of GSS in July 2009 (see paragraph 4).

⁴ The twelve DSG regions at the time of audit fieldwork were: Sydney Central, Sydney South West, Central Northern New South Wales, Australian Capital Territory and Southern New South Wales, Riverina Murray Valley, Victoria, Tasmania, North Queensland, South Queensland, Northern Territory and Kimberley, South Australia and Western Australia.

⁵ The five current DSG regions are North New South Wales, South New South Wales, Victoria and Tasmania, Queensland, and Central and West.

stakeholder management and risk management, and reducing the resources needed for contract management. Another reform is called the Base Accountabilities Model (BAM), which aims to resolve problems of blurred accountability and responsibility between DSG and the recipients of services, principally the Australian Defence Force (ADF). Implementation of both the BAM and the 'contractor hub model' is currently underway and is expected to be substantially completed by the end of 2009.

6. In June 2009, in the context of the Defence White Paper 2009 and the 2009–10 Federal Budget, Defence announced its Strategic Reform Program (SRP). The SRP aims to deliver over the 10 years to 2019 gross savings of around \$20 billion that are required to fund the achievement of the Government's plan to build a stronger ADF (known as Force 2030) and:

to fix key areas in Defence where under-investment in past years has left vulnerabilities in [Australia's] military capabilities and reduced critical support functions to the ADF. [the \$20 billion] will be reinvested to deliver stronger military capabilities, to remediate areas where there has not been enough funding in the past and to modernise the Defence enterprise 'backbone', all of which are essential to support the fighting force.⁶

7. As part of the SRP, the reform target savings associated with GSS has been set at \$700 million over 10 years.

Audit objective and scope

8. The objective of the audit was to assess the effectiveness of Defence's procurement and contract management for the provision of Garrison Support Services.

9. Defence's approach to the provision of GSS through outsourced providers has developed over some 10 years that these contracts have been used. The audit reviewed the conduct of one of the most recent GSS procurements undertaken by Defence, the tender for the Base Services contract for the former North Queensland region.⁷ In addition, the audit examined DSG's management of the existing GSS contracts relating to three of the 12 regions making up DSG's regional structure at the time of audit fieldwork: the

⁶ *The Strategic Reform Program, DELIVERING FORCE 2030*, Department of Defence, June 2009, Introduction by the then Secretary and the Chief of the Defence Force on p. 3.

⁷ Base Services contracts involve the combined delivery of both GSS and CMS.

former Riverina Murray Valley (RMV) region, the former Central/Northern New South Wales (CNNSW) region and the former Western Australia (WA) region.⁸ The audit did not examine the policy related to the level of security or access control at Defence establishments (or who should provide such services) which informs the requirements specified in GSS contracts.⁹

Audit criteria

10. The audit considered, in respect of the provision of GSS, whether:

- arrangements comply with Commonwealth legislative and policy guidance, as well as relevant Defence guidance;
- risks have been identified and managed;
- the roles and responsibilities of different parties within Defence have been identified;
- appropriate plans have been developed for tendering and contract management; and
- better practice has been applied as appropriate to procurement and contract management arrangements.

Overall conclusion

11. Defence contracts out the provision of Garrison Support Services (GSS) to allow the ADF to focus on its core functions. GSS encompass a range of services such as catering, access control and grounds maintenance.¹⁰ The ANAO examined the recent tender selection process conducted for the Base Services contract (which encompasses GSS) for the North Queensland region, and also contract management arrangements for three existing GSS regional contracts.¹¹

⁸ Fieldwork for the audit was conducted between February and April 2009. As noted in paragraph 4, DSG introduced a new regional structure on 1 July 2009 under which the twelve previous regions have been reduced to five. See Table 1.2 in Chapter 1 for details of the new DSG regional structure.

⁹ The access control service provided under GSS and Base Services contracts is one of the layers of security in place at Defence bases throughout Australia. For example, specific measures are taken to protect sensitive items of equipment and munitions, as well as buildings in which particularly sensitive work is undertaken.

¹⁰ See Table S 1 for a full listing of the categories of GSS that may be provided to Defence establishments under current GSS and Base Services contracts.

¹¹ As noted in paragraph 9, the ANAO examined the administration of the GSS contracts in the former RMV, CNNSW and WA regions.

12. Overall, the ANAO considers that Defence's current tender selection processes and contracting arrangements are delivering the necessary services. However, the effectiveness of GSS contracting is constrained by weaknesses in risk management, performance management and contract amendment administration for current GSS contracts. Inconsistencies in Defence's application of the performance management framework for GSS, both across and within regions, raise issues of the equitable treatment of contractors, and whether the level of performance payments made by Defence has been adequately substantiated.¹² Defence has recognised the need for reform of GSS/Base Services and has already commenced the implementation of a range of reforms.¹³ However, in the context of the challenging savings target for GSS under the SRP (\$700 million over the next 10 years), successful completion of reforms already in train and identification and implementation of further improvements will be essential.

13. In the longer term, to achieve efficiencies, reduce costs and improve competition, the ANAO considers that there are a range of initiatives that Defence could usefully consider to improve the procurement approach and contracting model being used, including:

- encouraging investment by contractors in longer term improvements in the provision of services that would lead to efficiencies through longer base terms for GSS/Base Services contracts (for example increasing the current five year base term to 10 years), subject to ensuring performance standards are met;
- encouraging innovation by contractors and promoting competition through improved tender and contract arrangements involving greater reliance on the specification of outcome standards to be met rather than focussing on specific processes to be carried out;¹⁴

¹² This is because analysis of performance scores awarded for contractor performance at or above 'agreed' performance targets for the three regions in the ANAO's audit sample identified markedly different scores being given for what appeared to be the same, or very similar, levels of performance. Contractors receive differing margin payments depending on the performance score received. Ratings between 80 and 90 per cent usually provide margin payment at the 'agreed quality target' level and ratings at 90 per cent and above usually attract a margin payment at the 'maximum quality target' level. Table 4.2 provides an illustrative example of how the GSS Performance and Risk Reward Remuneration Model might impact on contractor revenue.

¹³ These include a reduction in the DSG regional structure from 12 regions to five, steps to introduce a 'contracting hub model' and the new Base Accountabilities Model (BAM) by the end of 2009 (see paragraphs 4 and 5, Chapter 1 (paragraphs 1.16 to 1.20) and Chapter 3 (paragraphs 3.35 to 3.38)).

¹⁴ And/or requiring detailed information about how individual services are to be delivered.

- reducing the administrative burden on both Defence and contractors by simplifying the performance management arrangements, and improving contract arrangements for managing underperformance of contractors; and
- developing a mechanism to increase the knowledge of Defence users of GSS/Base Services about the services contractors are required to deliver to allow users to play a more explicit role in providing assurance that contracted services are delivered.

14. To help meet the challenge presented by the SRP savings target for GSS, Defence will need to streamline its contract management effort through improved procurement and performance management approaches that promote competition and foster innovation by contractors to provide service delivery solutions that deliver the required outcomes to Defence users, while also reducing costs to both Defence and contractors.

Key findings by Chapter

GSS Procurement – 2008 North Queensland Base Services tender (Chapter 2)

15. Defence undertook an open tender for Base Services (which included GSS) for the former North Queensland region during 2008. The contract was for an approved amount of \$197.9 million over five years and there were three tenderers for the contract (all of whom have existing GSS contracts in other regions). The successful tenderer was Serco Sodexo Defence Services Pty Ltd (SSDS).

16. Based on its Tender Evaluation Plan and Probity Plan, Defence established a comprehensive process for the tender selection process for North Queensland Base Services (NQ Base Services). From the material reviewed, there is evidence that matters such as fairness, impartiality, transparency, security, conflicts of interest and the negotiation of the contract were managed appropriately.

17. The Request For Tender (RFT) required tenderers to provide detailed information on how they would deliver particular services. The technical assessment evaluation of tenders contains an undue emphasis on a tenderer's ability to provide detailed information on how it proposes to deliver services, rather than concentrating on the tenderer's ability to effectively manage and deliver services. If a tenderer did not address how it proposed to carry out

relatively minor tasks, its assessment score was reduced. This approach adds to the cost of the overall tender process, can serve as a deterrent to new entrants to Base Services contracting, and provides an advantage to an incumbent firm (which can readily describe the services it is already delivering). The balance of the evaluation could be improved through focusing more on the ability of the tenderer to deliver services to a set standard; the tenderer's internal performance management and quality assurance systems; and the tenderer's ability to attract personnel with the necessary skills and experience.

18. The ANAO considers that Defence should evaluate whether the current design of the tender selection process for Base Services best supports an open, competitive tender process over the longer term. Defence informed the ANAO that it considers that any tender evaluation process must include a balanced consideration of all technical worth, price and risk aspects in order to make 'value for money' assessment decisions. However, Defence indicated that it is continually seeking to improve the procurement process and, as such, agrees that the tender evaluation approach can be reviewed with the aim of improving the efficiency and effectiveness for Defence and tenderers, whilst still ensuring that an appropriate 'balance' is achieved and that all tenderers are treated in a fair and equitable manner.

19. The ANAO also proposes that Defence improve the written debriefs provided to tenderers subsequent to tender assessments by providing tenderers with an assessment against each of the evaluation criteria, noting the strengths and weaknesses of the tender of the particular organisation.

Contract management framework (Chapter 3)

20. At the time of audit fieldwork, the DSG regional structure was made up of 12 regions.¹⁵ The 10 GSS and two Base Services contracts currently in place relate to that structure, that is one contract per region. The ANAO examined the management and administration of three of these GSS contracts—the contracts for the former Riverina Murray Valley (RMV) region, the former Central/Northern New South Wales (CNNSW) region and the former Western Australia (WA) region. These contracts are delivered by three different firms,

¹⁵ Fieldwork for the audit was conducted between February and April 2009. As noted in paragraph 4, DSG introduced a new regional structure on 1 July 2009 in which the twelve previous regions have been reduced to five. See paragraph 1.16 and Table 1.2 for details of the new DSG regional structure.

involve services being delivered to all three Services and include broad geographic coverage.

21. Under the GSS contractual arrangements there is a requirement for a Regional Contract Governance Plan (RCGP) for each contract. These plans, in large part, outline the processes that are to be followed as part of contract management and related administration, including how performance measurement will be dealt with in the particular region. Given the contractual arrangements in place and the substantial funding involved, it is important that Defence has recorded assessments of the key risks associated with its GSS contract management functions, and how it proposes to manage them. None of the three DSG regions in the ANAO's audit sample had documented risk assessments of DSG's responsibilities in connection with the region's contract for GSS.¹⁶ Structural reforms currently underway within DSG intend to develop GSS risk management at a national level. In the light of any risk assessments undertaken for contract management, there are likely to be changes needed to be made to RCGPs to take account of the outcome of the assessments.

22. In the three regions visited by the ANAO, DSG's communication arrangements with its GSS contractors and the ADF users of GSS appear generally effective. They cover all relevant parties and provide a framework to allow issues to be appropriately escalated. Most forums were being consistently utilised, and overall those interviewed were satisfied with the arrangements.

23. DSG staff in the regions visited informed the ANAO that they were generally able to access suitable training on procurement and systems such as CAPMAN.¹⁷ With the current process to introduce the 'Professionalising Contract Management' (PCM) course, the need for contract management training is now being addressed. However, the PCM course could be improved by the inclusion of specific guidance on the application of risk management to GSS. Although not specifically tailored to the detail of the GSS contracts, the training conducted in the former RMV region which focused on managing the relationships in contracts, including managing conflict during negotiation,

¹⁶ Such risk assessments should be reflected in each region's Regional Contract Governance Plans (RCGPs).

¹⁷ CAPMAN is Defence's Contract and Performance Management system for GSS.

appears to have contributed to the development of an effective collaborative relationship between DSG and contractor personnel in that region.

24. However, currently DSG does not have a central, easily accessed repository of training and guidance material for either its own staff or contractor staff involved in the management of GSS, CMS and Base Services. In order to improve access for base and regional personnel, including contractor personnel, to up to date training and guidance material and to provide a convenient mechanism for regular, timely communication with these personnel, the ANAO has recommended that Defence assess the benefits of establishing a central information source (possibly an intranet site) for GSS and CMS related communication, training and guidance material.¹⁸ Such a site would help contribute to a consistent national approach, allow for ease of communication, provide an authoritative up-to-date reference source and reduce the demand for local solutions.

Contract performance management and measurement (Chapter 4)

25. The framework for GSS performance management is based on the contractor meeting several performance and compliance indicators for each service. Performance measurement is based on a self-assessed score by the contractor, which is reviewed by DSG. Compliance indicators are based on objective criteria and are assessed as met or not met. DSG and contractor staff interviewed by the ANAO considered the assessment of performance against these compliance criteria as relatively straight forward. However, in contrast, performance indicators are subjective assessments of contractor performance in service delivery, and are scored out of 100.

26. ANAO analysed the performance scores allocated to contractors in 10 regions throughout Australia between July 2008 and December 2008. This analysis showed performance had predominately been assessed as having met or exceeded 'agreed' performance targets under the GSS performance management arrangements. This is consistent with the feedback provided by ADF representatives interviewed at the bases visited as part of the audit, who indicated that they were generally satisfied with the services provided by contractors under GSS.

¹⁸ Base Services contracts comprise both GSS and CMS.

27. However, there are difficulties in the scoring system differentiating between 'agreed' performance and 'maximum' performance, which are both shown as green traffic lights in the relevant reporting system, the Contract and Performance Management (CAPMAN) system. ANAO's analysis of performance scores awarded in this range for the three regions in the ANAO's audit sample identified markedly different scores being given for what appeared to be the same, or very similar, levels of performance based on the comments supporting the scores recorded in the CAPMAN system.

28. Under the GSS contracts, the scores for performance against the performance indicators for each service translate into different margin (or performance) payments. The ANAO identified inconsistencies in Defence's application of the performance management framework for GSS, across and within regions, that raise both issues of the equitable treatment of contractors and questions as to whether the level of performance payments made by Defence has been adequately substantiated. Contractors receive differing margin payments depending on the performance score received. Ratings between 80 and 90 per cent usually provide margin payment at the 'agreed quality target' level and ratings at 90 per cent and above usually attract a margin payment at the 'maximum quality target' level.¹⁹

29. In addition, GSS contractual provisions to recalibrate performance targets where maximum scores are consistently achieved have never been applied, even though in some regions, for particular performance indicators, the maximum margin payment has been made for an extended period. Without such a mechanism being applied, and in light of the inconsistencies around performance measurement, the contractual Performance and Risk Reward Remuneration Model is not able to ensure that ongoing performance across GSS contracts is consistently reflected in the margins paid to the various contractors.

30. Overall, the ANAO considers that the performance management and risk/reward elements of the GSS contracts are not operating consistently or effectively and recommends that they be reviewed.

¹⁹ For illustrative purposes, assuming a difference of 2 per cent in the margin between 'agreed' and 'maximum performance', and annual contract payments of \$30 million, the difference between the margin payment for 'agreed' and 'maximum' performance could be up to \$0.6 million per annum. Table 4.2 contains an illustration of the relationship between performance scores and margin payments.

Administration of GSS payments and contract amendments (Chapter 5)

31. Processing of payments to GSS contractors generally occurs in an effective manner. However, there is potential for considerable improvement in the administration of contract amendments by DSG. Records related to contract amendments were incomplete and the processing of amendments was not timely in the three regions comprising the ANAO's audit sample. Delays in processing amendments increase costs to Defence in some cases, as contractors charge higher labour rates for services not established in the contract.

32. Other matters identified in relation to GSS administration include:

- the need to emphasise to DSG regional staff the importance of pursuing any non-delivery of contracted services in a timely manner and, if appropriate, to seek adjustment to contractor payments;
- that in the view of both contractors and ADF members involved, it appears that the use of ADF personnel in contractor managed operations (such as messes) causes considerable dissatisfaction and tension, and there may be merit in re-examining this approach to maintaining relevant specialist skills for such ADF personnel; and
- in relation to the maintenance of savings over the life of GSS contracts (original contracts were entered into in 1998), Defence advised that, using analysis from a 2002 internal audit report as a baseline,²⁰ and adjusting for price changes and scope increases, real GSS expenditure has not varied significantly from that outlined in the internal audit report of 2002, which suggests that savings have been maintained over the life of the contracts.

The GSS Procurement and Contracting Model (Chapter 6)

33. The ANAO identified a number of options that Defence could consider regarding the future operation of GSS and Base Services procurement and

²⁰ Management Audit Branch, Report No: 01/008, *Contract Management of CSP Contracts – Garrison Support*, 7 February 2002.

contract management. The key options are set out in paragraph 13.²¹ While it is approximately four years until the term of any of the existing contracts under which GSS are provided is completed, it would be timely for Defence to commence planning for a new round of contracts now. This should allow for appropriate consideration of how best Defence can improve its approach to GSS and Base Services procurement and contract management to support achievement of the SRP savings target of \$700 million over the 10 years to 2019. In addition, there is scope for changes relating to the administration of existing contracts to set the scene for future arrangements, and make economies in current administrative practices.

Defence's response

34. Defence's response to the proposed audit report was as follows:

Defence acknowledges the findings noted in the ANAO Report in relation to the procurement and contract management of the Garrison Support Services Contracts. Defence agrees to each of the five recommendations made within the report.

Defence had already commenced a number of reform activities associated with the procurement and management of the Garrison Support Services contracts prior to and during the ANAO audit. Defence will continue to address the issues highlighted in the report, primarily through a number of reform activities currently underway as part of the Defence Strategic Reform Program and the Non-Equipment Procurement reviews.

Defence remains committed to pursuing ongoing continuous improvement in relation to the procurement and management of the Garrison Support Services Contracts.

35. Defence's full response to each of the ANAO's recommendations is contained in Appendix 1.

²¹ Other options raised in Chapter 6 include: placing greater explicit reliance on contractors' own quality assurance systems; reducing risk and administrative overhead through redesigning the contract arrangements to minimise the requirement for contract amendments and streamlining the administrative processes for necessary amendments; further exploring the opportunities for 'gain share' within contracts whereby contractors are provided with incentives to make efficiencies and/or economies with the benefits shared between Defence and the contractor; and, for discretionary services, considering whether there is scope for the user (principally the ADF) to deal directly with the contractor and apply its funds to meet the costs.

Recommendations

Recommendation No 1

Para 2.62

The ANAO recommends that Defence reviews its approach to providing debriefings to tenderers for future Base Services contracts with a view to providing:

- (a) tenderers with an assessment against each of the evaluation criteria, noting the strengths and weaknesses of the tender of the particular organisation; and
- (b) debriefs within 30 days of a contract being entered into.

Defence response: *Agreed.*

Recommendation No 2

Para 3.15

The ANAO recommends that Defence adopts a sound risk based approach to the management of GSS contracts and that the resulting risk assessment be used to assist in determining the appropriate processes for functions such as performance assessment, contract amendments and payment verification, and the level of resources best applied to those functions.

Defence response: *Agreed.*

**Recommendation
No 3**

Para 3.51

The ANAO recommends that Defence, in order to support effective GSS, CMS and Base Services related contract management and administration, assesses the benefits of establishing a central information source using an information technology solution (for example, an intranet site) to:

- (a) improve access for base and regional personnel, including relevant contractor personnel, to up to date training and guidance material; and
- (b) provide a convenient mechanism for regular, timely communication with these personnel.

Defence response: *Agreed.*

**Recommendation
No 4**

Para 4.45

The ANAO recommends that Defence reviews the Performance Management Framework and Risk Reward Remuneration Model relating to Garrison Support Services with a view to:

- (a) remedying inconsistencies in the way the different DSG regions approach performance measurement and the effect of this on both the margin outcome for individual contractors and the cost of GSS to Defence; and
- (b) better supporting the achievement of value for money as well as quality outcomes, through addressing weaknesses in the current Risk Reward Remuneration Model and its application by Defence in relation to maximum quality targets.

Defence response: *Agreed.*

**Recommendation
No 5****Para 5.36**

The ANAO recommends that Defence:

- (a) in consultation with GSS/Base Services contractors, takes steps to determine appropriate timeframe targets for both the contractor and Defence in relation to their respective responsibilities for contract amendments;
- (b) promulgates specific guidance on processing GSS contract amendments to relevant staff; and
- (c) introduces management and reporting mechanisms to promote adherence to this guidance and timeframe targets.

Defence response: *Agreed.*

Audit Findings and Conclusions

1. Introduction

This chapter outlines the development of Garrison Support Services contracting, its management structure and current reforms, and the audit approach.

Background

1.1 Garrison Support Services (GSS) describes a range of support services provided by contractors to Defence sites around Australia. Table 1.1 lists the services provided under GSS contracts.

Table 1.1

Categories of Garrison Support Services

| | | |
|-------------------------------------------------------|------------------------------|---------------------------------------------------------------------------|
| access control | fire fighting and rescue | range and training area management |
| accommodation management | grounds maintenance | reprographics and printing services |
| airfield and runway maintenance | hospitality and catering | sports and recreation services (e.g. gym operation, sport field markings) |
| cafeteria services | laundry and dry cleaning | transport services |
| cleaning | management of Defence stores | waste management |
| ensuring availability of petrols, oils and lubricants | pest and vermin control | workshop services |

Note: The majority of these services are delivered in all regions, although not all services are delivered in each region.

Source: GSS contracts

1.2 In 2008–09, total annual expenditure under Defence’s GSS contracts was \$454.77 million, with the following categories of GSS generally generating the highest contract payments (in order): hospitality and catering; access control; cleaning; grounds maintenance; fire fighting and rescue; and transport.

1.3 GSS contracts were introduced in 1998 in response to the findings of the Defence Efficiency Review, published in March 1997, and the then Government’s Defence Reform Program that was established in April 1997

following the review.²² The Defence Efficiency Review was established in October 1996 with the aim of improving the efficiency and effectiveness of Defence management and financial processes.²³ Among other things, the review noted that the use of commercial entities to deliver ‘non-core’ support services could reduce costs where the private sector already delivered similar services and large amounts of Defence work was made available.²⁴

1.4 The 1997 Defence Reform Program sought to improve the efficiency of Defence support and administrative functions, and to invest these efficiency savings to enhance military capability.²⁵ As part of this plan, Defence sought to achieve up to \$338 million worth of ongoing annual savings under the category of ‘administrative support’, which included ‘rationalisation and market testing of garrison services’.²⁶ In July 1997 Defence created the Defence Corporate Support Program to ‘achieve significant efficiency and effectiveness gains through rationalising, market testing and delivering non-operational corporate services on a Defence-wide basis’, which included Garrison Support Services.²⁷

²² McIntosh, Malcolm *et al.* (1997) “*Future Directions for the Management of Australia’s Defence*”: *Report of the Defence Efficiency Review*, 10 March; Ian McLachlan, Minister for Defence (1997) “McLachlan announces Defence Reform Program”, *media release MIN 61/97*, 11 April 1997.

²³ The Defence Annual Report 2007–08 makes the following comments on the portfolio structure:

‘The Defence portfolio consists of a number of legally distinct organisations. The three most significant of these are:

- the Department of Defence – a department of state, headed by the Secretary of Defence;
- the Australian Defence Force (ADF) – consists of the three Services (including Reserves) and headed by the Chief of the Defence Force (CDF);
- the Defence Materiel Organisation (DMO) – a prescribed agency, headed by its Chief Executive officer (CEO).’

In practice, these bodies work together so closely that they are effectively one organisation known simply as Defence (or the Defence organisation), although it has no separate legal identity. A series of internal directives and delegations effectively create a unified organisation.

²⁴ McIntosh, Malcolm *et al.* (1997) “*Future Directions for the Management of Australia’s Defence*”: *Report of the Defence Efficiency Review*, 10 March, p. 44.

²⁵ Ian McLachlan, Minister for Defence (1997) “McLachlan announces Defence Reform Program”, *media release MIN 61/97*, 11 April 1997.

²⁶ ‘Administrative support’ included clerical and administrative services as well as other corporate functions such as travel, publishing and legal services. Department of Defence (1998) *Defence Annual Report 1997–1998*, p. 15.

²⁷ Department of Defence (1998) *Defence Annual Report 1997–1998*, p. 289.

First round of GSS contracts, 1998–1999

1.5 The first round of GSS contracts were let from 1998 following the assessment of private sector tenders and in some cases in-house tenders. The contracts were based on regional areas, with one contract covering several Defence sites. Appendix 2 summarises the first round of GSS tendering. A 2002 Defence internal audit report identified that all but one of the contracts increased in cost during contract negotiations (held after the preferred tenderer had been chosen). Analysis undertaken by this Defence internal audit indicated that estimated overall savings at the time preferred tenderers were announced was 27.3 per cent, whereas the actual savings were estimated at 15.5 per cent once all contracts had been signed.²⁸

Second round of GSS contracts and Base Services tenders

1.6 A second round of contracts has been let on a rolling basis since 2004. All contracts were for five years, with the possibility of up to four one-year extensions based on performance. An Invitation To Register Interest (ITRI) was released in June 2003 for both GSS and Comprehensive Maintenance Services (CMS) contracts.²⁹ Ultimately eight companies were shortlisted for GSS tenders.³⁰

1.7 Unlike previous tenders, the recent Tasmanian and North Queensland tenders were open tenders based on a combined GSS and CMS contract (now called a Base Services contract). According to Defence, these two areas were merged in order to 'leverage the synergies that exist between these contracts in order to maximise efficiency and effectiveness'. Both tenders were for an initial five year contract period with the potential for four one-year extensions dependent upon performance. The Tasmanian contract was for an approved amount of \$16.4 million over the five years and commenced in December 2008. The North Queensland contract was for an approved amount of \$197.9 million over the five years and commenced in January 2009.³¹

²⁸ Department of Defence Inspector General Division (2002) *Contract Management of CSP Contracts: Garrison Support*, 7 February 2002.

²⁹ CMS contracts involve, amongst other things, the maintenance and repair of Defence fixed plant and equipment, and provision of engineering and other specialist advice.

³⁰ While each contract was let separately, the rules of the tender allowed tenderers to submit a combined GSS/CMS bid. There were 34 combined bids submitted during the second round of contracting, with only one (in South Queensland) successful.

³¹ Parliamentary Secretary for Defence Support, the Hon. Dr Mike Kelly MP (2008) 'New Defence Contracts for North Queensland and Tasmania', *Media Release 062/2008*. The contract prices were based on the contractor achieving 'maximum' performance payments.

1.8 Appendix 3 contains more detail on the second round of GSS contracts and the recent Base Services tenders.

Current providers

1.9 Four providers currently have all the GSS and Base Services contracts:

- Serco Sodexo Defence Services Pty Ltd (SSDS);
- ESS Worldwide Pty Ltd (Compass Group);
- Spotless; and
- Transfield Services.

A collaborative intent

1.10 The GSS and Base Services contracts place a strong emphasis on establishing a collaborative contracting relationship. The preamble to the second round of GSS contracts summarises Defence's intent for the collaborative contracting model:

For the relationship between the Commonwealth and the Contractor to operate successfully, there will necessarily be mutual trust, shared vision, and common goals between the parties. Joint Commonwealth and Contractor leadership and management teams will form part of the arrangements with the working relationships being open and transparent. As a part of the proposed collaborative contract approach, the Commonwealth is proposing arrangements, which include a risk/reward performance - based remuneration model that allows for profit/margin to be put at risk.

Performance management framework and payment

1.11 The contracts' payment structure is made up of two components: the cost of the provision of goods and services; and a margin component payable for these services, with the level of margin payment dependent on performance. There are three different margin categories: minimum quality target (Min QT), agreed quality target (AQT) and maximum quality target (Max QT). Margin is paid as a percentage of a contractor's cost, with the percentage applied increasing from a Min QT score to a Max QT score. The margin percentages vary between contracts and are nominated as part of the tender process. A more detailed examination of these arrangements is undertaken in Chapter 4.

Defence's Garrison Support Services management arrangements and resourcing

1.12 Overall responsibility for the GSS tendering process lies with the Business Services Procurement and Contracting Branch within the Defence Support Group's (DSG's) Chief Operating Officer (COO) Division. The branch is the 'process owner and technical authority' for procurement, contracting and commercial advice, and develops DSG policies and processes in these areas.

1.13 The tenders are conducted by the regional areas of DSG. Once the procurement process is complete, the administration of each GSS or Base Services contract is the responsibility of the relevant DSG region. Each DSG regional manager (the Contract Authority for their relevant contract or contracts) reports to the Head of the Defence Support Operations (DSO), a division within DSG responsible for delivery of base services to Defence.

1.14 The Head of DSO is supported by a Canberra branch led by the Assistant Secretary, Business Management which includes the Director of Business Management—Defence Support Operations, who has divisional responsibility for budgeting and planning. The Financial Management Branch within COO is also involved in GSS activity. It has responsibility for coordinating all aspects of DSG budgeting and planning, and interacts with all areas of DSG.

Current reforms relating to DSG

1.15 There are currently three main areas where Defence is undertaking reform that affects GSS.

Regional structure

1.16 The first area of reform, which was in the process of being implemented during the course of this audit, was a restructure of the regional structure that involved a reduction in the number of DSG regions from 12 to five. This change became operational on 1 July 2009.

1.17 Table 1.2 shows the change in regional structure.

Table 1.2**Changes to DSG regional structure**

| Regions from 1 July 2009 | Regions at time of audit fieldwork |
|--------------------------|----------------------------------------------------------------------------------------------------------------|
| North NSW | Sydney Central, Sydney South West (excluding Shoalhaven), Central Northern NSW |
| South NSW | ACT and Southern NSW, Riverina Murray Valley including Albury/Wodonga, and Shoalhaven (Creswell and Albatross) |
| Victoria and Tasmania | Victoria, Tasmania |
| QLD | North QLD, South QLD |
| Central and West | NT and Kimberley, SA, WA |

Source: Defence material

Contracting hubs

1.18 Secondly, DSO is introducing a ‘contracting hub model’. This involves establishing one ‘hub’—essentially a high level management team—for each contractor involved in delivering GSS and CMS services, to ensure that each of the contractor’s contracts are dealt with and managed in a consistent manner. Defence have defined a hub as being concerned with the structures and processes that underpin the GSS/Base Services and CMS contracts. Defence views the key aims of a hub to be:

- ensure contracting arrangements fit with the objectives of the wider Defence organisation;
- ensure Defence’s legal obligations are being met;
- stakeholder management;
- risk management; and
- reduce the amount of resources required for contract management.

1.19 Members of a hub will be comprised of current personnel involved in GSS and CMS management, with a key role given to particular regional directors, who will be the Contract Authority within the hubs. The hub model also envisages that DSG will ‘plan and implement a compliance/audit schedule including relevant quality assurance for GSS/CMS products and services’. Defence advised that hub structures and accountabilities became effective in July 2009, with hub/contract management arrangements and processes being progressively implemented.

Base Accountabilities Model

1.20 Finally, Defence is implementing a reform called the Base Accountabilities Model (BAM). The BAM aims to resolve problems of blurred accountability and responsibility at the base level between the Services/Defence Groups and DSG personnel. The BAM was developed in response to the findings of the Proust review.³² The key components of the BAM reform are the establishment of a series of agreements between DSG and the recipients of support services.

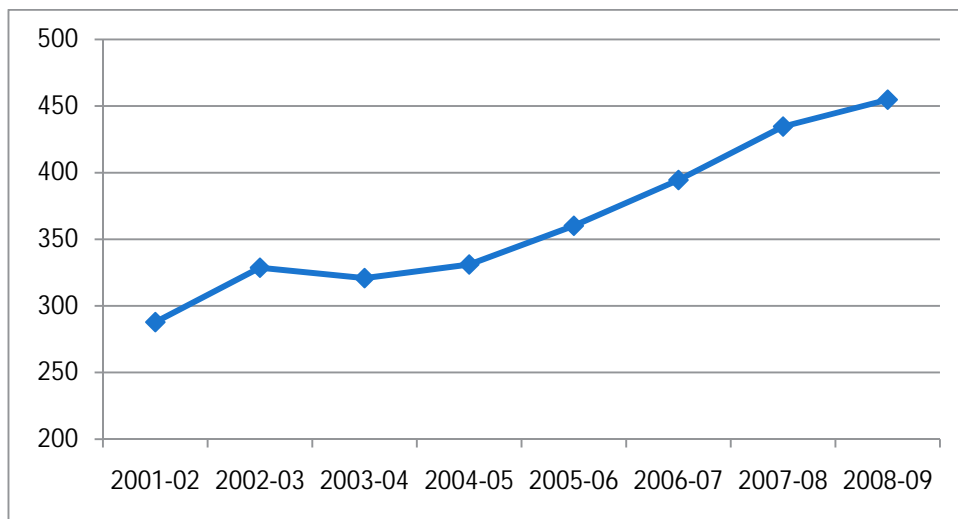
GSS resourcing

1.21 Reducing GSS expenditure has been a recent focus of Defence management because of the magnitude of the growth in GSS contract expenditure over the last decade. Figure 1.1 shows that GSS contract expenditure has increased by 58 per cent from \$287.82 million in 2001–02 to \$454.77 million in 2008–09, with a 26 per cent increase between 2005–06 and 2008–09. The majority of this increase can be attributed to the impact of price indexation arrangements over time, although there have also been increases in the scope of services delivered under GSS contracts (for an explanation of the significant scope changes see paragraph 5.61). In addition, some of the increase in GSS expenditure can be attributed to the higher Defence tempo of operations in recent years.

³² Proust, Elizabeth *et al.* (2007) *Defence Management Review 2007*, pp. 21–22.

Figure 1.1

GSS expenditure (\$ million), 2001–02 to 2008–09



Source: Defence data

1.22 In response to various Government savings initiatives (including efficiency dividends), the total savings required from the 2008–09 GSS budget was \$21.3 million (see Appendix 4 for more detail). The impact of these dividends is being addressed through an internal budget review team (refer to paragraphs 5.11 to 5.14 in Chapter 5).

1.23 In addition, in June 2009, in the context of the Defence White Paper 2009 and the 2009–10 Federal Budget, Defence announced its Strategic Reform Program (SRP). The SRP aims to deliver over the 10 years to 2019 gross savings of around \$20 billion that are required to fund the achievement of the Government’s plan to build a stronger ADF (known as Force 2030) and:

to fix key areas in Defence where under-investment in past years has left vulnerabilities in [Australia’s] military capabilities and reduced critical support functions to the ADF. [the \$20 billion] will be reinvested to deliver stronger military capabilities, to remediate areas where there has not been enough funding in the past and to modernise the Defence enterprise ‘backbone’, all of which are essential to support the fighting force.³³

³³ *The Strategic Reform Program, DELIVERING FORCE 2030*, Department of Defence, June 2009, Introduction by the then Secretary and the Chief of the Defence Force on p.3.

1.24 As part of the SRP, the reform target savings associated with GSS has been set at \$700 million over 10 years (see paragraph 5.65 in Chapter 5).

Audit approach

1.25 The objective of this audit was to assess the effectiveness of Defence's procurement and contract management for the provision of GSS.

1.26 Defence's approach to the provision of GSS through outsourced providers has developed over the 10 years that these contracts have been used. The audit reviewed the conduct of one of the most recent GSS procurements undertaken by Defence, the Base Services tender for the North Queensland region.³⁴ In addition, the audit examined contract management of three existing GSS contracts: Riverina Murray Valley, Central/Northern New South Wales and Western Australia.

1.27 Table 1.1 sets out the range of services that can be included under the GSS contracts and among these are access control services at bases. The audit scope included consideration of the management of the delivery of access control services at bases in accordance with the relevant GSS contracts but did not include any review of the appropriateness of Defence's policy related to the level of security or access control to be provided at Defence establishments (or who should provide such services), which informs the requirements specified in GSS contracts.³⁵

1.28 The criteria for the audit are summarised below. The audit considers, in respect of the provision of GSS, whether:

- arrangements comply with Commonwealth legislative and policy guidance, as well as relevant Defence guidance;
- risks have been identified and managed;
- the roles and responsibilities of different parties within Defence have been identified;

³⁴ As discussed in paragraph 1.7, unlike previous tenders, the recent Tasmanian and North Queensland tenders were open tenders based on a combined GSS and CMS contract (now called a Base Services contract).

³⁵ The access control service provided under GSS and Base Services contracts is one of the layers of security in place at Defence bases throughout Australia. For example, specific measures are taken to protect sensitive items of equipment and munitions, as well as buildings in which particularly sensitive work is undertaken.

- appropriate plans have been developed for tendering and contract management; and
- better practice has been applied as appropriate to procurement and contract management arrangements.

1.29 The ANAO engaged a consultant, Pat Farrelly, to assist with the audit. The audit was conducted in accordance with ANAO Auditing Standards at a cost to the ANAO of some \$370 000.

Report structure

1.30 The remainder of this report is structured into five chapters. Chapter 2 examines the tender evaluation process for the North Queensland Base Services tender. Chapters 3, 4 and 5 deal with different aspects of the ongoing GSS contracts with:

- Chapter 3 examining the contract management framework including the use of Regional Contract Governance Plans for GSS contracts, risk management, communication within DSG as well as with contractors and service recipients, and training and guidance for contract management;
- Chapter 4 examining performance management and measurement; and
- Chapter 5 examining contract amendments, payments and Defence's assessment of the degree to which contracting out GSS delivery has achieved the expected savings.

1.31 Chapter 6 discusses issues associated with GSS procurement and management identified during the audit and sets out a range of options that Defence could consider to improve, in the longer term, the overall GSS contracting model.

2. GSS Procurement – 2008 North Queensland Base Services tender

This chapter examines Defence's arrangements for conduct of the North Queensland Base Services tender including: the approach taken with the tender planning; planning for, and training of staff involved in, the tender evaluation; conduct of the tender evaluation; feedback to tenderers; and contract negotiation.

Introduction

2.1 In June 2003, for the second round of GSS contracts, Defence issued an Invitation To Register Interest (ITRI) which included scope for tenderers to submit a response where GSS and another category of services delivered to bases known as Comprehensive Maintenance Services (CMS) would be administered jointly.³⁶ Defence received 23 responses covering both GSS and CMS, with five of these screened out on initial assessment. Of the remaining 18 responses, 11 responses were for both GSS and CMS and seven responses were for CMS only. Of the 11 responses related to GSS, Defence included eight firms on a shortlisted GSS panel. Subsequently, until 2008, requests for tender for GSS were only provided to the panel members. Appendix 3 outlines the numbers of firms tendering for each of the 10 GSS regional contracts let under the panel arrangements instituted following the ITRI in 2003.

2.2 As discussed in paragraph 1.7, in 2008 Defence changed its approach to contracting for GSS. Where previously Defence had always put out two separate Requests for Tender (RFTs), one for GSS and one for CMS, the 2008 Tasmanian and North Queensland tenders were open tenders based on a combined GSS and CMS contract (now called Base Services contracts).³⁷ According to Defence, these two areas were merged in order to 'leverage the synergies that exist between these contracts in order to maximise efficiency

³⁶ CMS includes infrastructure maintenance services such as maintenance of fixed plant and equipment, general estate works management, engineering operations and expert estate advice. The South Queensland region was the only region where an alternate, joint GSS and CMS, tender had been successful under the previous arrangements where there were separate GSS and CMS tenders. This occurred in 2004.

³⁷ At the time of these tenders, North Queensland and Tasmania were each separate regions in the DSG regional structure. As noted in paragraph 1.16, from 1 July 2009 DSG implemented a new regional structure that reduced the number of regions from 12 to five. The former North Queensland and South Queensland regions have been combined to make up the current Queensland region.

and effectiveness'. Both tenders were for an initial five year contract period with the potential for four one year extensions dependent upon performance. The Tasmanian contract was for an approved amount of \$16.4 million over the five years and commenced in December 2008. The North Queensland contract was for an approved amount of \$197.9 million over the five years and commenced in January 2009.³⁸

2.3 Appendix 3 also shows the results of the recent open tender processes for the NQ and Tasmanian Base Services (combined GSS and CMS) contracts. Fewer firms tendered for these Base Services contracts (four for the Tasmanian contract and three for the NQ contract) than had provided responses for both GSS and CMS in the ITRI process in 2003 (11 firms).

2.4 The ANAO selected the North Queensland Bases Services tender for examination to address the procurement component of the audit objective, given that it is the more material of the two recent tenders conducted in terms of the value of the services to be delivered under the contract.

2.5 This examination was undertaken through reviewing papers and reports held by the Defence Support Group (DSG), and discussions with relevant DSG staff, the chair of the Tender Evaluation Team (TET) and representatives of each tenderer for the North Queensland Base Services (NQ Base Services) contract. The audit focused on the tender evaluation segment of the procurement process, and also examined documents related to the negotiation process following selection of the preferred tenderer.

2.6 Particular matters considered as part of the examination included:

- the approach taken with the RFT for North Queensland Base Services contract;³⁹
- planning for, and training of staff involved in, the tender evaluation;
- the tender evaluation process;
- advice to tenderers of the evaluation outcome; and
- contract negotiation.

³⁸ Parliamentary Secretary for Defence Support, the Hon. Dr Mike Kelly MP (2008) 'New Defence Contracts for North Queensland and Tasmania', *Media Release 062/2008*.

³⁹ Including the use of an appropriately competitive process. The Department of Finance and Deregulation (2008) *Commonwealth Procurement Guidelines* (p. 11) emphasise: 'Competition is a key element of the Australian Government's procurement policy framework. Effective competition requires non-discrimination in procurement and the use of competitive procurement processes.'

Approach taken with the Request for Tender for North Queensland

2.7 A consistent approach has been developed in DSG to tendering for GSS/Base Services contracts. The NQ Base Services tender was conducted using a similar approach to previous GSS tenders. The Requests for Tenders (RFTs) for GSS/Base Services contracts have comprised the following key documents:

- an introduction that provides an overview of the RFT, Defence's aims for the tender and the timetable;
- the conditions under which the tender is being undertaken;
- the evaluation methodology and price schedule, including high-level criteria and weightings, as well as Tender Deliverable Requirements;
- the statement of work, which contains the specifications of the services required under the RFT, and a range of background information that is designed to assist tenderers gain a full appreciation of the requirement; and
- the draft terms and conditions of the contract.

2.8 The Head of Defence Support Operations issued a Project Directive to Defence Support North Queensland (DS-NQ) providing it with the appropriate authority and direction to enable it to prepare an RFT for a Base Services contract for the region.

2.9 DSG's Directorate of Procurement and Contracting (DPC) has prime responsibility for ensuring the contractual format used for individual GSS/Base Services contracts is consistent with Defence's longer term approach to GSS/Base Services.⁴⁰ DPC also has principal responsibility for the evaluation methodology for tenders and the Performance Management Framework, which is a key part of the contractual arrangements. Accordingly, DPC provided guidance to the NQ Region in relation to the RFT arrangements.

⁴⁰ The DPC is part of the Business Services Procurement and Contracting Branch and is principally located in Melbourne.

2.10 The Contract Authority for the NQ contract is the DS-NQ Regional Manager.⁴¹ DS-NQ staff had the primary responsibility for compiling the RFT, with the support and guidance of DPC. DS-NQ also had responsibility for preparing the detailed statement of work, in consultation with the DSG technical authorities for GSS and CMS.⁴²

2.11 Figure 2.1 outlines the criteria applied in the evaluation of tenders for the NQ Base Services contract.

Figure 2.1

Criteria applied in the evaluation of tenders for NQ Base Services contract

- The tenderer's degree of overall compliance with the RFT.
- The extent to which the tendered solution is assessed as meeting the technical ability to provide the required services as described in Part 4 Statement of Work.
- The extent to which the tenderer is compliant with the draft conditions of contract and the assessed level of risk relating to the negotiation of a contract acceptable to the Commonwealth.
- The financial and corporate viability and capability of the tenderer and subcontractors to fulfil contract obligations.
- The tendered prices and pricing structure, including proposed payment schedule.
- The past performance of the tenderer and subcontractors in similar service-based contracts of a similar size and scope.
- The overall risk associated with the tendered solution and its ability to sustain the delivery of the scope of services to the standards required by the Commonwealth.

Source: Request for Tender: NQ Base Services No 01/08, Part 3 Section 1, p. 3.

⁴¹ Under the Terms and Conditions of the NQ tender, the Contract Authority will give Directions and carry out its other functions under the contract as the agent of the Commonwealth (and not as an independent certifier, assessor or valuer). In addition, the Contractor must comply with any Direction by the Contract Authority given under a provision of the Contract.

⁴² DSG technical authorities are responsible for oversight of the development of policy where DSG 'owns' the policy responsibility (for example, grounds, cleaning and facility operations); and to liaise and negotiate with non-DSG policy owners (for example, Defence Security Agency for access control services) and integrate their requirements into the relevant service specifications (that is, Statements of Work).

Responding to the tender

2.12 For each of the services to be delivered under the contract, Tender Deliverable Requirements (TDRs) were specified. Tenderers were required to respond on a range of matters relating to the TDRs including: delivery of core outcomes; resources; staffing; equipment and facilities; and specific issues.⁴³ Addressing these matters involves substantial detailed responses from the tenderers. For example, the core outcomes for hospitality and catering services TDR states:

Tenderers should provide an explanation of how, and by whom, each of the core outcomes detailed in the Statement of Work (SOW) for this service (Request for Tender (RFT) part 4) will be delivered at the day to day service delivery level in the NQ Region. Where the Tenderer is of the view that an initiative will significantly reduce the resource complement required to deliver this service, details of the initiative and its estimated impact on resources should be provided.

2.13 In relation to the specific issues identified in the TDR for hospitality and catering services, the TDR provides further comment on what is required to be provided by the tenderer in their tender response:

An explanation of how the tenderer proposes to provide meals away from the Mess in the context of military training exercise examples and regional locations identified in part 4, section 40, annex B. Where appropriate, provide a sample selection of meal delivery and selection options for consideration by DS-NQ and its customers

A detailed explanation of the action to be taken if a large number of additional personnel arrived unannounced for a lunch meal

A detailed explanation of the actions the Tenderer would undertake to provide a service in the event of unexpected equipment failure or power outage.

2.14 The ANAO interviewed the tenderers for the NQ Base Services contract as part of fieldwork for this audit. One of the tenderers commented to the ANAO on the lack of accuracy in the data provided with the RFT, the number of amendments required and the time that this added to consideration of what was already a complex RFT. For the NQ tender, there were 13 addenda to the RFT, which contained a large number of corrections and clarifications to

⁴³ For example, specific issues identified for hospitality and catering services include proposed cyclic menus and the system for meal entitlement control.

documentation provided as part of the RFT, as well as additional material. For example, amongst other things, Addendum 8 corrected Government Furnished Equipment (GFE) listings and the location of fire fighting services, explained inconsistencies found in the RFT in the number and type of ships to be serviced, and added additional detail for accommodation cleaning services. Defence advised that it acknowledged that some of the attachments to the addenda were large, however, where possible, marked up documents indicating changes or amendment logs were provided (for example, for the cost schedule a three page amendment log summarising the changes was provided in addition to the 183 page revised cost schedule).

2.15 Tenderers also raised concerns in interviews with the ANAO regarding the design of the tender approach for GSS or Base Services that, in their view, provided particular advantage to firms with existing contracts, and also made it difficult for new entrants to the GSS or Base Services contracting field. Tenderers commented particularly that:

- the RFT issued by Defence required large amounts of detailed responses:
 - while there is discussion in the RFT of an outcome focus to the tender, the tender documentation requires detailed responses to be made in many cases;⁴⁴ and
- given the detailed approach that is taken with the tender, the incumbent is at an advantage as site visits do not allow tenderers to fully understand the work involved.

2.16 Defence informed the ANAO that it does not agree with these comments and indicated that the purpose of its approach is to establish an understanding of how tenderers intend to deliver the service so that the quality of the services they provide, as well as their relevant expertise in delivering similar types of services, can be assessed. Defence considers that these assessments assist in differentiating between tenderers on technical and value for money terms, including risk; and without such material, it would potentially be left evaluating 'trust me' type statements to assess whether a tenderer has the capacity, experience, processes and quality systems and the

⁴⁴ This same issue was raised in a 2001 Defence internal audit report. That report stated: 'The Garrison Support Contract for South Queensland is based on a complex Statement of Work that relies heavily on stipulated processes rather than outcomes'.

evaluation would be heavily weighted towards the price offer. With regard to site visits, Defence advised that tenderers were required to take a 'risk' position on issues they did not gain a sufficient insight into, and that no requests were made for additional site inspections. Defence also drew attention to the Due Diligence period which applies to Base Services contracts.⁴⁵

2.17 The NQ Base Services RFT was made available on 30 January 2008, initially for a period of nine weeks, although this was later extended to 11 weeks following requests by tenderers. A further week was provided for an alternative General Estate Works Management services proposal.⁴⁶ Representatives of two of the three tenderers commented to the ANAO that the time available to contractors was insufficient for them to prepare a suitable tender, given the detailed nature of the material required to be provided. One tenderer commented that the time would have been appropriate if the tender had been properly outcome focused, and did not involve considerable detailed specification.⁴⁷

2.18 Defence informed the ANAO that it considers that the time provided was sufficient. Defence noted that the time provided was in excess of the minimum of 25 days set down in the Commonwealth Procurement Guidelines and was intended to provide tenderers with an appropriate response time, supported by the Due Diligence period.

2.19 The incumbent firm generally has substantially greater knowledge of the detailed requirements related to the GSS/Base Services arrangements in the region where they have been providing services. To help ensure there is effective competition in these circumstances, the ANAO suggests that there is scope for Defence to refine its assessment approach, reducing the need for detailed descriptions to be provided by tenderers, but having the ability to properly differentiate between tenderers without being reliant on tenderer assertions. As part of such an approach, Defence could put greater reliance on

⁴⁵ The Due Diligence period is a six month period from the commencement of service delivery during which activity rates included in the RFT are validated to ensure that the cost schedule reflects actual requirements, and that quality targets are fair and reasonable.

⁴⁶ General Estate Works Management covers a broad range of activities related to base facilities including receiving work requests, developing cost estimates and pre-tender estimates, developing the proposed 18 month works program, developing and presenting project plans, updating the works program, obtaining quotes, entering information into Defence Estate Management System (DEMS) and reporting on performance.

⁴⁷ Defence advised the ANAO that NQ contract was more outcome focused and consistent than earlier GSS contracts.

evaluating criteria through the examination of tenderers' systems at their existing sites (either with Defence or other organisations) and from interviews with tenderers' existing clients.

2.20 Defence informed the ANAO that it considers that any tender evaluation processes must include a balanced consideration of all technical worth, price and risk aspects in order to make 'value for money' assessment decisions. However, Defence indicated that it is continually seeking to improve the procurement process and, as such, agrees that the tender evaluation approach can be reviewed with the aim of improving the efficiency and effectiveness for Defence and tenderers, whilst still ensuring that an appropriate 'balance' is achieved and that all tenderers are treated in a fair and equitable manner.

Impact of tender design on tender preparation costs

2.21 Defence's records indicate that tenders were received within the prescribed timeframes.⁴⁸ As discussed in paragraphs 2.12 to 2.15, the RFT required tenderers to provide in their responses detailed information on how each of the services were to be provided. Based on the receipting records of Defence, the following were provided by the three tenderers:

- one tenderer provided 24 packages of documentation, as well as a number of computer disks;
- one tenderer provided 21 cartons of documentation; and
- one tenderer provided 12 cartons of documentation.

2.22 Tenderers advised the ANAO that there was a substantial cost involved in submitting a tender for the NQ Base Services contract. In addition, the representative of one tenderer indicated that their firm's costs of tendering had reduced over the years as they became more experienced in the GSS tendering process. However, the representative noted that if a tenderer did not have background in the type of tendering arrangement that Defence used for GSS (or Base Services), it could cost in excess of \$1 million to respond to a tender.

2.23 The cost of tender preparation is influenced by the design of the overall tender. Tenderers informed the ANAO that, in the case of GSS/Base Services

⁴⁸ Tenderers provided an original and three copies of their responses to the RFT, as well as electronic copies.

tenders, the requirement placed on tenderers to provide detailed information to describe, or attempt to describe, the processes that will be followed in providing specific services involves significant effort and cost. This detailed material is then considered as part of the technical assessment during the evaluation process.

Tender Evaluation Plan

2.24 Defence developed a Tender Evaluation Plan (TEP) and a Probity Plan to guide the processes for the NQ tender, and there was also a short training program put in place for members of the team undertaking the evaluation of tenders.

2.25 The TEP was prepared and issued on 14 April 2008, and outlined:

- the guiding principles to be followed including the evaluation process, ethics and fair dealing, probity, security and confidentiality;
- organisation and responsibilities for the tender evaluation, including the steering group, board, meetings, reporting and probity advisor;
- the evaluation process and method, including criteria, risk assessment and financial evaluation; and
- administrative matters related to the tender such as security, communication with tenderers and conflicts of interest.

2.26 The TEP listed 38 people as members of the tender evaluation organisation. In addition, consistent with the Defence Procurement Policy Manual, DSG engaged a probity advisor for the process.⁴⁹ This represented a substantial resource investment by Defence in the tender process.

2.27 The TEP provided a comprehensive outline of how the tender evaluation was to occur and includes important matters to be managed and administered as part of the tender process, such as evaluation methodology, security and conflicts of interest.

⁴⁹ Defence Materiel Organisation (2006) *Defence Procurement Policy Manual*, p. 3.13.8.

Probity Plan

2.28 A Probity Plan was also developed that set out in detail the probity tasks to be undertaken and provided more detailed guidance on matters such as security, conflicts of interest and the requirements of Tender Evaluation Team members. The detailed tasks set out in the Plan included:

- ensure that all team members and others meet specified probity requirements such as conflict of interest declarations and confidentiality agreements;
- ensure that all tenderers have access to the same information;
- set up confidentiality and proprietary information procedures;
- brief all staff; and
- review probity at completion of tender preparation, tender invitation stage, completion of evaluation and completion of supplier selection recommendation.

2.29 The Probity Plan's probity principles are consistent with those outlined in the ANAO's Better Practice Guide *Fairness and Transparency in Purchasing Decisions: Probity in Australian Government Procurement*.⁵⁰ The Plan provided a framework for the work of the Probity Advisor, as well as setting out background related to matters such as the Australian Public Service (APS) Values and Code of Conduct and security.

Training and guidance

2.30 Training was provided to Tender Evaluation Team (TET) members by DPC staff before the evaluation process commenced. The three day training course covered the tender and evaluation process, and the use of the computer based assessment tool used in the tender process.⁵¹ As part of the training, TET members were provided with a Participant's Handbook which provides a focus for the presentation during training sessions, and a longer term source of guidance for TET members.⁵²

⁵⁰ ANAO Better Practice Guide – *Fairness and Transparency in Purchasing Decisions: Probity in Australian Government Procurement*, p. 41.

⁵¹ The software used was called VFMFocus.

⁵² Defence informed the ANAO that the handbook used for the NQ tender was the *Northern Territory/Kimberley Tender Evaluation Training: Participant's Handbook* (July 2007).

2.31 TET members were also provided a copy of the Model Comparator. The Comparator sets out evidence that the evaluator is looking for in the response of the tenderer. The handbook indicates that the Comparator represents an attempt to provide evaluators with an indication of what an ideal response should generally look like.

2.32 DPC provided RFT Financial Evaluation Guidelines (dated January 2006) that specifically guided relevant members of the TET.⁵³ These Guidelines provide specific advice on a number of matters, including initial screening and analysis, individual bid assessment and finance meetings.

Tender evaluation

2.33 To facilitate the evaluation process, the TET was sub-divided into a number of Tender Evaluation Working Groups (TEWGs) to conduct evaluation of the tender responses. There were six TEWGs covering:

- compliance and management;
- finance;
- hospitality and catering and accommodation services;
- domestic services;
- capability support and logistics; and
- infrastructure.

2.34 The key phases of the evaluation process were: the detailed evaluation of service bids by assessors; comparative assessment of bids for services; interviews of tenderers; and the strategic risk assessment and value for money determination. The detailed evaluation involved assessing the degree of compliance with each requirement, writing a narrative to support the evaluation, assessing risk and assigning a numerical score to reflect the assessable element in accordance with guidance set out in the plan. Changes to the detailed evaluation scores can be made as a result of subsequent phases by the TEWGs or TEWG leaders. In addition, the role of each TEWG included identifying questions for subsequent tenderer meetings and noting potential issues to be considered at contract negotiation.

⁵³ This guidance is also used by DPC to assist other GSS, CMS and Base Services tenders.

Compliance with RFT requirements

2.35 The Tender Evaluation Report of the Steering Group indicated that all responses were examined by the TET prior to its evaluation to establish that they complied with the RFT. Attachment 1 to the Report outlined the work undertaken:

- review of mandatory declarations and Commonwealth requirements;
- initial review of Statements of Compliance to assess compliance with Conditions of Tender, and Terms and Conditions of Contract;
- initial review of price schedules; and
- consideration of any exclusion actions as a result of the reviews.

2.36 The Report indicated that no serious anomalies or shortcomings were identified and all responses met the essential requirements of the Conditions of Tender.

Minutes of meetings of the Tender Evaluation Board and Steering Group

2.37 The ANAO reviewed the minutes of the meetings of the Tender Evaluation Board and the Tender Evaluation Steering Group to ascertain whether there were any issues that arose that would raise concerns regarding the evaluation process.

2.38 The minutes of the Tender Evaluation Board did not reveal any issues of concern regarding the evaluation process. The main issues recorded in these minutes related to matters such as the software that was being used to record the results of assessments, progress with the tasks being undertaken by the Technical Evaluation Working Groups, staffing aspects and timing.

Technical assessments

2.39 A substantial process was undertaken for the 29 different categories under which assessments were made. These categories covered both management (for example, contract management reporting and performance, and innovation) and service delivery (for example, hospitality and catering services and general estate works management services).

2.40 The assessment of the various service components of each tender was undertaken by two assessors for those services of high value or perceived to be high risk, and by one assessor in the case of other services. In all cases there

was the opportunity for the leader of the particular TEWG to become involved, either to help resolve differences in assessments where there were two assessors, or to suggest changes to an assessment where there was only one assessor. In addition, the TET Chairman was able to intervene should subsequent discussion with a tenderer or consideration by the Steering Group warrant the scoring being amended.

2.41 In reviewing the written assessments attached to the Tender Evaluation Report, the ANAO observed:

- the primary assessments appear to have been made solely based on the written material presented by the tenderers;
- consistent with the TEP, there is evidence of TEWG leaders intervening to determine an agreed score when the two assessors could not agree on a score, even after both were given an opportunity to review their scores;
- there is evidence of a TEWG leader indicating that they were not satisfied with the assessment of an individual assessor, and asking for that assessment to be reviewed;
- there is evidence of changes to scoring being made by the TET Chairman in some cases where further information came to light during comparative assessment or later (for example, when the TET became aware through further analysis of a tender that a tenderer had under-resourced a particular service); and
- the incumbent GSS and CMS contractors for the NQ Region tended to obtain the highest scores in the particular services that they provided to the Region under their existing contracts.

2.42 These actions taken by Defence were consistent with the TEP and supported a sound approach to overall tender assessment.

2.43 As previously mentioned, under the RFT tenderers were required to provide detailed responses of how they intended to provide specific services (see paragraphs 2.15 and 2.23). The assessment observations attached to the Tender Evaluation Report in relation to one of the tenderers noted:

The tender has provided a marginal to satisfactory response. Specifically, the tenderer has not provided a detailed response to the following core outcomes and KSA's [Key Support Activity]:

41.1.6 and KSAs: Provide a booking service for Function areas (excluding Messing Areas);

41.2.1.24: Manage, issue and reprogram as required electronic keying systems to allow access to all transit accommodation which this system applies;

.....

41.3.1.14: Ensure all air conditioning controls and battery operated door locks are serviceable at all times and provide all replacement batteries;

41.3.1.15: Provide light globes and fluorescent tubes/starters and replace spent globes etc with the latest energy efficient globe that is consistent with the light fitting.

2.44 Requiring detailed responses as to how tenderers are to carry out the above tasks promotes an assessment that is focused on individual processes, rather than concentrating on the tenderer's ability to effectively manage and deliver services. If a tenderer did not address how it intended to carry out relatively minor tasks, its score was reduced. As outlined in paragraph 2.16, Defence considers that its approach of requiring tenderers to provide detailed responses on how they intend to carry out specified tasks is necessary for the assessment of tender responses to be made on the basis of value for money, rather than price alone.

2.45 However, the issue of low scores awarded by Defence assessors, who were focusing on the need for detailed information about how individual tasks were to be carried out, was considered by the Steering Group as part of its deliberations on the tenders. The Steering Group meeting minutes of 30 June 2008 stated the following:

There would appear to be a clear 'winner' but that tenderer, despite having the best overall Technical Worth and lowest price, has a potentially low score in the area of General Estate and Works Management (GEWM). Another tenderer has a similar issue and the root cause is that the assessors of that TDR [Tender Deliverable Requirement] had concerns about lack of detail in the responses and, particularly, a lack of demonstrated current capability and experience. The Steering Group discussed the issues in depth, including access to the necessary expertise (eg through the respective wider company structures), the real nature of the GEWM task, the limited recruitment pool, intended salary structures, and performance of each tenderer in related TDRs (eg 'Past Performance' and 'Alternative GEWM Proposal'). Ultimately, the Steering Group agreed all three tenderers appear to be capable of providing a

satisfactory service and that certainly no tenderer should be excluded under the 'low technical worth' provisions of the RFT.⁵⁴

2.46 The above quote from the Steering Group's minutes of 30 June 2008 gives an example of an intervention by the Steering Group to provide additional perspective to the ratings that have been provided by assessors for particular services. However, the general approach taken by Defence's assessors is illustrated in the example referred to in paragraph 2.43, with that approach also having an impact on the extent of detail tenderers seek to provide within their tenders. For the NQ contract, all tenderers had previous experience with GSS contracts, but still had difficulty providing sufficient detail in respect of certain services to satisfy Defence's requirements. The approach taken of requiring detailed information on the provision of individual services places a substantial burden on tenderers and can have the effect of reducing competition for the contract.

2.47 In the case of the NQ tender, the current arrangements have not encouraged many firms to seek this work, with there being only three tenderers for a contract worth almost \$200 million over five years, with the prospect of the contract being extended for a further four years.

Financial assessments

2.48 The Finance TEWG analysed the tenderers' financial submissions and one of its key tasks was to 'normalise' the tendered prices. Normalising tendered prices involves modifying tendered prices to ensure a like for like comparison between tendered bids. Price normalisation involved the TEWG applying the Annual Cost Multipliers consistently, and making allowances as

⁵⁴ The Tender Evaluation Report subsequently prepared also drew attention to the issue concerning two of the three tenderers receiving low technical worth scores for the General Estate Works Management component. After considerable discussion of the matter, the Report stated: 'Realistically, the critical issue for any of the contractors is getting the right people into the key positions.' In summarising the technical worth assessments later in the Report, in relation to this same issue it was stated:

'Further detailed examination of these scores, however, reinforced by clarifying questions, tenderer meetings and Referee Reports, has assuaged most of the original assessors' concerns – which essentially related to lack of detail and failure to adequately substantiate capability and experience'.

The approach taken in the Tender Evaluation Report appropriately reflects a broader assessment than that made by the original assessors. However, the final technical assessment scores for the two tenderers were not adjusted to reflect the approach taken in the Tender Evaluation Report. In this particular case, this was not a material issue as the technical worth scoring for this particular service would not have made a difference in the overall rankings.

necessary for omissions, differences in interpretation, and obvious errors.⁵⁵ The Tender Evaluation Report indicated that these amendments were informed by tenderers' responses to written clarifying questions.

2.49 The work undertaken by the Finance Working Group was checked by an external consultant who found that there were no material errors or omissions in the TEWG's analysis.

Tender Evaluation Report

2.50 The Tender Evaluation Report by the TET Chairman provides a comprehensive summary of the processes undertaken as part of the overall evaluation. The report outlines the technical worth assessments, comparative assessments and the strategic risk assessment.

2.51 In discussing price risk, the Tender Evaluation Report states:

In terms of Strategic Risk arising from pricing issues, the critical issue in a number of previous regions has been a concern about 'bottom line dollars' in some tenders. The emphasis on 'bottom line dollars' rather than, strictly, individual service lines reflects the fact that these are 'holistic' contracts and if a tenderer has inadvertently underbid in a particular service line, that tenderer has a lot of flexibility to make up the shortfall across other lines – so long as the overall dollar value of the contract is adequate. In this NQ instance, bottom line dollars appear satisfactory when compared with historical spend and, in general, when various parameters (food costs, wage rates, finance costs etc) have been subjected to more detailed analysis.

2.52 The Tender Evaluation Report indicated that the tendered prices of the three tenderers were of a similar order, although the successful tenderer, Serco Sodexo Defence Services Pty Ltd (SSDS), was the lowest priced tender. The report concluded that SSDS offered the best value for money and accordingly recommended that it be considered the top ranked tenderer.

2.53 The process undertaken in reaching this conclusion was in line with the approach to evaluation outlined in the RFT and the evaluation methodology set out in the Tender Evaluation Plan.

⁵⁵ The Annual Cost Multiplier is included in each service cost schedule for evaluation purposes to provide a consistent workload and activity volume basis for evaluating tendered costs for the five year contract period, ensuring a like for like comparison.

Probity reports

2.54 The Probity Advisor provided four reports during the evaluation process to the Chairman of the TET. In his final report of 16 July 2008 to the Chairman, the Probity Advisor stated:

From a probity perspective, the tender evaluation process appears to have been very well organised, documented and controlled and to have been conducted in a manner which was fully compliant with all requirements identified in the Tender Evaluation Plan and their supporting documents.

Advice to tenderers of evaluation outcome

2.55 DSG sent letters to the three tenderers on 6 August 2008 informing them of the outcome of the evaluation process. SSDS was selected as the top ranked tenderer and DSG's letter to SSDS indicated that the Commonwealth wished to commence formal contract negotiations for the provision of Base Services for the NQ Region.

Debriefing of tenderers

2.56 The RFT indicated that an offer of a debriefing would be made to all tenderers and that this offer would normally be made following contract signature. The RFT advised that the debriefings would be conducted by members of the TET and would generally address the following topics:

- reasons why the tenderer's tender was successful or unsuccessful;
- areas of strength, weakness or non-compliance in the tender; and
- what the tenderer can do to improve future tenders.⁵⁶

2.57 Guidance on debriefing tenderers is provided in the 2007 Better Practice Guide on *Developing and Managing Contracts* jointly published by the then Department of Finance and Administration (Finance) and the ANAO.⁵⁷ The Better Practice Guide indicates that topics covered in debriefings can include matters such as price, nominated personnel and experience of the tenderer generally. The Guide also indicates:

⁵⁶ Request for Tender, Part 2, Conditions of Tender, Base Services, Section 1.36.

⁵⁷ Department of Finance and Administration and the Australian National Audit Office (February 2007) *Better Practice Guide: Developing and Managing Contracts - Getting the Right Outcome, Paying the Right Price*, pp. 60-62.

It is important that the procuring entity's debriefing team present a fair and balanced view of the tenderer's submission. An effective way to do this is to provide tenderers with an assessment against each of the evaluation criteria, noting the weaknesses and strengths of the tenderer's submission. The tenderer should be provided with the opportunity to respond to and, where appropriate, discuss issues.

2.58 DPC provided the three tenderers with copies of written debriefs, dated 1 May 2009, some five months after the contract for Base Services in North Queensland was signed, and more than eight months after the tenderers were advised of the results of the tender evaluation.⁵⁸

2.59 The ANAO reviewed the three tender debriefs provided to the tenderers. The text of the three debriefs are for all practical purposes identical. The text in the debriefs under the headings of 'General Technical Worth Observations' and 'General Price Observations' are identical whether the tenderer was ranked first, second or third in the overall assessment. Comparative graphical material in relation to each of the TDRs is presented, and each tenderer is able to see how they performed in relation to the other tenderers for each TDR although the other tenderers are not identified against particular scores.

2.60 Such an approach to the preparation of the debriefs fails to provide individual tenderers with an assessment of the strengths and weaknesses of their particular tenders. Given that the debriefs were not provided to the tenderers for the NQ Base Services contract until May 2009, the NQ tenderers had not received feedback on the NQ tenders at the time the ANAO conducted its fieldwork for this audit. However, in discussions with the ANAO, representatives of two of the tenderers for the NQ Base Services contract expressed considerable dissatisfaction with the usefulness of the material presented within previous debriefs in respect of previous GSS contracts they had tendered for. Representatives of tenderers indicated that their organisations wished to know why they failed with a particular tender. The representative of one tenderer indicated that the feedback provided on small value tenders (\$2 million) with other organisations was better than that provided by Defence in relation to the more valuable GSS/Base Services tenders. The representatives of tenderers also indicated that the timing of the

⁵⁸ Press Release, the Hon. Dr Mike Kelly MP, Parliamentary Secretary for Defence Support – New Defence Contracts for North Queensland and Tasmania, 27 November 2008.

debriefs can be critical if there are other tenders (GSS or Base Services) that their firms are also tendering for soon after the tender in question.

2.61 In response to the tenderers' comments, Defence advised that with previous tenders under its national rolling procurement process (for GSS and CMS), verbal debriefs were provided following all regional procurements, generally after the conclusion of negotiations. Defence stated that, given its rolling program, the written debriefs were generic to ensure that no tenderer gained an advantage over their competitors with regards to the information provided and that they were all treated fairly and equitably. This approach is not satisfactory and does not provide an assessment of strengths and weakness as suggested by the 2007 Better Practice Guide on *Developing and Managing Contracts*. Providing tenderers with feedback on the strengths and weaknesses of their tenders for particular procurements is important in promoting improved competition in the longer term.

Recommendation No.1

2.62 The ANAO recommends that Defence reviews its approach to providing debriefings to tenderers for future Base Services contracts with a view to providing:

- (a) tenderers with an assessment against each of the evaluation criteria, noting the strengths and weaknesses of the tender of the particular organisation; and
- (b) debriefs within 30 days of a contract being entered into.

Defence's response

2.63 Defence *agrees* with the recommendation and its response is:

Defence will review all debriefing activities and timeframes prior to undertaking future tender processes associated with the provision of Base Services.

Contract negotiation

2.64 The ANAO reviewed documentation on the negotiation of the NQ Base Services contract with SSDS to examine the process involved and the nature of any cost increases over the tendered price agreed to during this process. Contract negotiations between SSDS and DSG were conducted over five days in mid September 2008.

2.65 Defence provided the ANAO with a list of specific issues that were addressed during negotiations. These related to scope changes, re-confirmation of tendered assumptions and readjusting 'normalised' prices (refer to paragraph 2.48).⁵⁹ Many related to the detail included in the contractual statement of work and the costings of SSDS, for example:

- amendments to access control services following a Defence Security Authority review;
- clarifying shift and food provision requirements for some locations as part of hospitality and catering services;
- what constituted 'clean and tidy' for vehicles;
- treatment of revenue from the sale of recyclable products such as metals, oils and fuels; and
- correcting SSDS's RFT response assumptions on cost and work level data, as well as their assumptions on what facilities/equipment were to be provided by Defence.

2.66 The original tendered price was \$191.5 million for the five year Base Services contract. This price included the cost of services that were market tested through the tender process but which were being delivered by APS staff. At the conclusion of negotiations the adjusted price was \$181.6 million. This amount did not include the cost of the services currently delivered by APS staff, however the contract included potential costs should Defence shift the delivery of these services to the contractor. The final amount approved was \$197.9 million which included provisions of \$8.35 million for requested services (both discretionary and non-discretionary) and \$8.0 million for prospective due diligence related changes.⁶⁰ The Head of Defence Support Operations briefed the Parliamentary Secretary for Defence Support that this amount included the addition of a range of activities previously provided

⁵⁹ Defence advised that the reason major scope changes were not made during the tender open period was to facilitate the bidding process by not adding significant changes in scope during that process.

⁶⁰ An explanation of requested services, as well as other service types within Base Services contracts, is included in Appendix 6. Discretionary funding is provided for 'one off' service requests (for example cleaning up storm damage). Additional funding is provided as part of due diligence (the first six months of the contract) in anticipation that the initial stages of the contract will involve a considerable number of work variations, as the scope of work is amended to account for inconsistencies in Defence's tender data on the detail of specific service requirements.

through Facilities Operations or other programs.⁶¹ As part of contract negotiations, the price of the contract cost schedule was reduced by approximately \$3.2 million. The primary sources of cost reductions were in cleaning services and accommodation management services.⁶²

2.67 The tender negotiation process was managed appropriately, with changes made where necessary for adjustments in price. The overall process resulted in the value for money of the tender evaluation being maintained.

⁶¹ Examples of such programs include fire break and live fire target management on Defence ranges; asbestos management; and the undertaking of additional activities at HMAS Cairns such as transport and mail delivery.

⁶² For cleaning services, the primary cost reduction arose because of incorrect SSDS tender assumptions about cleaning RAAF Townsville. For accommodation management, the main source of cost reduction was no longer requiring the contractor to purchase, manage and replace Defence furniture.

3. Contract management framework

This chapter examines the contract management framework for the GSS contracts including: the use of Regional Contract Governance Plans; risk management; communication within DSG as well as with contractors and service recipients; and training and guidance for contract management.

Introduction

3.1 As part of its examination of contract management arrangements for GSS, the ANAO considered the framework in which the ongoing contract management activities at regions and bases occurred. Evidence related to these matters was largely collected in the course of fieldwork conducted in a sample of three Defence Support Group (DSG) regions, Riverina Murray Valley (RMV), Western Australia (WA) and Central Northern New South Wales (CNNSW).⁶³

3.2 In respect of the overall framework being applied by DSG to contract management, the ANAO considered whether elements were appropriate for the GSS contractual arrangements and supported sound contract management practice. Key elements of the GSS contract management framework that the ANAO examined were:

- the use of Regional Contract Governance Plans;
- risk management;
- communication and relationships; and
- training and guidance material.

3.3 The ANAO also examined the potential benefits in Defence centralising the availability of communication, training and guidance material.

Regional Contract Governance Plans

3.4 The key planning document for GSS contract management within each region is a Regional Contract Governance Plan (RCGP), which is required under the GSS contracts. The RCGPs focus on:

⁶³ These regions were three of the 12 DSG regions in existence at the time of the audit. From 1 July 2009 DSG reduced the number of regions to five (refer to paragraph 1.16).

- governance requirements, including such matters as performance management, compliance management, financial management and risk management;⁶⁴
- roles and responsibilities, including authorities and delegations, as well as performance and compliance management; and
- governance processes, including such matters as annual audits, dispute resolution, training and customer feedback.

3.5 The RCGPs in the three regions in the ANAO's sample covered performance management matters in varying levels of detail and in different ways. The plans reflected the arrangements that were in place in the particular regions. The RMV region had commenced processes to revise its plan and introduce specific risk based contract management arrangements, although at the time of audit fieldwork this remained under development.

3.6 The RCGPs provide a useful reference point for DSG and contractor staff and formalise a number of the arrangements that it is important for both DSG and the contractor to understand, and commit to. However, while the contract management arrangements are operating in all the regions visited by the ANAO during fieldwork, in two regions the plans themselves were in draft form, or required amendment to include updated information.

3.7 In addition, the RCGPs did not reflect a sound risk based approach to the management of contracts. The main reference to risks in the plans related to the management of occupational health and safety risks, and environmental risks at the relevant Defence sites. The plans outlined the processes that would be applied in the management of these particular risks but did not refer to any assessment of risks related to management of the contracts.

3.8 Defence informed the ANAO that, as part of transitioning to its contracting hub management arrangements, a national contract governance framework is currently being developed. Following endorsement of the National Governance Framework, each Contract Authority, in collaboration with contractors, will be required to develop a contract governance plan consistent with the National Governance Framework.

⁶⁴ Risk management is intended to be addressed in the RCGPs. However, currently, the RCGPs only address risk management in relation to occupational health and safety and environmental issues.

Roles and responsibilities within DSG regions

3.9 The current GSS contracts outline the roles and responsibilities of Defence, as well as requiring additional detail to be included in the RCGPs. The contracts also provide that the roles and responsibilities of the contractor are to be detailed in the RCGPs. This enables DSG regions, through the RCGPs, to tailor the management structures used in their region to deliver GSS functions. While individual regions varied in relation to position titles and where functions sat within DSG structures, the following is illustrative of the organisational structures in place in each region for the day to day management of GSS contracts:

- a Regional Manager is the Contact Authority for GSS contracts, makes business integration decisions and negotiates changes to scope and dispute resolution;
- a Garrison Support Services Contract Manager is responsible for matters relating to technical worth, quality, complaints, scoping, regional consistency, timeliness and cost control (value for money) of service delivery (a regional position);
- a Site Manager or Base Support Manager (BSM) at each location in the region is responsible for service delivery, client/contractor relationship management and performance management (a base level position); and
- Garrison Support Officers (GSOs) are responsible for service delivery including clarification, inspections, complaints, quality and performance management and each GSO has responsibility for specified services (a base level position).

Risk management

3.10 The ANAO assessed whether risks had been identified with respect to the management of the GSS contracts in the three regions in the ANAO's audit sample and whether these risks were used to guide DSG's actions in managing the contracts. In discussing the identification and management of risks, the joint Finance/ANAO Better Practice Guide *Developing and Managing Contracts* identifies potential sources of risk as contract management capability; contractor performance; changes in circumstances; and stakeholder relationships. Examples of risks referred to in the Better Practice Guide include:

- failure to have sufficiently skilled and experienced resources to effectively manage the contract(s);
- failure to act on contractor under-performance;
- fraud and/or unethical conduct by the contractor; and
- differing and/or conflicting stakeholder expectations.⁶⁵

3.11 The GSS contractual arrangements provide for a collaborative approach to be taken to contract management (see paragraph 1.10 of Chapter 1). There are also statements in the contracts that performance management is to be a self-assessment process by the contractor. For example, the GSS contract for what was the WA region states that the Performance Management Framework ‘... is based on the preferred situation where Contractors undertake a self-assessment of performance and compliance that will subsequently be either accepted or not accepted by the Commonwealth’. Performance assessments can lead to different levels of remuneration (see paragraphs 5.4 and 5.6 of Chapter 5).

3.12 Given the existing contractual arrangements, it is important that Defence has identified the risks involved with performance monitoring and how it proposes to manage them. Matters which arise in the course of contract management, such as performance management and the assessment of claims for payment, can have a direct impact on the extent of Commonwealth expenditure and value for money of contracting arrangements.

3.13 In the three regions visited as part of the audit, the ANAO did not find evidence that a sound risk management approach was applied to contract management by DSG at the regional level (where Contract Authority rests). The assessment of contract management risks, and how such risks should be managed, needs to be undertaken by Defence, and is not a task that can be undertaken by the contractor. The ANAO recognises that implementation of improved risk management approaches in regions is likely to require amendment of RCGPs. This is because these plans contain considerable detail on how performance monitoring and management is to take place and the application of a formal risk management approach to DSG regions’ administration of the GSS contracts would be likely to affect how these

⁶⁵ Department of Finance and Administration and Australian National Audit Office (2007) *Developing and Managing Contracts*, Better Practice Guide, p. 73.

functions operate, therefore requiring some changes to the RCGPs. In the absence of systematic identification and management of risks associated with the management of GSS contracts, there is the potential that risks may be present that are not properly understood and resources may not have been deployed effectively to mitigate risks.

3.14 Subsequent discussion within the report highlights a number of areas where risks have not been systematically identified and managed and would benefit from an improved approach to risk management, such as:

- the extent of detailed checking that is undertaken by DSG as part of the performance monitoring process, and the resources that are applied to that process (refer to paragraphs 4.34 and 4.35);
- a lack of accurate and complete contract amendment information in the records held by DSG regions and lengthy delays in addressing contract amendment requests or proposals (refer to paragraphs 5.23, 5.24, 5.27 and 5.30); and
- the verification by DSG regions of tax invoices that are submitted by contractors (the tax invoices are based on summary data from systems operated by the contractors) (refer to paragraphs 5.45 and 5.46).

Recommendation No.2

3.15 The ANAO recommends that Defence adopts a sound risk based approach to the management of GSS contracts and that the resulting risk assessment be used to assist in determining the appropriate processes for functions such as performance assessment, contract amendments and payment verification, and the level of resources best applied to those functions.

Defence's summary response

3.16 Defence *agrees* with the recommendation and its summary response is:

As part of the implementation of Contract Hubs for the management of GSS contracts, Defence intends to undertake a formal assessment of all strategic and operational level risks associated with the management of the GSS contracts, including performance management, contract amendments, invoicing and payment processes. The resulting risk assessments will be used to identify opportunities to improve management and administration processes, responsibilities and timeframes for implementation across the Contract Hubs, where a primary objective is to achieve greater consistency and standardisation.

3.17 See Appendix 1 for Defence's detailed response to the recommendation.

Communication and relationships

3.18 Within the context of GSS contracts, communication occurs between contractors and DSG at the base, regional and national level. At the base level there is also considerable communication by DSG and contractors with the service recipients, primarily the ADF. DSG has established various communication forums to manage interaction between these parties. In addition, within DSG there is communication between those responsible for elements of GSS contract management at base, regional and national level.

3.19 The ANAO examined the key structured communication mechanisms in place for management of GSS. Appropriate communication is fundamental to the effective operation of outsourced service arrangements. It facilitates the resolution of any problems and ensures that all the various parties involved are kept appropriately informed. Communication is central to realising the stated collaborative intent of the GSS contracts.

3.20 Table 3.1 provides an overview of GSS communication between DSG, the contractors and service recipients.

Table 3.1

GSS communication between DSG, contractors and service recipients

| Level of interaction | Nature of interaction |
|----------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Base | <p>DSG and contractors</p> <ul style="list-style-type: none"> • performance measurement • arranging requested services • base level meetings • contract amendments <p>DSG and service recipients^A</p> <ul style="list-style-type: none"> • arranging requested services • base level meetings and receiving feedback on service delivery • base support agreements • contract amendments <p>Contractors and service recipients</p> <ul style="list-style-type: none"> • arranging requested services • feedback on service delivery |
| Regional | <p>DSG and contractors</p> <ul style="list-style-type: none"> • regional meetings • contractual reporting • strategic performance reviews • contract amendments • payment processing |
| National | <p>DSG and contractors</p> <ul style="list-style-type: none"> • annual reporting • 'board to board' meetings^B <p>DSG and service recipients</p> <ul style="list-style-type: none"> • contractor surveys on GSS delivery • agreements on service levels |

Notes: (A) Service recipients are generally ADF base personnel, although they can also include Defence civilian organisations such as Defence Materiel Organisation and Defence Science and Technology Organisation. Defence refers to service recipients as 'customers'.

(B) 'Board to board' meetings are annual meetings held between high level representatives of DSG and contractors.

Source: ANAO analysis

3.21 In additions to the interactions outlined in Table 3.1, within DSG there is communication related to GSS management and administration between the national, regional and base levels. For example, communication is necessary between the DSG regional and national levels related to the conduct of strategic performance reviews and requests for approval of contract amendments with a value greater than \$10 000.

3.22 Most DSG staff interviewed at the base level cited daily informal and ad hoc communication and interaction as necessary elements for service delivery and problem resolution. Common examples of ad hoc communication identified by DSG staff working at the regional or national levels included:

- regional offices assisting base personnel, and liaising with areas within DSG's national office (such as Defence Support Operations (DSO), Chief Operating Officer (COO) and the central finance area);
- national office advising DSG staff in the regions on technical issues; and
- Directorate of Procurement and Contracting advising regional staff on the Defence Estate Management System (DEMS),⁶⁶ payment processing, ministerial requests for information and new contract requirements.

Communication at the base level

3.23 Generally, at the bases visited, the DSG and contractor staff interviewed indicated satisfaction with how communication was operating in relation to the GSS contracts, although at one base there was considered to be scope for improvement. Most bases visited had instituted weekly or fortnightly meetings between DSG and contractor personnel. At some bases, these included all relevant personnel (including GSOs and the ADF Commanding Officer's representative), while at other bases DSG held separate meetings with contractor staff and with ADF base management. The majority of ADF representatives the ANAO interviewed at the bases visited were satisfied with both the delivery of services by the contractor and communication arrangements with DSG.⁶⁷

⁶⁶ DEMS is used for tracking and recording the quantities of activities undertaken and the application of performance margin adjustments.

⁶⁷ At Williamtown in the then CNNSW region, the Air Force representative indicated that, while satisfied with the services, there was a lack of consultation and communication on certain matters, with communication tending to be emails or crisis management.

3.24 At most bases visited normal practice was for any communication between the ADF (recipients of the GSS services) and the contractors to occur through DSG personnel rather than directly between the parties. In contrast, Singleton base in the former CNNSW region had established an 'open door' policy for direct contact between the contractor and the ADF Commanding Officer's representative. This was an arrangement the DSG Base Support Manager (BSM) had encouraged and the Army supported.⁶⁸ Singleton DSG personnel were also establishing a monthly report to provide to the Army. Defence advised that it acknowledges that this 'direct' approach may offer some practical benefits, however it needs to be balanced against an appropriate controls framework to ensure that consistency of standard and scope is maintained; and that ADF customers are not requesting services outside the scope of the contract or committing the Commonwealth to unnecessary costs.

Communication at the regional level

3.25 DSG and contractor staff interviewed by the ANAO in the three regions visited indicated they were generally satisfied with communication arrangements at the regional level. The primary communication channels used in the regions are Collaborative Management Team (CMT) meetings; Collaborative Strategy Board (CSB) meetings; and monthly and quarterly contract reporting required under the GSS contracts. The way in which meetings were utilised (such as how often and who attended) varied between regions depending on local arrangements.

3.26 CSBs are 'an upper level strategic board, responsible for providing strategic guidance to the operational management team and resolving all issues which cannot be resolved by the operational management team'. CSB meetings are attended by the most senior regional representatives from DSG and the contractor, and do not consider 'day to day specifics'. The type of issues CSB meetings consider may vary, ranging from performance management and issues identified through due diligence to relationship and communication issues between the contractor, DSG personnel and service

⁶⁸ Singleton base appeared more open to communication across different groups, with another example being GSOs communicating directly with sub-contractors, something that was not encouraged at other bases.

recipients.⁶⁹ These meetings are held every quarter to coincide with the release of the quarterly report.

3.27 Each region conducts annual collaborative workshops/conferences attended by both DSG and contractor personnel. These workshops/conferences focus on each group learning more about the other and how to work together and deal with problems.

Nature of base and regional relationships between DSG and contractors

3.28 The GSS contracts place a strong emphasis on the establishment of a collaborative relationship between Defence and the contractors (refer paragraph 1.10 of Chapter 1).

3.29 The nature of the collaborative relationship that had been developed between Defence and the particular contractor in the regions the ANAO visited varied. In the former RMV region, significant effort had been made to build a strong working relationship between DSG and the contractor. Personnel involved in the management of the GSS from both DSG and the contractor had undertaken training on managing contract relationships (see paragraph 3.44), and the personnel involved appeared to have put effort into building a relationship. The collaborative intent of the contract appeared to work in the former RMV region.

3.30 In contrast, at another region in the ANAO's sample there was some tension in the relationship between DSG and the contractor, with particular strains existing at one base. There were a large number of disputes over service delivery and a heavy focus from DSG personnel on detailed inspections and audits.⁷⁰ Accordingly, at the time of audit fieldwork the collaborative intent of the contract did not appear to be being met in that region. Defence advised that DSG is currently implementing reforms to improve stakeholder relationships. DSG's contract management reforms, including the adoption of hub management arrangements, are proposed to remove inconsistency in management of the collaborative relationships with GSS contractors. In

⁶⁹ The Due Diligence period is a six month period from the commencement of service delivery during which activity rates included in the RFT are validated to ensure that the cost schedule reflects actual requirements, and that quality targets are fair and reasonable.

⁷⁰ A central component of the contracting model is self-assessment of performance by the contractor, with Defence to undertake random checks to obtain assurance on these assessments.

addition, the GSS contracts provide an opportunity to take stock of collaborative arrangements, and seek improvements, through periodic strategic performance reviews (refer paragraphs 4.51 to 4.57 in Chapter 4).⁷¹

3.31 Defence informed the ANAO that, since the audit fieldwork was completed, a National Contract Governance Framework has been developed, which includes a National Contract Directive. The Directive sets out communication processes.

Communication at the national level

3.32 The last reporting requirement included in each of the GSS contracts is the requirement for an annual report. This report provides a summary of key results and issues for that year. The report also provides the contractor's assessment of their performance against specified strategic performance indicators.⁷²

3.33 At the national level, the key reporting mechanism used within DSG involves extracting a summary of regional performance from the CAPMAN system. DSG also has in place an internal forum to gather service recipient views, on an ongoing basis, about contractor performance and conducts 'customer' surveys every two years as part of the strategic review.⁷³ Apart from the summary report drawn from CAPMAN, there is no regular reporting of issues from the regions to the national level.

3.34 'Board to board' meetings are annual meetings held between national level representatives from DSG and each contractor holding GSS contracts (generally one meeting per contractor).⁷⁴ These meetings provide a forum for each party to communicate high level issues (for example the impact of an economic downturn on service delivery), and provide general updates on

⁷¹ GSS contracts provide for strategic performance reviews to be undertaken at the end of year two of the contract life, with subsequent reviews undertaken at two yearly intervals as required. At the time of audit fieldwork, strategic performance reviews were being undertaken, or about to be undertaken, at the three regions in the ANAO's sample.

⁷² These indicators are: level of small to medium enterprise (SME) engagement; contract service delivery performance; contract compliance performance; health of the collaborative contract relationship; corporate performance; achievement of continuous improvement and innovation; customer satisfaction; and contract financial outcome for the contractor.

⁷³ Unlike the other Services, Navy does not allow individual members to directly answer these surveys, instead using the base Commanding Officer to speak for the base personnel.

⁷⁴ Although two meetings were held with each contractor in 2008.

contract performance and DSG developments, such as the current processes to develop hub arrangements (see paragraph 3.38).

Current Defence initiatives

3.35 DSG is currently undertaking a number of initiatives to improve overall GSS management performance, including in the area of communication arrangements with contractors.

Base Accountabilities Model

3.36 As mentioned in Chapter 1, Defence is implementing a reform called the Base Accountabilities Model (BAM) to clarify accountabilities and responsibilities between DSG personnel and the recipients of GSS. The framework for BAM is based on agreements between DSG and the recipients (or 'customers') that will seek to encapsulate the responsibilities and expectations of both sides relating to their roles in the ongoing operation of bases and Defence establishments. The relevant agreements which will make up the BAM framework are:

- A Memorandum of Arrangements, which is a high level, principles based agreement between DSG and the three Services (signed September 2008).
- Customer Supplier Agreements (CSAs) to be developed between DSG and all recipients of DSG services, both ADF and non-Service organisations. These will set out the mutual responsibilities and accountabilities of each group and include a performance management framework (incorporating customer feedback) and a dispute resolution process. CSAs with each Service are planned to be established by mid 2009, and subsequently with other Defence groups in receipt of GSS (for example the Defence Materiel Organisation, the Defence Science and Technology Organisation and Joint Logistics Command).
- Base Support Agreements to be developed for each base between DSG and the head of each resident unit at a base.⁷⁵ This will set out the products and services each unit is to receive, and will also include relationship management and dispute resolution information.

⁷⁵ At any one ADF base there may be a number of distinct ADF units with their own command responsibilities.

3.37 DSG informed the ANAO that it plans to implement the BAM across Defence during 2009.

Hub arrangements

3.38 As discussed in Chapter 1 (see Chapter 1, paragraphs 1.18 and 1.19), DSG is introducing a 'contracting hub model' which will necessarily result in some changes to how communication between contractors and DSG occurs above base level. This is because under this model one 'hub'—essentially a high level management team—will be established for each contractor involved in delivering GSS and CMS services to ensure that each of the contractor's contracts are dealt with and managed in a consistent manner. The 'hub' model also envisages a changed, more consistent, approach by DSG to assuring itself regarding the performance self-assessments undertaken by contractors, although the precise nature of the revised approach had not been determined at the time of audit fieldwork.

3.39 Defence subsequently informed the ANAO that, as part of the implementation of contract hubs for the management of GSS contracts, it intends to undertake an assessment of all strategic and operational level risks associated with the management of the GSS contracts, including performance management, contract amendments, invoicing and payment processes. The resulting risk assessments will be used to identify opportunities to improve management and administration processes, responsibilities and timeframes for implementation across the hubs.

3.40 In addition, Defence informed the ANAO that a National Contract Governance Framework has been developed and will consist of a National Contract Directive and supporting Contract Hub-level Governance Plans. The National Contract Directive has been developed and was issued to industry for comment as part of the implementation of the hub arrangements, and is proposed to be issued by 31 October 2009. Contract hubs will be required to have their respective Contract Hub-level Governance Plans in place by no later than 28 February 2010. The Directive and Plans will mandate appropriate processes for functions such as performance assessment, contract amendments and payment verification.

3.41 Defence also informed the ANAO that the Contract Authorities are in the process of being changed to align Contract Authorities with hub arrangements.

Training and guidance

3.42 Directorate of Procurement and Contracting (DPC) in the DSG national office has traditionally provided training on the procurement process to GSS personnel in the regions when a GSS tender process was due to be undertaken. DSG at a national level has also assisted staff in the regions, including at the bases, to learn to operate the systems used in the management and administration of GSS.

3.43 The ANAO interviewed a range of base and regional DSG staff involved in the management of GSS in the three regions in the audit sample. The ANAO asked interviewees about the training and guidance that they had received. Comments provided by base and regional DSG staff regarding training included:

- all personnel are provided training and refresher courses on systems they are required to use, such as CAPMAN, DEMS and ROMAN;⁷⁶
- many had attended Defence's simple procurement training, with a few having completed the complex procurement module;⁷⁷
- some had undertaken training in contract management, contract law and auditing;
- specialised training was provided in high risk areas, such as fuel management and explosive ordnance;
- for some the main source of GSS specific training was 'on the job' training, for example GSOs and BSMs being assisted by their regional offices on contract interpretation; and
- on occasions, it can be difficult to get contractor personnel on training courses (for example, for Defence systems such as the Standard Defence Supply System used for inventory management) as Defence personnel have priority.

⁷⁶ Descriptions of these systems and their relevance to the management of GSS are contained in Appendix 3.

⁷⁷ Outlined in *Defence Procurement Policy Manual* (2006), pp. 1.5.1-1.5.3.

Training to maintain a strong relationship: former RMV Region

3.44 Personnel from the former RMV region—from both DSG and the contractor—undertook training with external consultants as part of their collaborative conferences. This training was in a copyrighted professional contract management model. A significant focus of the training was managing the relationship in contracts, for example managing conflict during negotiation. The training emphasised that, while differences between parties were an inevitable part of contracting, a good relationship was important and led to better performance and negotiation outcomes. DSG and contractor staff from the former RMV region informed the ANAO that they considered this training contributed to the collaborative relationship that they considered existed in the region.

Development of contract management training

3.45 DSG has recently developed a training course—‘Professionalising Contract Management’ (PCM)—tailored for all personnel involved in GSS, CMS and Base Services contract management, including contractor personnel. The PCM training was delivered in pilot form by an outside provider in 2008. While Defence had put considerable focus on training for the procurement process for GSS, CMS and Base Services, specific training on contract management had not been previously provided to base and regional personnel involved in managing the resulting contracts.

3.46 Defence informed the ANAO that ‘in-house’ delivery of the PCM training course commenced in April 2008, with training now having been delivered to the former WA, South Australia, Tasmania, North Queensland, Sydney Central, Sydney West South, ACT and Southern Victorian regions. Training will be delivered to the remaining regions, Northern Territory / Kimberley, South Queensland, RMV and CNNSW by 31 March 2010. This training program will then remain ongoing.

3.47 The course covers five key areas of contract management:

- the legal background to contracting, Defence legal requirements and an overview of key GSS/CMS/Base Services contract clauses;
- more detailed examination of the GSS/CMS/Base Services contracts, including contractor obligations;

- understanding the drivers of individual and commercial entities, common areas of conflict, differences and approaches to manage these issues in a contractual relationship;
- examination of performance management under the contracts; and
- background to Defence financial and budgeting requirements.

3.48 This PCM training is comprehensive and should provide a useful reference for those involved with GSS contracts, including contractor personnel. One area in the PCM training that could be expanded further is its consideration of 'management of risk'. Risk management approaches to the management of GSS contracts were generally not well developed in the regions visited (see paragraphs 3.11.to 3.14). Defence informed the ANAO in response to the proposed audit report that it agrees to expand the PCM training course to include overall risk management.

Centralising the availability of communication, training and guidance material

3.49 Currently DSG does not have a central, easily accessed repository of training and guidance material for either its own staff or contractor staff involved in the management of GSS, CMS and Base Services.

3.50 Creating a centralised location (for example, an intranet site) could greatly improve access to training and guidance material, and provide a useful mechanism for communicating key GSS material to DSG and contractor base and regional staff, such as new initiatives or developments. This would give base and regional personnel, including the contractor, access to a suite of both formal training material (such as the PCM handbook) and advice covering all areas of their work, such as contract amendments.⁷⁸ Further development of such a site could include an online contract amendment process (DSG is currently developing an electronic contract amendment process—see paragraph 5.35 of Chapter 5). Developing such a location for communication and guidance would contribute to a consistent national approach, allow for ease of communication, provide an authoritative up-to-date reference source and reduce the demand for local solutions.

⁷⁸ Some areas of the intranet site would need to be accessible only by select people, for example contract amendment processes would only be accessible to DSG staff responsible for doing amendments.

Recommendation No.3

3.51 The ANAO recommends that Defence, in order to support effective GSS, CMS and Base Services related contract management and administration, assesses the benefits of establishing a central information source using an information technology solution (for example, an intranet site) to:

- (a) improve access for base and regional personnel, including relevant contractor personnel, to up to date training and guidance material; and
- (b) provide a convenient mechanism for regular, timely communication with these personnel.

Defence's summary response

3.52 Defence *agrees* with the recommendation and its summary response is:

Defence has already developed, and is currently delivering, the Professionalising Contract Management Training Program to Defence and GSS Contractor Contract Management and Administration staff in the regional offices. This Training Program has been specifically tailored to these contracts.

Defence will also establish an intranet website for access by Defence and Contractor Personnel. It is envisaged that this intranet website will include general contract management training and guidance material, specific GSS Contract Management training, copies of the National Contract Directive and supporting Governance Plans, relevant document templates, notices, issues registers etc.

3.53 See Appendix 1 for Defence's detailed response to the recommendation.

4. Contract performance management and measurement

This chapter examines the performance management framework for GSS contracts including: its administration in the regions in the ANAO's audit sample; the risk/reward model; the national reporting of GSS performance; and the use of strategic performance reviews.

Introduction

4.1 Effective performance management and measurement are fundamental to achieving the benefits expected from contracting out of service delivery. Performance management needs to be informed by appropriate performance measurement which requires the establishment of:

measures that can be used as the basis for assessing the performance outcomes of a service provider. Comprehensive performance measures look at output, input, quality, timeliness and success of achievement of contract objectives. They can be both qualitative and quantitative.⁷⁹

4.2 The ANAO examined the existing Defence performance management and measurement arrangements for GSS including:

- contractual provisions for monitoring progress and assessing performance; and
- the application of the GSS performance management framework including:
 - guidance on performance and margin payments in the GSS contracts and CAPMAN;
 - processes adopted by DSG base and regional staff in the three regions in the ANAO's audit sample;

⁷⁹ ANAO Audit Report No.37 2004–05, *Management of Business Support Service Contracts*.

- ANAO analysis of performance ratings of the GSS contractors for these three regions;
- the impact of these performance ratings on the margins paid to the contractors;
- national reporting and oversight of GSS performance; and
- strategic performance reviews.

Contractual provisions for monitoring progress and assessing performance

4.3 The GSS contracts provide a significant amount of guidance for undertaking performance management and measurement for GSS contracts. This guidance is supplemented by specific information in relation to the tools and systems to be used in the monitoring and recording of GSS contract performance. To facilitate the provision of support services to Defence across a number of regions, GSS contracts contain provisions for each region to tailor its governance and performance management frameworks to meet not only prescribed common service standards, but also local ADF needs.

4.4 Defence's approach to performance management is an amalgam of inter-connected procedures, processes, systems and tools. The requirements related to performance management are contained within the GSS contract itself, and are outlined below:

- The Performance Management Framework (PMF) has Strategic Indicators which focus on long term issues and form part of considerations for contract extensions, as well as indicators related to ongoing performance. For ongoing performance management there is one Key Performance Indicator (KPI) for each service, which is supported by Performance Indicators (PIs). The PMF also includes Compliance Indicators (CIs) that have been created to objectively measure contractor activity against a clear contractual requirement. The contract describes PIs and CIs and sets out how they are to be measured.

- The Risk Reward and Remuneration Model (RRRM) uses PI and CI monthly outcomes to calculate the margin payable for each service on a monthly basis.
- The Statements of Work (SOW) for each service describe the service outcomes, minimum standards and particular requirements for that service.

4.5 In addition, at the time of audit fieldwork each Regional Contract Governance Plan (RCGP) outlined how performance monitoring was to occur for a particular contract.⁸⁰ There are also information technology systems/tools (outlined in Appendix 5) for use as identified in the contract:

- the Contract Performance Management Tool (CAPMAN);
- the Defence Estate Management System (DEMS); and
- the Resource Output Management Accounting Network (ROMAN).

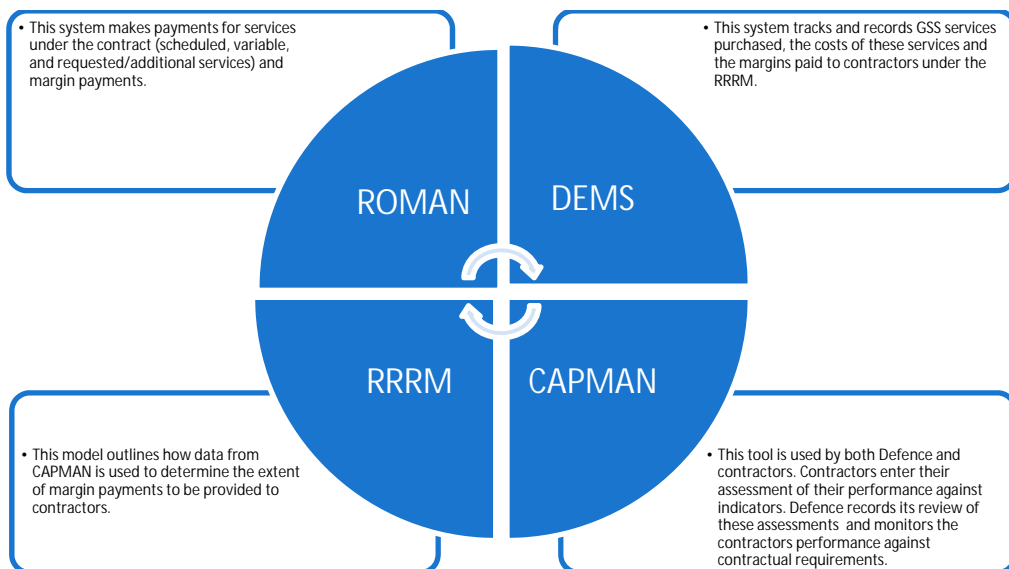
Application of the GSS performance management framework

4.6 Figure 4.1 illustrates the interaction of the various systems and tools related to the PMF.

⁸⁰ At the time of audit fieldwork it was not clear what impact, if any, the reduction in the number of DSG regions (from 12 to five) would have on the RCGPs.

Figure 4.1

Operation of the Defence GSS Performance Management Framework



Source: ANAO analysis

4.7 The fundamental principle of the PMF is that performance management is undertaken collaboratively with the contractor. The overview of the PMF as set out in the GSS contracts states:

The PMF aims to develop the quality of the relationship between Defence and the Contractor to a point where Defence is able to confidently rely on the performance reporting provided by the Contractor without the need to undertake rigorous and ongoing audits.

Guidance on performance and margin payments in the GSS contracts and CAPMAN

4.8 The PMF has three levels of reporting for performance measurement (see Table 4.1). Each of these reporting tiers has a 'scoring' mechanism applied. The GSS contracts state:

The performance scores assessed by the Contractor at the PI level, and confirmed by Defence, should provide a valid and reasonable reflection of the quality of the service across all of the Defence locations being assessed for the particular month at the KPI level.

Table 4.1**Assessment tiers for ongoing performance in GSS contracts**

| Tier name | Description |
|---------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Key Performance Indicators (tier 1 scoring) | These are the highest and broadest level output for each GSS service, with one KPI for each service. Results are scored out of 100 (the performance score). CAPMAN calculates the performance score by averaging the score of the tier 2 PIs relating to the particular service. |
| Performance Indicators (tier 2 scoring) | PIs are measures of the quality/performance against particular aspects of each service. They are expressed as a score out of 100 (the assessment rating). Supporting Criteria are used as the basis of assessment for subjective services. |
| Supporting Criteria (tier 3 scoring) | <p>Supporting Criteria generally underpin the PIs for grounds maintenance, cleaning and hospitality and catering services. Supporting Criteria assist assessors in areas where objective assessment is difficult. They require yes/no responses. An averaged calculation of the responses against the relevant Supporting Criteria provides the rating for each PI (for example eight 'yes' and two 'no' answers will result in an assessment rating of 80).</p> <p>The GSS contracts specify that, although Supporting Criteria must always be used as the basis for the initial assessment of a PI, they must never preclude other factors being taken into account to ensure the final rating is a reasonable reflection of performance.</p> |

Source: GSS contracts

4.9 Guidelines on CAPMAN reporting state that: 'Each Performance Indicator requires an assessment outcome (a rating value recorded as a number between 0 and 100) and a Pass or Fail decision for Compliance Indicators'.⁸¹

4.10 To assist in the monitoring and assessment of contractor performance, Defence has established 'Quality Targets' for each GSS service:

- The Minimum Quality Target (Min QT) reflects the level at which performance quality begins adversely affecting operational capability and is unacceptable to Defence. Performance scores and assessment ratings below this point will be reported with a red traffic light in CAPMAN reporting.
- Performance scores and assessment ratings at or above the Min QT but below the Agreed Quality Target (AQT) will be reported with an amber traffic light in CAPMAN reporting.

⁸¹ Department of Defence, *Guidelines on CAPMAN reporting standards (Supporting Comments)* p. 1.

- AQT is the level at which performance is equivalent to Defence's expectations and reflects customer capability requirements, and group and base level customer supplier agreements. Performance scores and assessment ratings at or above AQT will be reported with a green traffic light in CAPMAN reporting.
- The Maximum Quality Target (Max QT) reflects the level at which performance exceeds Defence's expectations. Performance scores and assessment ratings at Max QT will be reported with a green traffic light in CAPMAN reporting (similarly to AQT).⁸²

4.11 The GSS contracts provide that 'In respect of the PMF, there is no place for financial considerations in its processes.'⁸³ However, as the performance based remuneration model allows the contractor's profit margin to be put at risk, in real terms, the performance scores entered and accepted in CAPMAN have a direct effect on the contractor's profitability. Defence informed ANAO that the intent of this statement was to ensure that performance assessments, which measure the quality of the service provided, are a fair and accurate reflection of the quality of the services delivered and were not biased as a result of funds availability.

Prevention events

4.12 In the case of both PIs and CIs the Contract Authority (the DSG regional manager) has the ability to invoke a 'prevention event' within CAPMAN to take account of any extraneous circumstance affecting performance. Invoking a prevention event will record in CAPMAN that significant mitigating circumstances surrounded the relevant non-performance against the performance or compliance indicator. Use of a prevention event removes the impact of the assessed performance against the relevant indicator on the average score used for the purposes of the RRRM, although the prevention event will not change the traffic light state for the particular indicator.

Disagreements between the contractor and DSG on particular assessments

4.13 GSS contracts provide that where the Contract Authority does not substantially agree with the contractor's assessment of its performance against

⁸² Department of Defence, DS-WA Garrison Contract, Part C Schedule 4, *Performance Management Framework*, p. 3.

⁸³ Department of Defence *DS-WA Garrison Contract Part B Terms and Conditions*, p. 4.

an indicator, the relevant entry in CAPMAN should be noted 'Disputed by Defence'. The contracts set out a number of suggestions as to how this should be resolved, and emphasise that there should be 'a genuine attempt to understand each other's rationale behind their respective assessment'. There are processes in the various regions for escalating any disputed assessment in the event of continual disagreement.

4.14 In two of the regions the ANAO examined, performance assessment scoring appeared to generally proceed without disagreement between DSG and the contractor. In the case of one base in the remaining region in the ANAO's sample, some tension existed surrounding performance measurement, with contractor staff attempting to influence the measurement process to reduce the likelihood of adverse scores. For example, DSG staff informed the ANAO that on occasions when there was a low score for the cleanliness of a building, the contractor may either remedy the problems and re-assess the score, or inspect additional buildings in order to improve their overall score.⁸⁴ It is understandable that there can be tension when the level of the score can have an impact on the risk/reward payment made to the contractor.

Risk Reward Remuneration Model

4.15 The key elements of the RRRM are:

- the assessment of performance for each service is undertaken against a range of PIs at a number of bases throughout a region. At each base the PIs are averaged to provide a performance score for each service;
- the base performance scores are then averaged to provide a performance score for each service at a regional or contract level; and
- these regional scores are used by the RRRM to calculate the extent of margin payment for each service.⁸⁵

⁸⁴ Defence advised that this circumstance, where there is an alleged attempt on the part of the contractor to influence the risk/reward payment, highlights the challenge in ensuring no financial considerations should influence activities under the PMF. Defence stated that clear cases of actions contrary to the requirements/spirit of the PMF should be recorded in the Management of Services compliance indicator 1013. Where it is clear that a contractor is persistently not acting in the spirit of the PMF, this behavior could be considered as part of a region's Strategic Review process.

⁸⁵ DSG Western Australia Garrison Support Services contract, Part C Schedule 9, *Risk/Reward Remuneration Model*.

4.16 As part of the tendering process, the contractor is required to nominate the expected margin percentage payment for the achievement of performance at each quality target. Accordingly, these margin levels vary between contracts. The margin is calculated against the base amount payable by Defence for a particular service in the relevant period.

4.17 Table 4.2 illustrates the linkages between assessed contractor performance scored in CAPMAN and the RRRM using the example of Access Control services and notional margin percentages. For the purposes of illustrating the type of margin involved, the table includes a notional margin amount which gives an indication of the approximate amount of margin being paid to contractors.

Table 4.2

An illustrative example of the Performance and Risk Reward Remuneration Model linkages for Access Control Services

| CAPMAN Score | = a Quality Target | = Traffic Light indicator ^A | = Margin Payment ^{BC} |
|--------------|--------------------|----------------------------------------|------------------------------------------|
| 0—69% | Nil | Red | zero (nil margin) |
| 70—79% | Min QT | Amber | Between 2% and 3.99% |
| 80—89% | AQT | Green | Between 4% and 5.99% |
| 90—100% | Max QT | Green | 6% (for any score 90 or above in CAPMAN) |

- Notes:
- (A) Traffic light Indicators are used in CAPMAN reporting and summary reporting within DSG.
 - (B) Margin payment will vary according to the specific CAPMAN score. For example, using the numbers above, a CAPMAN score of 85 would result in a margin payment of 5%, and a score of 75 would result in a margin payment of 3%.
 - (C) The level of margin payment shown here (2% for a 70% CAPMAN score, 4% for a 80% score and 6% for a 90% or higher score) is for illustrative purposes, with each contractor having set margin levels as part of their original tender.

Source: ANAO analysis

4.18 The same CAPMAN scores are used to assess performance of most services—70, 80 and 90 for Min QT, AQT and Max QT respectively. However, for four services deemed high risk (petrol, oils and lubricants; air support services; fire fighting and rescue; and range and training area management) higher scores apply for each target (90, 95 and 100 respectively). For all services, if performance against a CI is recorded as being non-compliant in a

particular period, such a score precludes payment to the contractor of any margin for the particular service in the period concerned, regardless of the PI score otherwise achieved for the service.

4.19 Some services have been identified in the GSS contracts as being unsuited to the full application of the standard risk/reward arrangement under the RRRM. The operation of the RRRM for these services differs in that it provides for a 'risk only' outcome in that no reward can be gained, however the margin can be lost. In compensation for forgoing the prospect of reward, the particular services' KPI value only has to reach the Min QT point to secure payment of the target margin which is equivalent to the margin paid for AQT.⁸⁶

Use of stretch targets in contracts

4.20 GSS contracts state: 'The Commonwealth expects that service delivery performance will typically meet the Agreed Quality Targets (AQT)'.⁸⁷ The PMF indicates that all performance indicators will be subject to ongoing monitoring and that when consistently high performance assessments against a service are evident, the indicators are to be reviewed to ensure that the contractor is being sufficiently 'stretched':

The impact of performance stretch targets, and the annual performance review process detailed at Schedule 4 [the PMF], is that, where any service delivery performance indicator consistently exceeds the AQT, Defence and the Contractor will recalibrate the performance indicator to align the performance level to a new revised AQT against which performance will be assessed, and margin paid.⁸⁸

4.21 From its examinations of the CAPMAN reports relating to the three regions in which the ANAO conducted fieldwork, there were multiple occasions where Max QT had been regularly achieved for particular services. In addition, the 2008 GSS Budget Management Review stated that, across all regions, contractors are consistently achieving a level of performance between AQT and Max QT. Defence advised the ANAO that contractual provisions

⁸⁶ The services operating under this arrangement are Management of the Services and the risk only Services, which are Pest and Vermin, Laundry and Dry Cleaning, and Accommodation Services.

⁸⁷ Department of Defence DS-WA Garrison Contract, Part C Schedule 3 Pricing Schedule, Part 2 Margin Schedule. p.1.

⁸⁸ Department of Defence, *DS-WA Garrison Contract, Part C Schedule 4 Performance Management Framework*, Annex A, B, C and E. p.4.

relating to stretch targets had never been applied in any of the GSS contracts. Given that the provision related to performance stretch targets has never been applied, there are doubts as to whether this aspect of the PMF is workable, or can be made to be effective.

'How Measured' scoring guidance

4.22 The 'How Measured' guidance within the contract (and shown in CAPMAN) provides assistance to both contractor and DSG staff when determining the performance rating that should be applied when assessing performance for a particular indicator.

4.23 For example, one access control Performance Indicator (PI 5051) is rated against the requirement that: 'Assignment Instructions that encompass full operational instructions for the effective security at each site are in place and are being adhered to.'

4.24 The 'How Measured' guidance states that this performance indicator is to be rated as follows:

Having a full range of Assignment Instructions and being able to demonstrate full adherence to them at all times will score 100. Minor deficiencies in the Assignment Instructions or one or two minor examples of non-adherence will result in a score of 80. Missing Assignment Instructions or Assignment Instructions that are clearly in-effective or deficient will score between 0 and 69 depending on the seriousness of the situation as will one or more major examples of non-adherence or three or more minor examples of non-adherence.

4.25 This guidance assists staff to make decisions on what is considered to be performance for which a score of 100, 80 or below 70 should be awarded. Staff can also interpret what might be involved with a score of say 85 or 75, although there is no specific comment on what would warrant such a score.

4.26 Similar guidance is provided in respect of other performance indicators. In the example referred to above, the 'How Measured' scoring guidance states that unless there is noted under performance, the CAPMAN rating should be 100 per cent. When the CAPMAN scores are rolled into the RRRM this equates to a Max QT margin payment in different contracts and regions. Based on this type of approach, it could be expected that an assessment of Max QT would be recorded reasonably frequently.

4.27 However, GSS contracts also provide that AQT is the level at which performance is equivalent to Defence's expectations and reflects customer

capability requirements, and group and base level customer supplier agreements. The scoring recorded for the access control performance indicator referred to in paragraph 4.23 differed in the three regions in the ANAO's audit sample, although there was nothing recorded in CAPMAN to suggest that actual performance in the three regions was markedly different. The impact of these different assessments is discussed in paragraphs 4.39 to 4.44. It is unclear precisely what contributed to these different results, although it may occur because of differences in interpretation and the extent of reliance placed on particular parts of the contract (such as the definition of AQT or the 'How Measured' guidance). Defence informed the ANAO that, depending on how a region was applying the PMF in certain circumstances, 'training, guidance and coaching have been provided to those regions to calibrate their understanding of the intended application of the PMF'.

Processes adopted by DSG base and regional staff

4.28 The PMF is based on the principle that the contractor undertakes self assessments of its performance. This rating is entered into CAPMAN and subsequently accepted or disputed by Defence. The ANAO met with contractor representatives in each region visited during the audit and undertook a high level review of the performance monitoring processes in use by the contractors.

4.29 Each contractor had various systems and records in place to support performance assessment and ratings for each service delivered. Contractors monitor and analyse information provided through comments books and other feedback mechanisms, food safety plans and customer satisfaction surveys. Records were held of internal and external audits, and compliance items such as insurances, licensing and staff qualifications.

4.30 The PMF acknowledges that each region will place different degrees of importance on the services provided. Accordingly, it provides that DSG will decide in each region how, and to what extent, the self assessments undertaken by the contractor are confirmed and verified by Defence. Under the GSS contracts, the confirmation and verification strategy to be adopted should be formalised in the RCGP.⁸⁹ However, none of the three regions examined had

⁸⁹ Department of Defence, Performance Management Framework, p.15 [DS-WA Garrison Contract].

undertaken a risk assessment to help inform their approach to assessing the performance of the GSS contractor.

4.31 DSG regions advised the ANAO that the verification of contractor performance was measured through reviews of contractor data and scheduled joint inspections. In order to conduct the inspections, regions had developed checklists in various formats based on the performance indicators and supporting criteria in CAPMAN, as well as, where pertinent, items or performance standards sourced directly from the Statement Of Work. Some of the checklists included scoring systems and formulas to support the final assessment rating that was to be entered into CAPMAN. The results of these inspections and the subsequent CAPMAN scores were usually then agreed by DSG and the contractor prior to the rating being recorded in CAPMAN. Most assessments are jointly undertaken, and disputes are generally resolved by the contractor and DSG staff who have undertaken/reviewed the assessments prior to CAPMAN entry.

4.32 In two of the three regions in the audit sample, when, where and what service or location was to be inspected was usually nominated and scheduled by the contractor.⁹⁰ In all three regions, the majority of these inspections were conducted in the high profile/high visibility areas such as hospitality and catering, cleaning and grounds maintenance services.

4.33 In relation to contract performance monitoring, the ANAO Better Practice Guide *Managing and Developing Contracts* states that:

It is important to focus monitoring activity on key deliverables; very detailed monitoring can be costly and can unduly shift the focus away from achieving contract outcomes.⁹¹

4.34 In each of the three regions, DSG staff have been conducting a large number of joint inspections with contractor representatives each month in order to verify contractor performance. The ANAO acknowledges that prudence would indicate that, until an appropriate level of understanding and assurance had been reached in regard to contractor performance of a GSS contract, regular and extensive joint inspections may be required to verify that

⁹⁰ By contrast, in the former CNNSW region DSG staff nominated the services that were to be inspected in a particular month, and did not give advance notice of which particular sites were to be examined.

⁹¹ ANAO Better Practice Guide—*Developing and Managing Contracts*, ANAO & Department of Finance and Administration, p. 83.

the required quality of service delivery was being achieved. However, effective collaborative arrangements should allow, after this initial period, for a reassessment of the inspection effort required, with the focus being on particular risk areas and occasional random checks on lower risk areas.⁹²

4.35 In interviews with the ANAO, DSG staff at the base level indicated that, often, at least half of a Garrison Support Officer's (GSO's) time was spent on CAPMAN related matters each month. Contractors commented that CAPMAN related work was often almost the whole workload of one of their staff members at each base. Overall, the CAPMAN system involves considerable administrative effort.

4.36 DSG and contractor staff at bases also indicated that compliance assessments were much more straightforward to undertake because they did not require the exercise of subjective judgments. Generally, these staff indicated that they were comfortable assessing compliance measures that were aimed at assessing whether specific contractual requirements were met (with the result being either a pass or fail).

Guidance on CAPMAN commenting standards

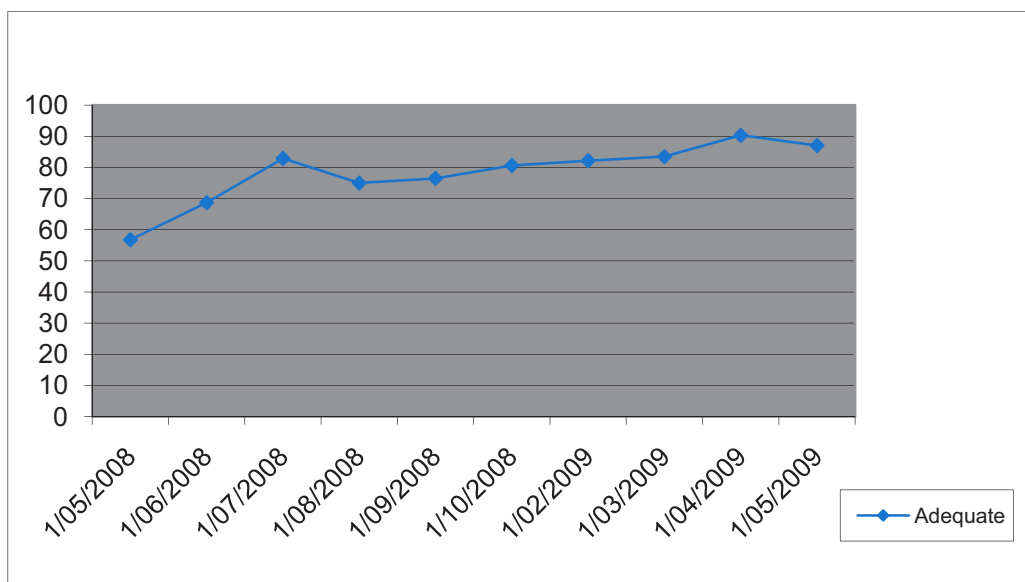
4.37 In May 2008, in recognition of the lack of rationale recorded in support of some ratings recorded in CAPMAN, DPC issued DSG regions with guidance entitled '*Minimum Commentary Standards*' for all performance indicators that do not have supporting criteria.

4.38 Regional GSS supervisors are required to complete a monthly reasonableness check on the data entered into CAPMAN by the contractors and GSOs. This check is focused on approximately 16 performance indicators that do not have supporting criteria. DSG analysis of the information subsequently entered into CAPMAN (see Figure 4.2) indicates some improvement in the qualitative assessment of the data since the issue of the guidance on minimum commenting standards.

⁹² Such an approach would be consistent with the recommendation of a 2001 Defence internal audit which developed a concise better practice model for auditing support contracts. It stated that personnel should apply the '80/20 rule', with a significant proportion of their time to be spent on building relationships (80 per cent) as opposed to checking (20 per cent).

Figure 4.2

Percentage of relevant performance indicators across all regions for which CAPMAN source data is considered adequate—May 2008 to May 2009



Source: Defence documentation

ANAO analysis of performance ratings

4.39 The ANAO examined the CAPMAN ratings applied under the GSS contracts in the three regions visited for the period January 2008 to January 2009. From this examination, the ANAO observed inconsistencies in the ratings applied for what appeared to be similar contractor performance, both across and within regions. For example, in the former CNNSW and WA regions:

- *Access control indicator PI 5051:* The ratings applied ranged from 69 per cent to 100 per cent in the period examined. While clear reasons were provided for ratings under 80 per cent, limited or no clear justification was provided to substantiate the differences in the ratings between 80 and 100 per cent at different times, or at different bases and/or in different regions;⁹³

⁹³ For example, at the same base a score changed from one month to the next with no explanation as to why.

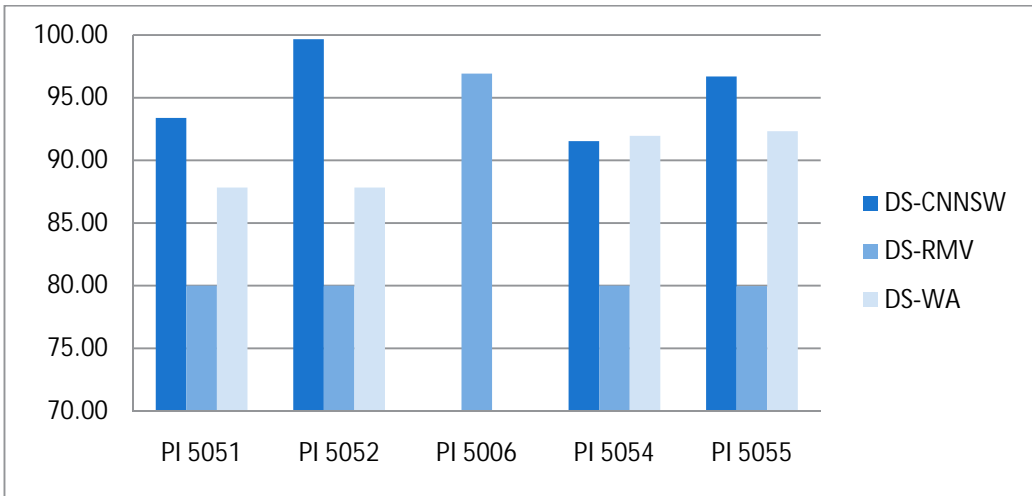
- *Grounds maintenance indicator PI 5456*: The ratings applied ranged from 80 per cent to 100 per cent during the period examined, with limited or no clear justification provided to substantiate the differences in the ratings at different bases and/or in different regions; and
- *Pest and vermin indicator PI 5552*: The ratings applied ranged from 69 per cent to 100 per cent. Reasons were provided for ratings under 80 per cent, however limited or no clear justification was provided to substantiate the differences in the ratings between 80 and 100 per cent at different times, or at different bases and/or in different regions.

4.40 In addition, the ANAO examined the performance ratings given for particular services across the former RMV, WA and CNNSW regions. Figure 4.3 and Figure 4.4 show the differences in the performance scores across two services (access control and stores management) in these regions.⁹⁴ From information in CAPMAN, the ANAO was unable to discern why the identified level of discrepancy in the scores provided to different contractors, within the range 80 to 100, occurred.

⁹⁴ The assessments of performance against the PIs for these two services were selected for illustration because they demonstrate the issue that ANAO identified in relation to ratings in the green traffic light range between 80 and 100 per cent.

Figure 4.3

Average access control performance ratings over the period January 2008 to January 2009

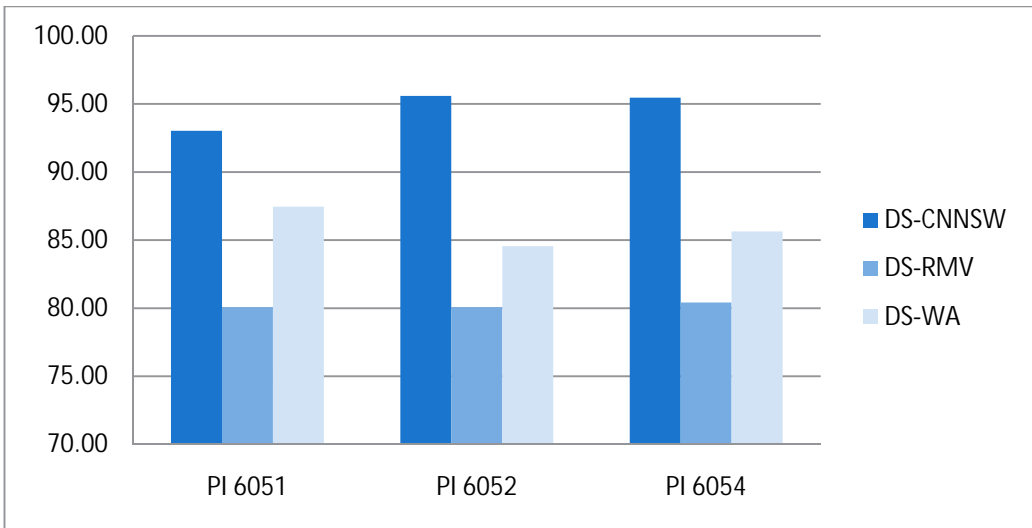


Note: The figure includes all access control PIs for the three regions visited. PI 5006 is only used in the RMV contract.

Source: ANAO analysis

Figure 4.4

Average stores management performance ratings over the period January 2008 to January 2009



Source: ANAO analysis

4.41 These results could, in part, arise because of the scope for different interpretations of available guidance, and the qualitative nature of the assessments being made. From interviews with DSG staff in the three regions and an analysis of performance data, there is evidence that Defence has reasonable assurance that a consistent approach is taken with the performance scoring where the contractor receives a score in the red or amber ranges, that is below AQT. However, this is not the case in relation to scoring within the green traffic light range (generally between a score of 80 and 100). As discussed in the following section, while scores in the green traffic light range mean that performance is assessed as at least meeting AQT, there are different financial outcomes for both contractors and Defence depending on whether or not the contractor receives a score in the AQT range or the MQT range.

Margin impact

4.42 Ratings between 80 and 89 per cent usually provide margin payment at AQT and ratings at 90 per cent and above usually attract a margin payment of Max QT. For example, access control services in the CNNSW region had an average performance rating of 93.4 per cent over the period examined, whereas for the RMV region the average was 80 per cent over the same timeline. The CNNSW contractor would have received a Max QT margin payment whereas the RMV contractor would have received an AQT payment.

4.43 Similarly, for stores management services in the CNNSW region the average performance rating over the period examined was 94.69 per cent, whereas for the RMV region the average over the same timeline was 80.2 per cent. From an analysis of the comments within CAPMAN, the ANAO could not identify evidence of clear differences in the actual performance of the contractor service delivery in the two regions.

4.44 The Garrison Support Services Budget Review of September 2008 stated that 'contractors are consistently achieving a level of margin in between the Average Quality Target and Maximum Quality Target'. That report estimated future budget requirements related to margin payments based on past achievement, and not on a particular level of achievement such as AQT. The impact of margin payments on the GSS budgets is linked to the scoring mechanisms established in the CAPMAN system, which have been demonstrated to be inconsistent across regions. When consistently high performance assessments against a service are evident (greater than AQT), GSS contracts provide that the indicators will be reviewed as the contractor is not

being sufficiently 'stretched'. However, the stretch provision has not been applied in any of the GSS contracts (see paragraph 4.21).

Recommendation No.4

4.45 The ANAO recommends that Defence reviews the Performance Management Framework and Risk Reward Remuneration Model relating to Garrison Support Services with a view to:

- (a) remedying inconsistencies in the way the different DSG regions approach performance measurement and the effect of this on both the margin outcome for individual contractors and the cost of GSS to Defence; and
- (b) better supporting the achievement of value for money as well as quality outcomes, through addressing weaknesses in the current Risk Reward Remuneration Model and its application by Defence in relation to maximum quality targets.

Defence's summary response

4.46 Defence *agrees* with the recommendation and its summary response is:

Defence is in the process of engaging an external consultant to review the Performance Management Framework and Risk Reward Remuneration Model.

The key area of the review is the Risk Reward Remuneration Model; changes to the Risk Reward Remuneration Model will set the minimum information requirements needed from the Performance Management Framework. The Performance Management Framework will then be redeveloped to meet the Risk Reward Remuneration Model's minimum information needs.

4.47 See Appendix 1 for Defence's detailed response to the recommendation.

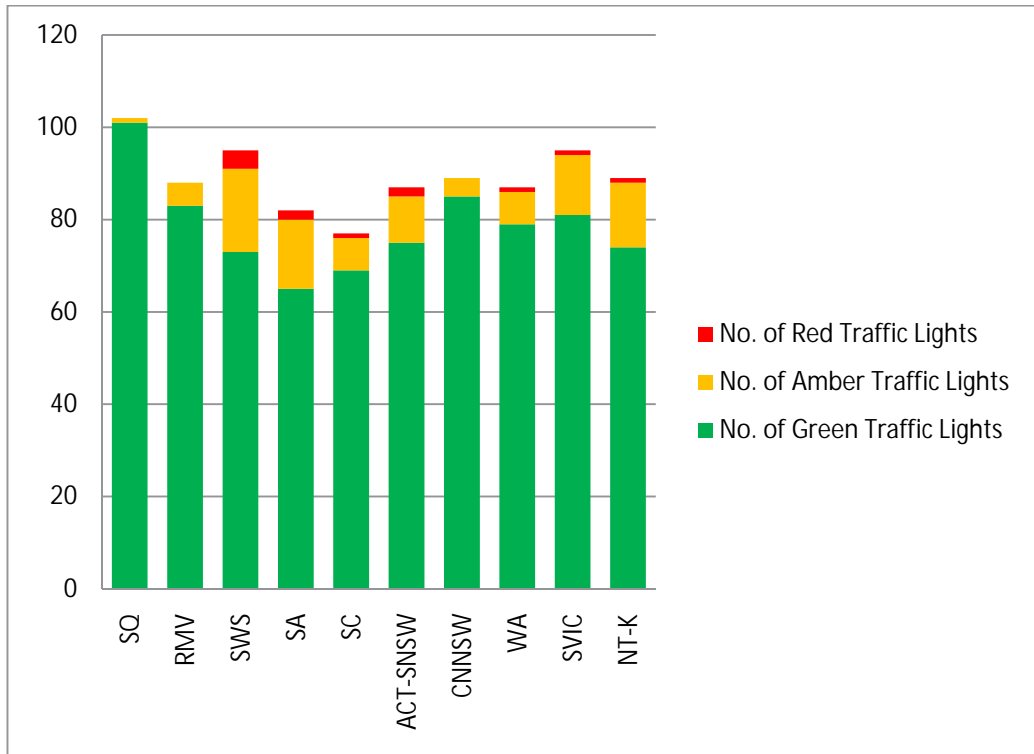
National reporting and oversight of GSS performance

4.48 A CAPMAN traffic light report is provided to the DSG Executive on a monthly basis. The report is compiled from a number of spreadsheets and provides a single page report (a coloured pictograph of the status of each indicator, across each service and region). The report also provides a limited commentary on the issues that result in CAPMAN Red/Amber results across all the contracts.

4.49 Figure 4.5 and Figure 4.6 summarise CAPMAN records relating to contractors in the 10 former DSG regions where GSS contracts were in operation during 2008.⁹⁵ In this analysis, the ANAO added the number of green, amber and red PIs in each region over the six month period. For CIs, the results are either green or red (pass or fail).

Figure 4.5

GSS CAPMAN Performance Indicator scoring frequency—July to December 2008



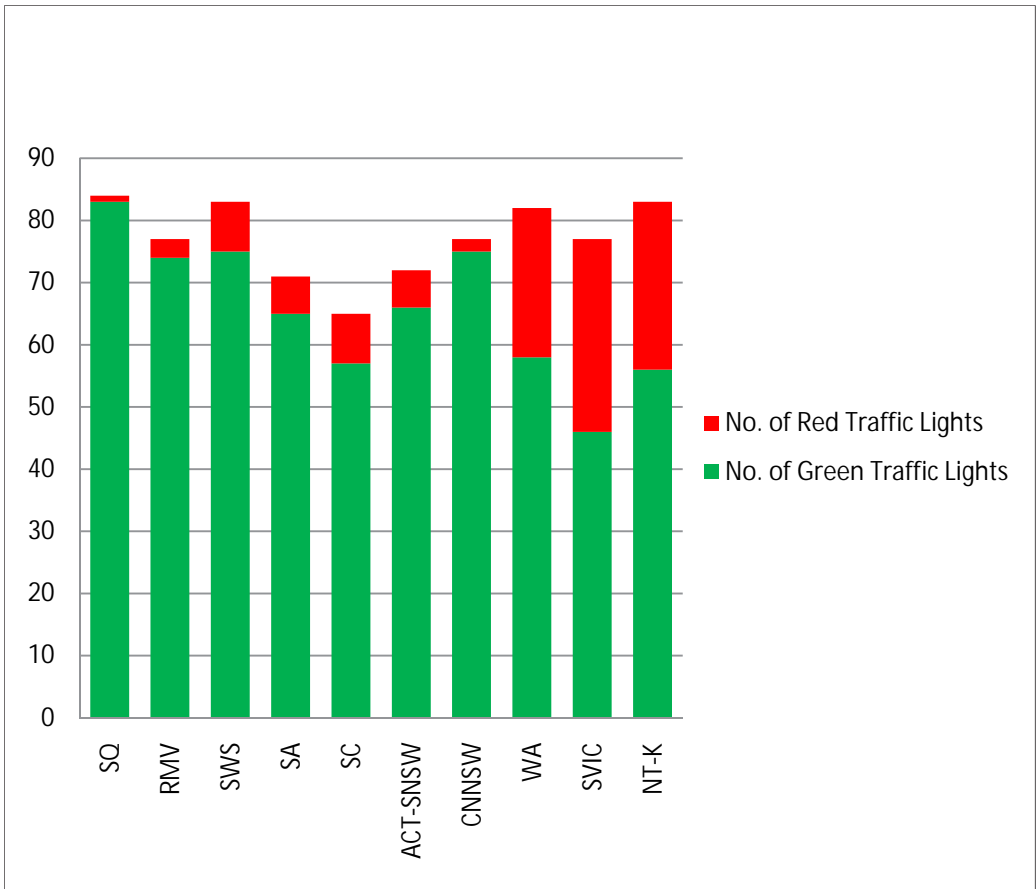
Note: South Queensland (SQ), Riverina Murray Valley (RMV), Sydney West/South (SWS), South Australia (SA), Sydney Central (SC), ACT/Southern NSW (ACT-SNSW), Central/Northern NSW (CNNSW), Western Australia (WA), Southern Victoria (SVIC), Northern Territory/Kimberley (NT-K).

Source: ANAO analysis

⁹⁵ This analysis excludes the then Tasmanian and NQ Regions for which Base Services tenders were being considered and negotiated during this six month period. This analysis is based on the regional structure before 1 July 2009; see paragraph 1.16 for details of the new regional structure.

Figure 4.6

GSS CAPMAN Compliance Indicator scoring frequency—July to December 2008



Note: South Queensland (SQ), Riverina Murray Valley (RMV), Sydney West/South (SWS), South Australia (SA), Sydney Central (SC), ACT/Southern NSW (ACT-SNSW), Central/Northern NSW (CNNSW), Western Australia (WA), Southern Victoria (SVIC), Northern Territory/Kimberley (NT-K).

Source: ANAO analysis

4.50 The analysis summarised in Figure 4.5 supports the view that overall contractors are providing the required services, although based on the analysis summarised in Figure 4.6 not all CI contractual requirements are being met. CAPMAN reporting indicated that instances of non compliance for CIs have arisen where, for example, specific contractor staff may not have the required qualifications, or the contractor may not have the required environmental plan

in place.⁹⁶ From the information within CAPMAN, the individual instances of non compliance did not appear to have a significant impact on service delivery. The result demonstrated in Figure 4.5, where indicators are predominantly green, is consistent with the feedback provided by the ADF users at the bases visited as part of the audit. Service user representatives interviewed by the ANAO indicated that services were being delivered satisfactorily.

Strategic performance reviews

4.51 GSS contracts provide for strategic performance reviews to be undertaken at the end of year two of the contract life, with subsequent reviews undertaken at two yearly intervals as required. Annual reports are considered as part of any strategic performance review, with quarterly and monthly reports also considered where appropriate. Strategic performance reviews were being undertaken, or about to be undertaken, at the three regions in the ANAO's sample for this audit.

4.52 DPC staff provide guidance and assistance to regional DSG staff in carrying out strategic performance reviews.

Strategic performance indicators

4.53 The strategic performance review requirements are outlined in the GSS contracts. The strategic performance indicators that are considered as part of these reviews are set out below:

- level of engagement of Small to Medium Enterprises;
- contract service delivery performance;
- contract compliance performance;
- health of the collaborative contract relationship;

⁹⁶ Defence advised that the former NT-K region's incidence of fail scores for CIs were higher during the due diligence period which ran from commencement of the relevant GSS contract in May 2008 until January 2009. During due diligence, it is common for higher rates of fail scores against CIs as the contractor settles into the new arrangement. Since the end of the due diligence period, the incidence of fail scores for CIs in NT-K have fallen considerably. The high incidence of fail scores for CIs in the former SVIC region related mainly to the absence of an approved chemicals register and delays in its approval by DSG. A significant number of fail scores for CIs in the WA region related to contractor staff not holding competencies and qualifications proposed and accepted in order to deliver the service, and/or security clearances. The high incidence of fail scores for CIs in the WA region is being considered as part of the strategic performance review process currently being conducted.

- corporate performance on matters such as occupational health and safety and environmental management;
- achievement of continuous improvement and innovation;
- customer satisfaction; and
- contract financial outcome for the contractor.

Review process

4.54 Examinations and data collections undertaken as part of the strategic performance review process include:

- a consultant's examination of the contractors' systems underlying their reporting against PIs and CIs;
- a customer (service user) survey;
- the completion by the contractor of a strategic performance assessment, providing data against detailed elements of the strategic performance indicators;
- the conduct of an online survey of DSG and contractor staff; and
- DSG gathers data on matters such as the process and timeframes for contract amendments, and the extent of contract disputes.

4.55 The ANAO interviewed DSG staff within the three regions in the audit sample who were responsible for managing the strategic performance reviews. These staff commented that the reviews are time consuming, and that on occasions contractors struggle to provide the level of supporting information being sought by DSG.⁹⁷ To be able to respond to the requirements of the strategic performance review as specified under the GSS contract, it is important that contractors have in place the necessary systems to gather the required performance data and ensure its accuracy over the course of the contract. Defence informed the ANAO that the annual report to be provided by contractors should include information against the strategic performance indicators and this should facilitate preparation of the response to the strategic

⁹⁷ In the former CNNSW region, DSG staff informed the ANAO that the contractor had commented that they were not happy that DSG was raising matters covered in the original Tender Deliverable Requirements (TDRs) (this can relate to how the contractor proposes to deliver particular services) within the strategic performance review context. The contractor contended that if it was meeting outcomes it should be acceptable, even if they were not meeting a particular TDR.

review report. Defence indicated that it is also considering whether quarterly reporting on the strategic indicators should be mandated.

4.56 From discussions with DPC, the ANAO observed that Defence has found the strategic performance reviews undertaken of existing contracts provided useful input to Defence's decision making regarding the extension of contracts. These reviews contain evidence regarding the strengths and weaknesses of particular contractors, and provide a basis for putting in place remedial processes where necessary. At the time of audit fieldwork, DPC advised that all GSS contracts considered up to that time had received contract extensions following consideration of strategic performance reviews.

4.57 In October 2009, Defence informed the ANAO that the 2009 RMV strategic review has been completed. Defence noted that a range of minor issues were identified which required action and resolution by the contractor and by Defence, with some to be addressed jointly. Following confirmation that the contractor has resolved its actions, an extension to the contract will be offered in accordance with the contract. Defence informed the ANAO that the 2009 WA strategic review has been substantially completed, although there are a number of actions/recommendations to be addressed by the contractor. Defence proposes to review the contractor's progress on these actions/recommendations in December 2009, prior to making a decision on the extension of the contract. Defence further informed the ANAO that the 2009 strategic review for CNNSW is still in progress.

5. Administration of GSS payments and contract amendments

This chapter discusses the expenditure related to GSS, including costs of administering GSS contracts, in the three regions in the audit sample. It also outlines: the key savings initiatives identified by the 2008 Defence GSS Budget Management Review; the results of the ANAO's examination of contract amendments and payments arrangements in these three regions; and describes the results of Defence's analysis of whether savings, originally expected when GSS was introduced, have been maintained over time.

Introduction

5.1 The ANAO examined a range of issues related to the administration of GSS contracts. The examination of contract administration in the three regions visited—RMV, WA and CNNSW—helped draw out particular issues related to contract amendments, payments and resource management generally.

5.2 Matters considered by the ANAO included:

- expenditure related to GSS in the sample of three regions examined as part of the audit, including administration costs associated with GSS contracts;
- the 2008 Defence GSS Budget Management Review;
- contract amendments processes in the three regions;
- payment arrangements in the regions; and
- available evidence about the extent to which expected savings when GSS contracts were first entered into have been realised and maintained.

Expenditure related to GSS

5.3 Within GSS contracts there are a number of different categories of services provided to Defence.⁹⁸ These categories are 'scheduled', 'variable', 'requested' and 'additional' services. Each of these service types is also subject

⁹⁸ Referred to as service types by Defence.

to an annual Price Variation Formula (PVF) which is set out in each contract. Details of what is included in each of these service types are set out in Appendix 6.

5.4 In respect of the 'scheduled', 'variable' and 'requested' service types, the contract provides that contractors will receive a performance margin based on their performance in delivering the services. The amount of the margin will vary depending on the individual contract and the levels of margin proposed by the successful tenderer for that contract.

5.5 Table 5.1 summarises the payments made by service type under the GSS contracts in the three regions in the ANAO's sample for the 12 months 1 March 2008 to 28 February 2009.

Table 5.1

Payments made by service type – 1 March 2008 to 28 February 2009

| Region | Scheduled (\$m) | Variable (\$m) | Requested (\$m) | Additional (\$m) | Total (\$m) |
|--------|-----------------|----------------|-----------------|------------------|-------------|
| RMV | 34.501 | 19.643 | 3.612 | 0.055 | 57.812 |
| WA | 28.845 | 4.161 | 6.550 | 0 | 39.555 |
| CNNSW | 12.126 | 5.215 | 2.497 | 0.001 | 19.839 |

Note: Figures may not add due to rounding.

Source: ANAO analysis of Defence data

5.6 Within the total payments for each service type made to each of the three contractors, there are margin payments. The margin payments result from the operation of the Risk Reward Remuneration Model which is illustrated in Chapter 4 (paragraphs 4.15 to 4.19). The average margin applied in the former RMV, WA and CNNSW regions in the period 1 March 2008 to 28 February 2009 was 3.99 per cent, 3.76 per cent and 5.44 per cent respectively.

5.7 The categorisation of services into different types under the GSS contracts has implications for the financial administration of these contracts. For example, changes to 'scheduled' services, other than straightforward changes such as whether a facility is to be used or not, often require contract amendments which involve additional administrative effort.

5.8 'Requested' services involve the greatest ongoing administrative effort because of the need to process a large number of requests for particular services that often involve small costs. The 'survey and quote' method is applied to 'requested' services and this involves an administrative cost for both

Defence and the contractor.⁹⁹ As well as the 'requested' services that are paid for by DSG (and therefore appear in Table 5.1), at some of the bases the ANAO visited there was a strong emphasis on having the ADF (or civilian) users pay for particular 'requested' services (in which case there are administrative costs for the contractor, DSG and the ADF).

Costs associated with the administration of GSS contracts

5.9 Defence advised that it did not hold accurate costing data related to the cost of administration of GSS contracts. It informed the ANAO that the best information available related to product costing undertaken by DSG at a base and region level. Based on information provided by Defence, the total product cost related to GSS contracts in 2008–09 is estimated to be \$13.3 million. However, this estimate does not include the full costs associated with the administration of GSS contracts. In particular:

- these costs do not include costs of staff in DSG National Office who play a role in the ongoing administration, policy and guidance arrangements related to GSS;
- the costs at the base and region level provided by Defence relate only to staff who are directly involved in contract management, and may not include the full impact of GSS on related areas such as financial administration; and
- product costing arrangements do not include a full attribution of overheads related to staff undertaking GSS contract administration at the base and regional level.

5.10 Defence advised the ANAO that it is seeking to improve the available information related to systems and costing. As part of these improvements, Defence is making changes to its chart of accounts to enhance data and obtain greater visibility of costs. Defence noted that having reliable information related to GSS contract administration will be important in the context of efficiencies being sought generally in the management of DSG, as well as

⁹⁹ Under the 'survey and quote' method, DSG seeks a quote from the contractor to provide extra services that were not specifically stipulated within the contract. However, under the contract it is expected that the contractor would apply rates from the contract's pricing schedule where applicable. It is open to DSG to also seek quotes from other potential providers for the provision of these services, if it wishes. Any quotes need to be considered by DSG on value for money grounds.

proposals to change the way GSS contracts are administered (see discussion in Chapter 1, paragraphs 1.16 to 1.19).

GSS Budget Management Review

5.11 For 2008–09, Defence was subject to efficiency dividends and other savings initiatives that required savings in GSS expenditure (details are outlined in Appendix 4) that helped maintain pressure on the GSS budget. In view of increases in GSS expenditure in past years (a 26 per cent increase being recorded from 2005–06 to 2008–09) and the need to meet expenditure targets, in 2008 Defence undertook a review of GSS contract expenditure.

5.12 According to the report of the 2008 Defence GSS Budget Management Review:

Consolidated and standard reporting of GSS expenditure at any disaggregated level has not been available. Budgeting for GSS expenditure and reporting of actual results against budget in previous years has been aggregated at a level that has provided only a minimal level of transparency. This level of budget management and reporting has not allowed regions and [Defence Support Operations] DSO to correctly identify significant reasons for variances in expenditure against budget.

An inability to more effectively articulate variances, particularly expenditure increases has created the perception that GSS is over funded, and related expenditure growth is not being effectively managed.¹⁰⁰

5.13 Defence's internal budget review team undertook a 'zero base' budget review in the 2008 GSS Budget Management Review to formulate the 2008–09 budget. This was a 'bottom up' review that examined all sources of contract expenditure, rather than funding the contracts based on data from previous years. Additionally, Defence considers that recent further refinement of GSS information systems has provided DSG with more transparency over detailed GSS costings.

¹⁰⁰ Department of Defence (2008), *Garrison Support Services Budget Management Review*, 15 September, p. 12.

5.14 The Review recommended a number of initiatives to respond to the need to identify savings, including:

- having a 'Sunset Clause' for all ongoing work orders (for 'requested' services) that are not formally progressed to contract amendment orders to avoid user expectations of unfunded scope increases;
- enhancing regional GSS contract reporting to allow DSG National Office to better understand overall consumption patterns and recognise emerging budget pressures;
- changing services from 'variable' to 'scheduled' where differing activity levels are not affecting cost;
- where 'requested' services are provided on an ongoing basis and are routinely recovered from the user, requesting a funding transfer to the GSS budget for these services to reduce ongoing administrative cost; and
- undertaking a further review of the available data on 'requested' and 'additional' services.¹⁰¹

Contract amendments

5.15 Any proposed contract variation needs to be assessed:

- in terms of its suitability to appropriately address the relevant Defence requirement or contractual issue;
- for compliance with Australian Government legislative and policy requirements; and
- to ensure that value for money is maintained and that there is no unexpected transfer of risk back to Defence.

5.16 During the life of a GSS contract, amendments may be driven by:

- a detailed review of the contract at commencement where the scope of works are checked (referred to as the due diligence period);
- changes to Defence's operational capability requirements; and
- the addition or removal of services within regions.

¹⁰¹ Department of Defence (2008), *Garrison Support Services Budget Management Review*, 15 September, pp. 5-6.

5.17 The audit examined Defence's GSS contract amendment arrangements, including: contractual provisions; available guidance to contract authorities and regions; adherence to contractual procedures; processes to assess/support the reasons for proposed variations; whether sufficient documentation detailing variations and their potential impact (including on contract price) are maintained; whether contract variations are appropriately authorised; and whether Defence has met reporting requirements (such as updating the Department's contract registers and including details in AusTender).¹⁰²

Contract Provisions

5.18 Each of the GSS contracts contains provisions to vary or amend the contracts and stipulates the terms, conditions and authority under which the contract can be altered. Figure 5.1 outlines this process.¹⁰³

Figure 5.1

Key stages in the GSS contract amendment process

| |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p>Either the contractor or Defence identifies or initiates the need for a change to the contract. When a change requirement arises, Defence may raise a Contract Amendment Request (CAR) with the contractor which sets out details of the proposed amendment.</p> <p>On receipt of a CAR from Defence, the contractor is required to raise a Contract Amendment Proposal (CAP) setting out any material effect and adjustments to the Pricing Schedule and Statement of Work.</p> <p>The contract specifies that the contractor has 14 days to respond to a CAR from Defence or if the contractor identifies that a work direction issued should potentially form a change to the scope of the contract.</p> <p>The contractor may also raise a CAP (without first receiving a CAR) if they identify a change requirement.</p> |
| <p>A Contract Amendment Order (CAO), setting out the proposed adjustments to the Pricing Schedule and Statement of Work, is developed on the basis of a CAP. Alternatively, at any time during the contract Defence may issue a Contract Amendment Order (CAO).</p> |
| <p>Approval is required by the Contract Authority (the Regional Manager) for potential contract amendments involving expenditure of less than \$10 000 per annum, and by the Head of the Defence Support Operations Division when over \$10 000 per annum.</p> <p>Approval of the contract amendment is to be notified to the contractor and the contract amended accordingly.</p> |

Source: ANAO analysis of GSS contracts

¹⁰² AusTender is the Australian Government's procurement information system which provides centralised publication of Australian Government business opportunities, annual procurement plans, multi-use lists and contracts awarded.

¹⁰³ These provisions are usually contained in each of the Garrison Support Services Contracts' Terms and Conditions, under *Contract Amendments*.

Guidance

5.19 GSS contracts outline the information to be included in any contract amendment such as material effect, adjustment to pricing and the effect of any contract amendment on service delivery. The *Defence Procurement Policy Manual* (DPPM) details Defence's specific procedures for contract amendments.¹⁰⁴

5.20 The guidance contained in both the GSS Contracts and the DPPM comprehensively describe the processes and legal requirements for GSS contract amendments. Regional Contract Governance Plans also provide local guidance and/or standard operating procedures to assist contractor and Defence staff with the contract amendment process. Defence informed the ANAO that the National Governance Framework that is currently being developed in support of contract hubs (refer paragraph 3.8 in Chapter 3) will include a section on 'critical processes'. This section will map out critical contract processes, including contract amendments, and require all hubs to comply with these processes.

Examination of contract amendment records

5.21 As part of the audit, the ANAO undertook an examination of available contract amendment records for the three DSG regions in our sample.¹⁰⁵

Record keeping

5.22 Reasons for contact variations should be clearly documented and contract variations should be undertaken in line with the procedures set out in the GSS contracts and the DPPM. There was evidence of inconsistencies in the process undertaken and documentation prepared and retained in each region examined.

5.23 The ANAO reviewed the CAP, CAR, and CAO records held in each region (both hard copy and electronic). DSG staff in each region use spreadsheets to record and monitor the contract amendment process. A detailed examination was undertaken of 10 contract amendment processes in each region. In the former CNNSW region, 90 per cent of the records sampled were complete, whereas none of the records examined in the former RMV or

¹⁰⁴ Defence Material Organisation *Defence Procurement Policy Manual* (2006), Section 6, Chapter 6.7 and Section 1 Chapter 1.4.

¹⁰⁵ These were the RMV, CNNSW and WA regions.

WA regions were complete. The data available within the DSG regional offices did not consistently record initial or final costings for contract amendments and, accordingly, the material effect of the amendments could not be determined for any of the regions examined.

5.24 In particular, the ANAO identified weaknesses in documentation such as:

- incomplete or missing CARs and/or CAPs. For example, limited or no information was provided supporting the reason and impact of the variation, or the documentation was not signed;
- incomplete or missing business cases and/or risk assessments;
- incomplete or missing documentation for CARs and/or CAPs involving expenditure of over \$10 000 per annum;¹⁰⁶
- incomplete CAOs (including detail of the required changes, dates of effect, impact and signatures); and
- a lack of evidence that the contractor had been appropriately informed of and/or accepted the CAO.

5.25 Defence Support Operations (DSO) advised the ANAO that it has been monitoring and approving CAPs and/or CARs (involving expenditure of over \$10 000 per annum) since April 2008. However, the ANAO's review of a sample of CAPs and CARs held by DSO identified similar issues with the completeness of these records including:

- incomplete or missing documentation for CARs and/or CAPs; and
- incomplete or missing business cases and/or risk assessments.

Approvals

5.26 The DPPM identifies that the following approvals are required for contract amendments:

- proposal approver (under the DPPM, this approver exercises the responsibilities under Regulation 9 of *Financial Management and Accountability Regulations 1997*);
- procurement approver;

¹⁰⁶ Including copies of the 'DS-Regional justification for contract change request over 10K per year' forms.

- contract approver;¹⁰⁷
- contract signatory;
- Regulation 10 (of the *Financial Management and Accountability Regulations 1997*) approval where required; and
- additional provisions as decided at the local level—in the case of GSS, approval from the Head of DSO for CAOs involving expenditure of over \$10 000 per year.¹⁰⁸

5.27 The contract amendment records examined by ANAO (with the exception of 90 per cent of those examined in CNNSW) lacked completed documentation. In RMV and WA the documentation held was generally insufficient to gain assurance that the required approvals had been obtained.

Timeliness

5.28 Any proposed contract amendment may affect the existing terms and conditions of the contracts, the allocation of risks between the Commonwealth and the contractor, the contract price and/or service delivery. Accordingly, it is important that Defence ensure that contract amendment processes are conducted in a timely and effective way.

5.29 Other than the contractual requirement for the contractor to respond to a CAR within 14 days, there are no targets for the time in which DSG is to carry out its responsibilities for contract amendments. Monitoring and reporting of contractor and DSG timeliness in processing contract amendments was not undertaken by the three regions in the ANAO's sample.

5.30 Analysis of the timeliness of the CAO process in the regions audited showed that the CAO processes took, on average, approximately eight months to complete.

5.31 Table 5.2 details the numbers of contract amendment processes commenced for the extant GSS contract in each region in the ANAO audit sample and the average time taken in those regions. As at the time of audit fieldwork, Table 5.2 covered the entire period that contract amendment records were maintained by the relevant DSG regions in their contract

¹⁰⁷ According to the DPPM, a delegate can undertake up to two of the proposal, procurement and contract approvals.

¹⁰⁸ Defence Material Organisation (2006) *Defence Procurement Policy Manual*, Section 1, Chapter 1.4, p. 1.4.1.

registers. Table 5.2 also indicates there were a high percentage of outstanding amendments in WA and CNNSW.

Table 5.2

Timeliness of the contract amendment process

| | Western Australia | Central Northern NSW | Riverina Murray Valley |
|--------------------------------------------------------------------|-------------------|----------------------|------------------------|
| Total number of contract amendments commenced | 78 ^A | 50 ^B | 314 ^C |
| Contract amendments completed (percentage of total) | 21.8 | 38 | 79 |
| Contract amendments outstanding (percentage of total) | 65.4 | 36 | 3.8 |
| Contract amendments cancelled (percentage of total) | 12.8 | 26 | 15.9 |
| Average time taken for contract amendments (months) ^(D) | 8.9 | 8.4 | 7.2 |

- Notes:
- (A) The contract amendment register records processes initiated from 9 March 2007 to 25 February 2009.
 - (B) The contract amendment register records processes initiated from 11 December 2006 to 12 March 2009.
 - (C) The contract amendment register records processes initiated from 9 March 2007 to 16 December 2008.
 - (D) Represents contract amendments completed, outstanding or cancelled (where timelines were available).

Source: ANAO analysis of data held by DSG regions

Financial Impact

5.32 Where Defence or the contractor identifies that a change to service level requirements is needed, a Work Direction is initiated (through the Defence Estate Management System (DEMS)) to ensure that service provision commences. If a Work Direction represents an ongoing change to a service level, it may prompt the commencement of the contract amendment process.

5.33 Generally, Work Directions are generated on a month by month basis until the contract amendment process is completed.¹⁰⁹ The ANAO identified that DSG regional staff did not monitor the cost of ongoing Work Directions (that is the ongoing cost of providing the additional service) prior to the finalisation of each contract amendment process.

5.34 The lack of monitoring of the proportion of GSS costs that relate to Work Directions has reduced the visibility of the costs, and increased the risk that Defence may have incurred higher than necessary costs during the time taken to complete the amendment process. For example, pending the approval of a contract amendment (and therefore an assured ongoing payment), contractors frequently use temporary staff to provide services required under a Work Direction. As the cost for these staff is generally higher than ongoing staff, this may result in the cost of the service provision being higher than if the work was undertaken by the contractor's full-time staff.

5.35 As a result of the 2008 GSS Budget Management Review, Defence has undertaken initial development of an electronic 'workflow' contract amendment process. In addition, a test plan has been developed for regional testing which is dependent on achievement of planned DSO organisational reform (the re-organisation of regions and the introduction of contractor hubs). Defence intends to implement the electronic 'workflow' contract admendment system following regional testing.

Recommendation No.5

5.36 The ANAO recommends that Defence:

- (a) in consultation with GSS/Base Services contractors, takes steps to determine appropriate timeframe targets for both the contractor and Defence in relation to their respective responsibilities for contract amendments;
- (b) promulgates specific guidance on processing GSS contract amendments to relevant staff; and
- (c) introduces management and reporting mechanisms to promote adherence to this guidance and timeframe targets.

¹⁰⁹ In some cases there were automatic monthly extensions of the Work Direction. This required the Work Direction to be cancelled when the contract amendment came into effect.

Defence's summary response

5.37 Defence *agrees* with the recommendation and its summary response is:

Defence has already developed National Contract Directive and Hub-level Contract Governance Plan templates and these have been provided to GSS Contractors for consideration and comment. These documents include proposed timeframes, minimum content requirements, processes, mandated templates, costing and assessment methodologies and management and reporting requirements.

In addition, Standard Operating Procedures have also been developed to support the National Contract Governance Framework.

5.38 See Appendix 1 for Defence's detailed response to the recommendation.

Reporting of contracts and variations

5.39 There are two external reporting requirements for GSS contracts. A Senate Order requires each Australian Government agency (as defined by the *Financial Management and Accountability Act 1997*) to publish aspects of its contracts with a value of \$100 000 or more on its Internet homepage.¹¹⁰ Defence publishes this information online in the Department's *Interim Defence Contract Register* (IDCR).¹¹¹ The Department of Defence Chief Executive Instructions also provide:

Responsibility for inclusion of the required information in the Interim Defence Contracts Register rests with the Contract Approver.¹¹²

¹¹⁰ The requirements of the Senate Order for Departmental and Agency contracts underline the principle that the Parliament's and the public's access to information on government programs and services should not be prevented, or otherwise restricted, through the use of commercial contractual arrangements, unless there is a sound reason to do so. Amongst other things, agencies' lists of contracts must indicate whether each contract contains provisions requiring the parties to maintain confidentiality of any of its provisions or whether there are any other requirements of confidentiality.

¹¹¹ Department of Defence Internet, Defence Material Organisation, *Reporting Defence and DMO Contracts* <http://www.defence.gov.au/dmo/id/cic_contracts/cic_contracts.cfm> [accessed 6 May 2009].

¹¹² Department of Defence, *Chief Executive Instruction*, CEI 2.1, Edition 4, AL3 December 2005. p. 9.

5.40 In addition, agencies must report on the AusTender website all contracts including amendments valued above \$10 000.¹¹³

5.41 The ANAO examined Defence's compliance with the Senate Order and AusTender reporting requirements in relation to the GSS contracts in the three regions visited (the former RMV, WA and CNNSW regions) and the Base Services contract for North Queensland. From the information available, the ANAO was unable to verify that the reporting of GSS contracts and associated amendments had occurred in accordance with the Senate Order and AusTender requirements. Defence informed the ANAO that it recognises that there are weaknesses in its administrative arrangements related to Senate Order and AusTender reporting, and proposes to implement procedures to strengthen these processes.¹¹⁴ In October 2009, Defence indicated that improved procedures will be implemented by 30 November 2009.

Payment arrangements

5.42 The contractor receives two types of payments for GSS work: a payment for the cost of services delivered across the month, and a margin payment related to the Risk Reward Remuneration Model under the contract. Each GSS contract contains a cost schedule that establishes the monthly cost of scheduled services and also contains labour/task rates used to calculate any variable or additional work (for example hourly rates for hospitality personnel; daily fees for emptying different size bins). The contractor enters monthly activity data into DEMS, which contains the contract cost schedules. DSG

¹¹³ Agencies must report on AusTender all procurement contracts, including standing offer arrangements and amendments to these contracts which meet the contract reporting criteria. The contract reporting criteria include:

- the instrument to be reported is a Commonwealth contract, agency agreement or standing offer arrangement or amendment thereto; and
- the instrument meets the relevant contract reporting value. That is, the value of the Commonwealth contract (including GST where applicable), agency agreement, standing offer arrangement or amendment thereto is, for FMA Act agencies, \$10 000 or above.

Department of Finance and Deregulation (2008) *Commonwealth Procurement Guidelines*, p. 21.

¹¹⁴ Figure 4.1 of ANAO Audit Report No. 27 2005–06, *Reporting of Expenditure on Consultants*, includes excerpts from ANAO reports on compliance with the Senate Order for Department and Agency Contracts. These excerpts indicate that improvement in the reporting of Senate Order matters had been promised for many years. ANAO Audit Report No.7, 2007–08, *The Senate Order for Departmental and Agency Contracts (Calendar Year 2006 Compliance)* included further consideration of Defence's compliance with the Senate Order. In that report Defence advised the ANAO that it 'will fully comply with Finance guidelines for reporting contracts according to the Senate Order by 30 September 2007'. Based on the four contracts examined as part of this audit, this timeline has not been met.

personnel at the regional level verify that the services in DEMS have been provided, and the contractor will then produce a monthly invoice.

5.43 Margin payments are paid as a percentage of the cost of services. The payable margin varies according to the performance score given to each service in CAPMAN (performance measurement is discussed in paragraphs 4.8 to 4.44 of Chapter 4).

5.44 Each month, the contractor is automatically paid 'target' margin (the equivalent of AQT scores) for all services. Every three months, a margin adjustment is made whereby Defence calculates the average score in each service for each of the three months and makes an adjustment accordingly—scores lower than target margin result in negative adjustments, and scores above result in positive adjustments.

Review of payments

5.45 The ANAO selected four months (April 2008, July 2008, October 2008 and January 2009) and undertook payment testing for each month (each incorporated margin adjustments). The ANAO undertook a check to ensure that amounts recorded in DEMS for each type of service (scheduled, variable, requested/additional) matched the invoiced amounts; the performance margins had been correctly recorded in the CAPMAN system; and payments were made in a timely manner. This testing did not extend to checking that each billed item was delivered.

5.46 The ANAO's testing indicated that in the regions visited the payment process generally operated satisfactorily, with correct amounts being paid. For WA, RMV and CNNSW, payments were made within the agreed payment terms (30 days).¹¹⁵ However in the RMV region, margin adjustment payments were being processed one month later on average than margin adjustment payments in WA and CNNSW, with the fourth quarter 2008 adjustment still not settled over two months after the other regions had been paid. RMV informed the ANAO that this was because of technical issues with DEMS and a lack of personnel.¹¹⁶

¹¹⁵ Defence Chief Executive Instruction 2.4 (Payment of Accounts) states that generally Defence should pay accounts not exceeding 30 days after a correctly rendered invoice. 30 days is the payment terms used for GSS payments.

¹¹⁶ The RMV region takes a different approach to margin adjustment payment claims than other regions. Rather than include the adjusted margin with a monthly invoice every quarter, RMV creates a separate payment claim to deal with adjustments. The RMV region considers that this makes margin payments more transparent, and also reduces the potential size of a combined invoice.

Accounting for cash collected by contractors on base

5.47 Cash can be paid for casual meals, light meals and guest meals at graduation parades. This money is collected by the contractor. This arrangement is based on Section 12 of the *Financial Management and Accountability Act 1997* (FMA Act), which states that a properly authorised non-Commonwealth official may receipt or keep custody of public money.¹¹⁷ FMA Act section 12 agreements had been established with each contractor in the regions visited.

5.48 Defence has established an arrangement whereby the contractor collects this money and returns it to Defence on a monthly basis. The contractor collects this money daily and banks it weekly (except in the case of money received for guest meals at graduation parades, which is banked the next working day). The contractor provides DSG activity data for the money collected, which forms the basis for an invoice that DSG issues to the contractor. For example, after the end of the month, in the RMV region DSG regional personnel obtain activity data on cash collected during the month and, once an invoice is raised, the contractor has seven days to pay. Once or twice a year DSG regional personnel will validate the contractor's activity data. DSG base personnel are provided with the summary data as well, and may undertake their own checks. According to the 2007–08 Defence Portfolio Budget Statements, approximately \$3 million was received from casual meals purchased in Defence messes in 2005–06.¹¹⁸

Members Required in Uniform

5.49 The concept of Members Required in Uniform (MRU) has been implemented in GSS contracts to allow certain service personnel to maintain their skills by operating in areas covered by the GSS contracts. The contractors are required to provide positions for a number of service personnel as part of their contractual obligations. The main example of MRUs in GSS contracts are chefs, with most from Navy. Chefs work in the kitchens that the contractors manage, with the contractor still responsible for food service delivery. The standard arrangement is for the contractor to be paid for the services provided and to then provide a rebate for the MRU element to Defence every month.

¹¹⁷ These arrangements must serve the Commonwealth's interest and achieve the most efficient and effective transmission of the relevant public money to an 'official account'.

¹¹⁸ Department of Defence (2007) *Defence Portfolio Budget Statements 2007–08*, p. 60.

The contractor is paid for managing MRU personnel. In the regions the ANAO visited, MRU were operating at HMAS Stirling in WA and RAAF Williamtown in CNNSW.

5.50 Having ADF personnel work under direct supervision of a GSS contractor creates some tension.¹¹⁹ Defence has evidence that MRU members understand they work for the contractor, but do not approve of it and may not 'care' about contractor management. In addition, data within the CAPMAN system for 2007–08 indicated that Navy personnel's satisfaction in WA with MRU arrangements did not meet the agreed quality target for nine of the 12 months.

5.51 At HMAS Stirling in the WA region, there was uncertainty over the process for use of MRU personnel and their competing responsibilities to the ADF and the contractor. Matters had not been assisted by a high turnover of contractor hospitality and catering managers in WA. Navy personnel interviewed by the ANAO about MRU in WA indicated that it would be beneficial to remove hospitality and catering from GSS contracts where there are MRU personnel. At Williamtown in the CNNSW region, RAAF indicated that in future it may want to change its approach to MRU personnel in that it may be a false economy to have RAAF personnel undertaking certain basic kitchen tasks. The contractor at Williamtown informed the ANAO that the current arrangements applying to MRU personnel are difficult, and that there are continual problems with where particular responsibilities lie.

5.52 The ANAO suggested that Defence consider whether current arrangements effectively meet its intended aims. Defence advised that the use of Navy MRU personnel is currently the subject of discussions within Defence and agrees that it needs to consider whether current MRU arrangements effectively meet the intended objectives.

Payment for services possibly not provided

5.53 As part of its examination of contract monitoring and performance matters at one base within the RMV region, the ANAO sought an explanation from DSG staff regarding the reasons behind the high turnover of contractor staff in the stores area. DSG staff informed the ANAO that the turnover in

¹¹⁹ This has been illustrated in an earlier report by the ANAO: see Auditor-General (1998) *Commercial Support Program*, Audit Report No. 2, 1998–99, p. 67 – 68; and in a Defence internal audit: see Management Audit Branch (2005) *Garrison Support Contract CSI-WA Members Required in Uniform*.

contractor staff resulted from certain stores staff being dismissed by the contractor. The ANAO was informed that the dismissals occurred because the relevant stores staff had made claims for work done after hours when they had not presented for duty. The contractor had become aware of the deception in June 2008, advised the DSG Regional Manager within days and dismissed the staff concerned within the month. However, the contractor advised the ANAO in April 2009 that it had not been requested by the Commonwealth to reimburse any moneys that may be owed for services that were apparently not delivered but which were invoiced for.

5.54 In advice to the ANAO of 27 May 2009, the RMV DSG office advised:

No conclusive evidence could be obtained by either Army or the GSS contractor to confirm the full period over which the deception is likely to have occurred. This lack of evidence limited the extent to which the allegations could be substantiated by DSG.

5.55 In the same advice, DSG indicated that the contractor did not submit any claims for payment in relation to the four occasions when Army had confirmed services were not provided in accordance with contractual requirements. The ANAO considers that there is likely to be little benefit in pursuing this matter now so far after the relevant events occurred, with the contractor staff involved having been dismissed and recollections by Army personnel likely to have been affected by the passage of time. Nevertheless, the response by DSG to this matter was neither timely nor appropriate. When this issue was discovered, following a period for which services were apparently not delivered but invoiced for, the CAPMAN reporting system for the base and region does not provide any indication that such an issue had arisen.

5.56 In light of the lack of a timely and appropriate response by DSG Regional staff in relation to this matter, the ANAO suggested that Defence emphasise to staff responsible for GSS contract management the importance of ensuring that the Commonwealth only pays for services that are provided. In addition, where there are grounds to suspect that services may not have been provided, contract management staff should, in a timely fashion, determine the extent of the services not provided and consider whether there are grounds to seek reimbursement of any moneys from the contractor. Defence informed the ANAO in response to the proposed audit report that, in order to emphasise these principles to regional contract staff, Defence will incorporate these principles within the PCM training course (refer to paragraphs 3.45 to 3.47) and Regional Contract Governance Plans (see paragraph 3.4).

5.57 This incident is also an example of a weakness in the current administrative model related to GSS/Base Services contracts. The contractor staff were providing services out of hours in relation to the provision of ammunition to Army members at a range. The ANAO suggests that Defence overall would have greater assurance that it was only paying for the services received if the service users or recipients (principally the ADF) had greater knowledge of the contracted services that Defence is paying for. Currently, DSG attempts to take much of the responsibility for confirming services are delivered itself. In the context of the Base Accountabilities Model (see Chapter 3, paragraphs 3.36 and 3.37), the ANAO suggests that having a mechanism whereby the relevant ADF user personnel are knowledgeable about the services contractors are required to provide would help improve Defence's overall assurance on the actual services provided. This could also be considered as part of any overall re-examination of the GSS/Base Services contracting model and how it is best administered (refer to the discussion in Chapter 6). In response to the proposed audit report, Defence advised the ANAO that it will consider this suggestion through the implementation of the Base Accountability Model (refer to paragraph 3.36).

Savings related to GSS contracting

5.58 When the original GSS contracts were introduced between July 1998 and December 1998, Defence made claims that significant savings were going to be made by adopting the service delivery model. As part of the audit, the ANAO sought from Defence information relating to savings made when the original GSS contracts were introduced and whether these savings had been maintained since that period. ANAO also reviewed recent steps within DSG to generate savings in GSS.

Savings with the introduction of GSS contracts

5.59 At the time of the first round of GSS contracts, Defence announced savings ranging from 'around 16 per cent of future costs' in the case of Southern Victoria to 'up to 38 per cent of future costs' in the case of the Northern Territory and Kimberley region.¹²⁰ These 'announced' savings were calculated on the basis of the preferred tenderer's bid prior to contract negotiations.

¹²⁰ Department of Defence, Media Release, Thursday 5 August 1999, *Defence to contract out Garrison Support Services in Southern Victoria*; Media Release, Thursday 11 March 1999, *Defence to contract out Garrison Support Services in Northern Australia*.

5.60 In response to the ANAO's request for information about the level of savings actually achieved through the contracting out of GSS, Defence drew attention to a 2002 report undertaken by Defence's Management Audit Branch (MAB).¹²¹ The MAB report contains an analysis of savings prepared by Defence's Commercial Directorate and modified by MAB to reflect data obtained from other sources.¹²² Defence also referred to the difficulty in considering whether the original level of savings had been maintained over time and, in particular, significant changes in scope that have occurred since GSS contracts were implemented.

5.61 Defence undertook a projection of contract commencement values (as set out in the 2002 MAB report) to 2007–08. Using the Non-Farm GDP Price Deflator, Defence projected that the original contracted price at commencement of the first round of GSS contracts would have grown to an annual contract expenditure of \$379.13 million in 2007–08. Defence advised the ANAO that significant scope changes are reflected in the current expenditure under GSS contracts, and referred specifically to:

- security at Defence bases was raised to Safebase Alert status 'Bravo' following the terrorist attacks in the United States on September 11 2001 at a cost of approximately \$33 million per annum;
- operating cost increases of \$13 million per annum as a result of new facilities coming online and facilities being upgraded; and
- additional security costs of approximately \$5 million per annum for enhanced security arrangements for RAAF aircraft and the guarding of Russell Offices in Canberra, which had previously been provided by the Australian Federal Police.

5.62 Defence suggested that, using the MAB report as a baseline, and adjusting for price changes and scope increases, real GSS expenditure has not

¹²¹ Management Audit Branch, Report No: 01/008, *Contract Management of CSP Contracts – Garrison Support*, 7 February 2002.

¹²² The analysis prepared by Defence's Commercial Directorate indicated that the 'announced' savings in relation to GSS (savings offered by the preferred tenderers bid prior to contract negotiations) demonstrated an overall saving to Defence of 27.3 per cent. However, the analysis by MAB indicated that the overall savings calculated at the dates of contract signature (post negotiations) were 15.5 per cent.

varied significantly from the MAB report of 2002 (the comparable actual GSS expenditure in 2007–08 was \$413.8 million).¹²³

Savings from the second round of GSS contracting

5.63 Defence advised the ANAO that any savings achieved when re-tendering occurred with the second round of GSS contracts (post 2004) have been re-invested into service delivery, including:

- allowing for increased volumes and frequencies for particular service types;
- providing services previously delivered outside GSS contracts, such as environmental management obligations; and
- the introduction of enhanced national standardisation of services (for example cleaning standards).

Further savings initiatives

5.64 The GSS Budget Management Review undertaken by Defence in 2008 (discussed in paragraphs 5.11 to 5.14) arose from the pressure to constrain GSS expenditure. A key proposal from that Review was to establish improved central controls over GSS expenditures, particularly in relation to contract amendments. In addition, as part of its 'Board to Board' meetings with contractors, Defence has raised the issue of efficiencies related to matters such as the preparation of meals, as well as the possible introduction of 'gain share' arrangements under the contracts.¹²⁴

5.65 On top of the work undertaken in 2008–09, Defence plans to undertake further major work to provide additional savings in the longer term. Following the Defence White Paper 2009 and the Defence Budget Audit (the Pappas Review), and in the context of the 2009–10 Federal Budget, in May 2009 Defence announced the establishment of the Strategic Reform Program (SRP) to overhaul the entire Defence organisation.¹²⁵ Over the 10 years to 2019, the

¹²³ The figure of \$413.8 million was derived from taking the figure for 2007–08 GSS expenditure provided by Defence on 1 June 2009, and reducing it by the amount included for regions that were not part of the original MAB calculation in 2002.

¹²⁴ Gain share refers to a mechanism in a contract that would promote initiatives by contractors to make savings in the cost of the contract, with the benefit of the saving being shared by the organisation receiving the service and the service provider.

¹²⁵ The Department of Defence (2009) *The Strategic Reform Program - Delivering Force 2030*.

SRP intends to deliver gross savings of around \$20 billion. The reform target associated with GSS under the SRP has been set at \$700 million over 10 years. Under the SRP, Defence intends to follow an estate reinvestment strategy to provide a strategically aligned, affordable, sustainable estate that supports capability.¹²⁶ Changes to the estate will also have substantial impact on the delivery of Garrison Support Services.

5.66 This activity will mean that the GSS budget continues to be under a high level of scrutiny.

¹²⁶ *ibid.*, pp. 3, 18, 23 and 24.

6. The GSS Procurement and Contracting Model

This chapter discusses issues associated with GSS procurement and management identified during the audit and also discusses a range of options that Defence could consider to improve the overall GSS contracting model in the longer term.

Introduction

6.1 As noted in paragraph 5.65, the reform target associated with GSS under the SRP has been set at \$700 million over 10 years. To meet this target, Defence will need to be innovative in its approach to purchasing services from contractors and in how it manages its relationship with industry. As part of this effort, it would be timely to consider whether some refinement of the outsourcing model used with GSS (or Base Services) would assist Defence in achieving longer term economies. Part of this improvement needs to involve reducing the administrative overhead of both contractors and Defence in managing the contracts.

6.2 In this context, this chapter discusses issues associated with GSS procurement and management identified during the audit and sets out a range of options that Defence could consider to improve, in the longer term, the overall GSS (or Base Services) procurement and contracting model.

Issues identified by the audit

6.3 The audit identified a range of issues that may best be remedied by taking a long term view of how GSS (or Base Services) might best be procured and managed. Key issues are summarised below:

- *The detailed specification by tenderers of how they will deliver specific services that currently occurs as part of the tendering process.* This is a costly and time-consuming process for tenderers, and also serves to limit the number of firms that tender for GSS (or Base Services) (paragraphs 2.15 and 2.19). This detailed approach also increases the cost to Defence in assessing tenders, with a large team being involved in the assessment process (paragraphs 2.22, 2.23 and 2.26). Tenderers for the NQ Base Services contract informed the ANAO that they considered there was scope to improve aspects of the outsourcing model (paragraph 2.15);

- *Analysis by the ANAO demonstrates that the existing performance management arrangements do not operate fully effectively, particularly in regard to the risk/reward arrangements in place.* Assessments of performance are based on judgments made by relatively low level staff, the actual ratings are inconsistent across regions (for no apparent reason) and there is a considerable administrative cost to DSG and contractors with the current arrangements (paragraphs 4.8 to 4.41 refer). For some indicators, the inconsistent performance assessments lead to different levels of reward being applied to different contracts, without there being evidence of different standards being met (paragraphs 4.42 to 4.44). Provision within the existing contracts for the introduction of stretch targets have not been utilised; and
- *The contract amendment process is not timely or well administered (paragraphs 5.21 to 5.35).* This could lead to additional costs whereby contractors use more expensive casual labour to deliver services rather than permanent employees, or services that are no longer required are paid for because the contract has not been changed.

6.4 In addition to these points, tenderers for the NQ Base Services contract noted in interviews with the ANAO that the initial length of the current contracts (five years) does not allow potential contractors to invest to make longer term improvements in the delivery of services, but that a longer contract term would do so. Tenderers also noted that large service provider companies operate their own corporate quality assurance systems to make sure that the services meet appropriate standards.

6.5 Defence commented during the audit that it is considering whether the current suite of services being sought in Base Services contracts is too broad. The issue being considered is whether Defence would be better served by splitting the Base Services around perhaps two key specialties: such as food and logistics support.

6.6 At many locations visited during the audit a large number of requested services were ultimately being paid for by the ADF user (or in DSG's terms the 'customer') and there was a process of this having to be passed through DSG, and journals occurring to pass on the cost to the ADF user. There may be scope to reduce the DSG involvement in much of the administrative effort related to certain requested services (for example morning teas or other special catering), and have the ADF user retain the funds and deal directly with the contractor. In these cases, the billing for the requested services would be directly to the

ADF user. Where the level of use is directly controlled by the ADF user, there may be benefit in having that user meet the cost and deal directly with the contractor.

6.7 The ANAO also suggests that there may be improved efficiency and assurance overall if relevant ADF users had better knowledge of the services that contractors were required to provide. DSG could rely more explicitly on the ADF users to confirm that services are being provided appropriately (refer to discussion in paragraphs 5.53 to 5.57)

Options for changing the base support model

6.8 The ANAO suggests that any move to re-design the outsourcing model related to GSS (Base Services) should be done in consultation with industry participants, as well as the users of services, principally the ADF. It is only through a thorough examination of the options available, and both the benefits and risks associated with those options, that Defence will be able to assess the most effective future approach to provide economies and efficient administrative arrangements. There are a range of potential initiatives Defence could usefully consider as part of determining any longer term changes and these are outlined in the following sections. These initiatives are raised with a view to assisting Defence achieve longer term economies and efficiencies related to GSS (Base Services), although it is recognised that the quantity and quality of services that Defence requires from contractors will always be major factors affecting GSS (Base Services) costs.

Longer base term for GSS/Base Services contracts

6.9 The current GSS/BSS contracts are for a five year initial term. They have the prospect of being extended from five years to nine years, although the extensions are all subject to certain criteria being met. As discussed in Chapter 2, the ANAO interviewed representatives of the tenderers for the NQ Base Services contract that commenced in January 2009. The tenderers noted that the five year initial length of the current GSS/Base Services contracts does not allow potential contractors to invest to make longer term improvements in the delivery of services. Accordingly, there may be benefit in Defence considering extension of the base term of future GSS/Base Services contracts to say 10 years with a view to providing tenderers with the opportunity to make greater investments in the provision of services that would lead to efficiencies, subject to ensuring performance standards are met throughout contract terms.

Improved outcome approach for services

6.10 The current approach to procurement of GSS/Base Services requires tenderers for these contracts to respond to specific service requirements by setting out in detail how those particular services are to be delivered.¹²⁷ Tenderers for the recent NQ region Bases Services contract informed the ANAO that this is a costly and time-consuming process for tenderers. This detailed specification of stipulated processes also increases the cost to Defence in assessing tenders and monitoring service delivery performance. Tenderers also raised concerns with the ANAO that the existing tender approach provided particular advantage to firms with existing contracts and also made it difficult for new entrants to the GSS/Base Services contracting field. In particular, tenderers noted that the detailed approach that is taken with the tender advantages the incumbent as site visits do not allow tenderers to fully understand the work involved.¹²⁸

6.11 In designing future contract and tender arrangements, the ANAO suggests that Defence considers relying more on the specification of outcome standards to be met rather than stipulating processes to be carried out or requiring detailed information about how individual services are to be delivered. Such an approach potentially offers a number of benefits including: lower costs for both tenderers and Defence in the tendering process; motivating contractors to innovate in the delivery of services while holding them accountable to specified performance standards and outcomes; and reducing administrative costs for both the contractor and Defence during the contract term. An improved outcome focus in tendering for GSS/Base Services may also promote increased competition by decreasing the cost of entry for potential new suppliers. Maintaining competition over the longer term has potential to contribute to Defence's efforts to limit expenditure increases in GSS/Base Services.

6.12 Evaluation of tenderers' responses could then relate to: the ability of the tenderer to deliver services to a set standard (rather than detailed consideration of how the tenderer intends to deliver every service); the financial viability of the tenderer; its management expertise; its internal

¹²⁷ Defence's current approach to tendering for GSS/Base Services is discussed in Chapter 2 using the recent NQ region tender process as a case study.

¹²⁸ Defence informed the ANAO that it did not agree with these comments by tenderers. See paragraph 2.16.

performance management and quality assurance systems; its ability to attract quality personnel with the required skills and experience; and the financial viability of the bid. Defence may also be able to increase the efficiency of its tender evaluation processes by increasing its reliance on information about tenderer performance at existing operations of the companies concerned, and the views of their existing clients about their performance.

Increased reliance on contractors' quality assurance systems

6.13 Defence could consider placing greater explicit reliance on contractors' own quality assurance systems to assure itself that service outcomes are of the required quality. This would offer the potential for efficiencies and economies for both contractors and Defence from a reduction in the kinds of detailed checks currently undertaken by local DSG staff at bases.

6.14 Expert teams, separate from local DSG or contractor management, could assess or audit the operation of contractors' quality assurance systems, as well as take into account other information available on contractor performance—such as service user feedback. These assessments could be undertaken periodically—for example, at quarterly or six monthly intervals. The expert assessment teams may involve both Defence and contractor staff, although Defence alone would determine whether performance was acceptable, and what level of performance was obtained.

Simplified performance management arrangements

6.15 Current performance management arrangements for GSS/Base Services contracts are based on the aggregation of assessments against a large number of individual performance indicators. Defence could consider moving to an arrangement where performance is instead assessed against a much smaller number of high level indicators. These could include: reliability of contractors' performance and quality assurance systems; quality of the relationship between local DSG staff, contractor staff and service users; service user feedback related to the overall service received; and quality of the contractor's local management.

6.16 The adoption of such a simplified performance management arrangement should provide economies for both contractors and DSG compared to the current arrangements, and could incorporate matters that are currently reviewed separately in the two yearly Strategic Performance Reviews.

Improved contract arrangements for managing under performance

6.17 Currently under-performance by contractors results in monetary adjustments downwards to quarterly margin payments. That is, Defence pays less because the required level of service has not been delivered. In addition, the contractor forgoes the opportunity for increased margin payments on the basis of performance quality above the AQT level. Accordingly, the level of margin payment is the only tool for sanctioning poor performance and encouraging achievement of performance at least at the AQT level.

6.18 There may be benefit in Defence considering the introduction of a cumulative system whereby repeated under performance could ultimately lead to a reduction in the length of a contract, or if the failures were of a critical nature, the cancellation of the contract. Such an arrangement could also incorporate a penalty where there are repeated failures to comply with compliance indicators.

Reduce the administrative burden associated with contract amendments

6.19 The current GSS contracts have required numerous amendments during their life. Generally, these have occurred as a result of the detailed review carried out by the contractor during the due diligence period at the commencement of the contract; because of changes to Defence's operational capability requirement; and to provide for the addition or removal of services. There is increased risk and a significant administrative overhead associated with processing so many contract amendments.

6.20 Accordingly, the ANAO suggests the Defence considers whether the procurement approach for GSS/Base Services could be modified to reduce the number of contract amendments required, or streamline the administrative processes relating to administration of contract amendments.

Explore the opportunities for 'gain share' within contracts

6.21 In line with its current initiative with contractors, Defence should further pursue the inclusion of provisions related to 'gain share' within the contractual arrangements for the procurement of GSS/Base Services. Such arrangements provide an incentive to contractors to make efficiencies or economies, and the benefits are shared between Defence and the contractor. Such changes can be difficult to achieve within the Defence context where there are often traditional or accepted ways in which particular services are

delivered, and the service user needs to be convinced of the appropriateness of the change, but may not obtain a direct financial benefit.

Direct funding by Defence users of discretionary services

6.22 Where the level of use of a particular service is discretionary and determined by the user or 'customer' (principally the ADF), Defence could consider whether there is scope for the user to deal directly with the contractor and for the user to apply its funds to meet these costs. Depending on where funds to meet these needs currently reside, there may be a need to reallocate funding between DSG and the user. There are a very large number of these transactions at all bases throughout a financial year. Under current arrangements DSG plays a 'middleman' role between the 'customer' and the contractor, which requires considerable administrative effort on the part of DSG staff, and also requires a large number of journals to be made in cases where the ultimate cost of the service is met by the 'customer'. Providing an appropriate mechanism for the 'customer' to deal directly with the contractor in circumstances where the level of use of a particular service is discretionary and determined by the 'customer' would reduce Defence's overall administrative costs in relation to such services.

Increase user surveillance of service delivery

6.23 Users of services provided under GSS/Base Services contracts are in a good position to play a role in monitoring, on a day to day basis, whether services have been delivered and to what quality standard. However, during the audit the ANAO identified that relevant user personnel on bases are not sufficiently knowledgeable about the services that contractors are required to provide to make an informed judgement. ANAO suggests Defence considers establishing a mechanism whereby relevant user personnel are provided with the required information and can therefore play a more explicit role in providing assurance that contracted services are delivered.

Defence comment

6.24 Defence thanked the ANAO for the suggestions in the report. Defence noted that it had already considered some of the initiatives, and will further consider the initiatives through the SRP activities and future procurement and contracting processes.



Ian McPhee

Auditor-General

Canberra ACT

17 November 2009

Appendices

Appendix 1: Defence comments

Table A 1

Defence's full comments in relation to the ANAO's recommendations

| No. | ANAO Recommendation | Defence Response |
|-----|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1. | <p>The ANAO recommends that Defence reviews its approach to providing debriefings to tenderers for future Base Services contracts with a view to providing:</p> <ul style="list-style-type: none"> a) tenderers with an assessment against each of the evaluation criteria, noting the strengths and weaknesses of the tender of the particular organisation; and b) debriefs within 30 days of a contract being entered into. | <p>Defence agrees with Recommendation 1.</p> <p>Defence will review all debriefing activities and timeframes prior to undertaking future tender processes associated with the provision of Base Services.</p> |
| 2. | <p>The ANAO recommends that Defence adopts a sound risk based approach to the management of GSS contracts and that the resulting risk assessment be used to assist in determining the appropriate processes for functions such as performance assessment, contract amendments and payment verification, and the level of resources best applied to those functions.</p> | <p>Defence agrees with Recommendation 2.</p> <p>As part of the implementation of Contract Hubs for the management of GSS contracts, Defence intends to undertake a formal assessment of all strategic and operational level risks associated with the management of the GSS contracts, including performance management, contract amendments, invoicing and payment processes.</p> <p>The resulting risk assessments will be used to identify opportunities to improve management and administration processes, responsibilities and timeframes for implementation across the Contract Hubs, where a primary objective is to achieve greater consistency and standardisation.</p> <p>A National Contract Governance Framework has been developed and consists of a National Contract Directive and supporting Contract Hub-level Governance Plans, as well as a range of other elements such as training, an intranet contract management resource web-site and a Group mailbox for procurement and contract management advice for access by both Defence and Contractor personnel.</p> <p>The National Contract Directive has already been developed and was issued to industry for comment as part of the implementation of the Contract Hub arrangements. The Directive and Plan mandate appropriate processes for functions such as performance assessment, contract amendments and payment verification.</p> <p>The level of resources to be applied will be</p> |

| No. | ANAO Recommendation | Defence Response |
|-----|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| | | <p>addressed through the establishment of a standard national structure for Contract Hubs and consistent Regional Contract Management Training functions. This is supported by a mandated national Professionalising Contract Management Program and supporting training manual which can be used as guidance in the workplace. The Professionalising Contract Management Training Program commenced in April 2008 and is progressively being rolled out across regions. The Program covers the five key areas of Contract Management including Legal Awareness, Understanding the GSS and CMS Contracts, Relationship Management, Performance Management and Financial Management and Contract Administration. Defence will also incorporate training in relation to Risk Management.</p> <p>Defence is also in the process of engaging a Contractor to examine the processes and resources currently used for GSS Contract Management functions such as performance management, contract amendments, payment verification and the processing and management of requested works.</p> <p>It is intended that these activities will improve the efficiency, effectiveness and consistency of GSS Contract Management.</p> |
| 3. | <p>The ANAO recommends that Defence, in order to support effective GSS, CMS and Base Services related contract management and administration, assesses the benefits of establishing a central information source using an information technology solution (for example, an intranet site) to:</p> <ul style="list-style-type: none"> a) improve access for base and regional personnel, including relevant contractor personnel, to up to date training and guidance material; and b) provide a convenient mechanism for regular, timely communication with these personnel. | <p>Defence agrees with Recommendation 3.</p> <p>Defence has already developed, and is currently delivering, the Professionalising Contract Management Training Program (detailed at Recommendation 2) to Defence and GSS Contractor Contract Management and Administration staff in the regional offices. This Training Program has been specifically tailored to these contracts.</p> <p>Defence will also establish an intranet website for access by Defence and Contractor Personnel. It is envisaged that this intranet website will include general contract management training and guidance material, specific GSS Contract Management training, copies of the National Contract Directive and supporting Governance Plans, relevant document templates, notices, issues registers etc.</p> <p>Defence is also developing a single central mailbox to manage GSS Contract Management and Administration issues and requests for</p> |

| No. | ANAO Recommendation | Defence Response |
|-----|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| | | <p>advice.</p> <p>Furthermore, Defence is in the process of providing interpretation/guidance on the Statement of Works to ensure consistency. This information will be provided through a Web page on the DSG intranet for all base and regional personnel to access.</p> |
| 4. | <p>The ANAO recommends that Defence reviews the Performance Management Framework and Risk Reward Remuneration Model relating to Garrison Support Services with a view to:</p> <ul style="list-style-type: none"> a) remedying inconsistencies in the way the different DSG regions approach performance measurement and the effect of this on both the margin outcome for individual contractors and the cost of GSS to Defence; and b) better supporting the achievement of value for money as well as quality outcomes, through addressing weaknesses in the current Risk Reward Remuneration Model and its application by Defence in relation to maximum quality targets. | <p>Defence agrees with Recommendation 4, although it should be noted that the ANAO found that the ADF representatives interviewed indicated that they were generally satisfied with the services provided under the GSS Contracts.</p> <p>The Performance Management Framework and Risk Reward Model are currently being examined and Defence is in the process of engaging an external consultant to review the GSS Performance Management Framework and Risk Reward Remuneration Model.</p> <p>The key area of the review is the Risk Reward Remuneration Model; changes to the Risk Reward Remuneration Model will set the minimum information requirements needed from the Performance Management Framework. The Performance Management Framework will then be redeveloped to meet the Risk Reward Remuneration Model's minimum information needs.</p> <p>In the interim, for highly subjective services such as catering, cleaning and grounds maintenance, Defence has tried to remove some of the subjectivity in the scoring of performance indicators through the use of supporting criteria which elicit a 'yes' or 'no' response and then roll up to automatically calculate a performance score.</p> <p>Defence is also in the process of engaging a Contractor to examine the processes and resources currently used for GSS Contract Management functions, including performance management.</p> <p>All subsequent changes to the Performance Management Framework and Risk Reward Remuneration Model will be implemented through the Contract Hubs and will be formally included within the Contract Governance Framework.</p> |

| No. | ANAO Recommendation | Defence Response |
|-----|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 5. | <p>The ANAO recommends that Defence:</p> <ul style="list-style-type: none"> a) in consultation with GSS/Base Services contractors, takes steps to determine appropriate timeframe targets for both the contractor and Defence in relation to their respective responsibilities for contract amendments; b) promulgates specific guidance on processing GSS contract amendments to relevant staff; and c) introduces management and reporting mechanisms to promote adherence to this guidance and timeframe targets. | <p>Defence agrees with Recommendation 5.</p> <p>As identified in relation to Recommendation 2, Defence has already developed National Contract Directive and Hub-level Contract Governance Plan templates and these have been provided to GSS Contractors for consideration and comment. These documents include proposed timeframes, minimum content requirements, processes, mandated templates, costing and assessment methodologies and management and reporting requirements.</p> <p>In addition, Standard Operating Procedures have also been developed to support the National Contract Governance Framework.</p> <p>Defence has also mandated a process for additional approvals to be obtained for any amendments involving expenditure of more than \$10,000 per annum. This requirement has been in place since April 2008.</p> <p>Furthermore, Defence has developed an electronic 'workflow' contract amendment process which will be implemented following regional testing. The electronic form with 'time stamps' will allow for reporting of the timeliness of contract amendments and the current status of all amendments in process.</p> <p>These activities will ensure consistency across Contract Hubs.</p> |

Appendix 2: First round of GSS contracts: announced dates and actual savings

Table A 2

First round of GSS contracts

| region | date winning tenderer announced | expected contract cost (\$ million) | actual contract cost (\$ million) ^A | difference between actual and expected contract cost (\$ million) |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------|-------------------------------------|------------------------------------------------|-------------------------------------------------------------------|
| South Queensland | July 1998 | 100 | 116.555 | 16.555 |
| North Queensland | September 1998 | 50 | 63.518 | 13.518 |
| South Australia | November 1998 | 70 | 88.526 | 18.526 |
| Western Australia | January 1999 | 107 | 125.432 | 18.432 |
| Northern Territory & Kimberley region | March 1999 | 98 | 112.28 | 14.28 |
| ACT & Southern New South Wales | May 1999 | 110 | 116.322 | 6.322 |
| Sydney Central | June 1999 | 122.5 | 163.939 | 41.439 |
| Southern Victoria | August 1999 | 285 | 322.88 | 37.88 |
| Riverina Murray Valley | October 1999 | 70.92 | 69.787 | (1.133) |
| Sydney North-West & NSW South Coast regions | November 1999 | 151 | 152.729 | 1.729 |
| TOTAL | | 1 164.42 | 1 331.968 | 167.548 |
| <p>Notes:</p> <p>A: The actual 'contract cost', as stated in a Defence internal audit, is the contractor's price against each item of the contract plus additional Defence costs and the cost of supplying Members Required in Uniform (MRU). This amount is at the contract signature and does not include any subsequent amendments that increased a contract's price.</p> | | | | |

Source: Defence media releases; Department of Defence Inspector General Division (2002) *Contract Management of CSP Contracts: Garrison Support*, 7 February 2002; Department of Defence (2000) *Defence Annual Report 1999-2000*, p. 90.

Appendix 3: Second round of Garrison Support Services contracts and Base Services contracts

Table A 3

Second round of GSS contracts (let under ITRI arrangements)

| Region | Number of tenderers | Contract commencement | Successful tenderer |
|------------------------|---------------------|-----------------------|-------------------------------|
| South Queensland | 6 | August 2004 | Spotless |
| Riverina Murray Valley | 5 | April 2005 | Eurest Support Services |
| Sydney West/South | 6 | October 2005 | Serco Sodexo Defence Services |
| South Australia | 6 | December 2005 | Transfield Services |
| Sydney Central | 4 | May 2006 | Eurest Support Services |
| ACT/Southern NSW | 4 | October 2006 | Serco Sodexo Defence Services |
| Central/Northern NSW | 4 | February 2007 | Serco Sodexo Defence Services |
| Western Australia | 4 | March 2007 | Transfield Services |
| Southern Victoria | 4 | August 2007 | Transfield Services |
| NT/Kimberley | 4 | May 2008 | Serco Sodexo Defence Services |

Source: ANAO analysis of Defence data

Table A 4

Base Services contracts (let under open tender arrangements)

| Region | Number of tenders | Contract commencement | Successful tenderer |
|------------------|-------------------|-----------------------|-------------------------------|
| Tasmania | 4 | December 2008 | Eurest Support Services |
| North Queensland | 3 | January 2009 | Serco Sodexo Defence Services |

Source: ANAO analysis of Defence data

Appendix 4: Efficiency dividends and other savings initiatives

1. The Department of Defence is subject to two Government efficiency dividends which only apply to civilian and non-operational areas (these areas equate to 11.2 per cent of the Defence 2008–09 portfolio budget):
 - an ongoing 1.25 per cent efficiency dividend that has been applied to Commonwealth agencies since 1987–1988 (decreased to 1 per cent in the 1994–95 budget then returned to 1.25 per cent in the 2005–06 budget); and
 - an additional 2 per cent efficiency dividend to be applied to 2008–09 and forward years' departmental expense estimates.¹²⁹
2. In relation to GSS, Defence advised that these dividends were addressed through an ongoing 1.5 per cent compounding efficiency dividend to the budget of GSS and a further 2 per cent dividend from 2008–09. This decreased the GSS budget allocation for 2008–09 by \$8.6 million. In addition, the Government tasked Defence in March 2008 with finding \$1 billion of savings per annum. Defence's response—the Economy and Efficiency (E2) requirement—required the GSS budget to be further reduced by \$12.7 million a year. For this required E2 saving, the ANAO was informed that there has been interaction at the Headquarters and base level between DSG and the Services in an attempt to identify sources of savings, for example changes to cleaning schedules and meal structures. This brought the total savings required from the 2008–09 GSS budget to \$21.3 million. The impact of these dividends was being addressed through an internal budget review team (refer to paragraphs 5.11 to 5.14 in Chapter 5).

¹²⁹ In the Estimates Memorandum 2008/03, this additional 2 per cent efficiency dividend is referred to as a 'one-off' dividend in that agencies are not expected to find an additional efficiency in every year (cumulative dividend) as per the current ongoing efficiency dividend. A pro-rata reduction was also applied to 2007-08 appropriations in January 2008.

Appendix 5: Tools and systems related to Performance Management Framework

Defence Estate Management System (DEMS)

1. DEMS is used for:
 - tracking and recording GSS, including the schedule of services and costs, the quantities of activities, and the invoice validation process; and
 - the application of performance adjusted margin for GSS determined through performance assessments recorded on CAPMAN.¹³⁰

Contract and Performance Management (CAPMAN)

2. CAPMAN is used for recording contract service delivery performance and compliance for GSS. The contractor must ensure accurate and timely input to DEMS and CAPMAN, including as detailed in the Management of Services Statement of Work at Schedule 2 of the contract.¹³¹

Risk Reward Remuneration Model (RRRM)

3. The RRRM applies to all services delivered at bases, although there is some variation in its application to particular services. It uses the contractor's compliance and performance results (as assessed under the Performance Management Framework) to calculate the extent to which monthly margin amounts will be payable to the contractor against each of the services covered under the contract.
4. The efficiency and effectiveness of the RRRM relies upon performance assessments being undertaken in a fair and reasonable manner without regard to what the financial implication may be.
5. To achieve the goals of the RRRM it is important that both Defence and contractor staff develop a shared understanding of what constitutes quality performance in terms of the Performance Management Framework.

¹³⁰ Department of Defence *DS-WA Garrison Contract Part B Terms and Conditions*, pp. 35-36.

¹³¹ Department of Defence *DS-WA Garrison Contract Part B Terms and Conditions*, pp. 35-36.

Resource Output Management and Accounting Network (ROMAN)

6. ROMAN is Defence's payments system. In exchange for the contractor performing its activities, the contractor will be paid cost and margin. The cost will be calculated in accordance with detailed provisions in the Pricing Schedule (Schedule 3 of the contract). The margin will be calculated in accordance with Schedule 10 (the RRRM).¹³²

¹³² Department of Defence *DS-WA Garrison Contract Part B Terms and Conditions*, p. 2.

Appendix 6: Definition of service type categories

1. 'Scheduled' services are paid at the same value for each month of the contract and are associated with fixed ongoing services (for example, access control and stores). Real increases and decreases in 'scheduled' services will generally only occur where there is a change in the scope of the contract. Changes in scope may occur through an increase/decrease in a service, or change in the standard of an existing service.
2. 'Variable' services are those where rates are applied to a volume of services (for example, number of meals served for hospitality and catering) to derive the monthly fee. Changes in volume from month to month will result in changes in expenditure.
3. 'Requested' services relate to expenditure that is considered to be within the scope of the contract, but are not included within 'scheduled' or 'variable' fees due to their non-routine nature. These services are costed on what Defence terms a 'survey and quote' basis, with each quotation for the works required to be assessed on a value for money basis. Quotations are based on the rate schedules submitted in the tender responses. Examples of requested services are the removal of hazardous waste and official functions.
4. 'Additional' services are similar to requested services, but are considered to be out of scope of the contract due to their nature having no direct link to the overall suite of services included in the contract. In most cases these services should involve a funding transfer from the requesting area within Defence to meet the relevant cost.

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| Some Better Practice Principles for Developing Policy Advice | Nov 2001 |
| Rehabilitation: Managing Return to Work | June 2001 |
| Building a Better Financial Management Framework | Nov 1999 |
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