

**ACQUISITION: SMART OR NOT?**

Acquisition initiatives have not been scarce in recent years. Most will agree that the direction of these initiatives is right as is much of their detail, but they will also agree that implementation has been at best patchy and that the benefits gained are considerably fewer than originally envisaged. But how much of the criticism is valid and how much obscures real progress? Philip Pugh says that useful progress is being stifled by flawed processes and assumptions, while Paul Nixon and Dr David Moore of the UK's Defence Academy point to very real progress. Major General Verna of the French Army discusses the need to improve the relationship between the different Government players as well as the relationship between MoD and industry.

# Delusions of Management

by Philip Pugh

*Philip Pugh is an independent consultant who has worked extensively on cost models that are now in use in UK, France, Germany and Australia. He examines the 'illusory improvements' quoted by the McKane Report from the National Audit Office's Major Projects Reports and says that serious deficiencies within the current UK defence procurement system will not be cured until MoD abandons such flawed assumptions.*

Just as the cuckoo is heard each spring, and each autumn sees swallows gathering on telephone wires, so with equal regularity since the introduction of so-called 'smart' procurement has come the announcement of yet another reform of procurement within the Ministry of Defence.

There is a ritualistic quality to all such events. Details may differ, but the essence is always the same. The latest reform, expounded in the McKane report,<sup>1</sup> is no different. As before, it begins by telling us that previous reforms have been successful. Yet, somehow, even though those reforms when promulgated were said to be definitive, further change is now necessary. That change comprises principally the execution of an elaborate quadrille amongst holders of the top jobs and the addition of a few more to their number.

All such reforms are doomed to fail. They are founded upon assumptions dear to so-called 'smart' procurement, but flawed fatally. Those assumptions are reviewed here.

## Illusory Improvements

First is the assumption that previous reforms must be said to have succeeded in their aims.

Thereby, much effort is wasted in presenting at least the appearance of such success. The McKane report appeals to the National Audit Office Major Project Report 2005. Let us examine that evidence, for it is a peculiar kind of success that is being claimed.

For Type 45 destroyer, the raw figure for in-year (2004/05) change of forecast cost is +£68M, big enough by any standard. Moreover, for that year 'changed budgetary priorities' include 'savings in ships capability' of £145M. Thus, on a proper like-with-like basis, cost has grown actually not by £68M, but by £213M. Anyone can control costs if they reduce what they buy. Cost growth is not being controlled, but disguised.

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For Nimrod MRA4, the raw figure for in-year (2004/05) change of forecast cost of Nimrod MRA4 is +£215M. However, for that year 'changed requirement' includes a reduction of the number of aircraft to be procured from 18 to 12 at a saving of £155M. Thus, on a proper like-with-like basis, cost has grown actually not by £215M, but by £370M. Two more years of such 'success' would see the UK taxpayer being charged over four billion pounds and getting no aircraft whatsoever. In any other world than

the wonderland of MoD procurement, this is not success but abject failure.

Other projects also tell the same story. For example, upon the raw figures alone the taxpayer is expected now to spend £2,644M on the A-400M project, £100M less than approved at Main Gate. However, that approval included £116M of 'risk differential', i.e. contingency over and above expenditure then thought to be necessary. Moreover, 'changed requirements' include the saving of £238M through the deletion of defensive aids from 16 of the 25 aircraft to be procured – leaving only 9 aircraft fit to fly in harm's way. On a proper like-with-like basis, forecast cost has not reduced by £100M, but has increased by £254M. All this even before a prototype has flown to bring technical problems to light.

There is more of spin than of substance in claims of success made upon such a basis.

## Chimerical Cost Growth

The second flawed assumption is that growth in the forecast cost of a project manifests something wrong with its current conduct. Therefore, it is supposed erroneously, 'cost growth' can be remedied by 'strong management', whatever that may be.

In fact, 'cost growth' is the product not of slack project management, but of the conspiracy of optimism that pervades the start of virtually every major project, ensuring that they are launched upon unrealistic estimates of their costs. So-called 'cost growth' is no more than the realities of building and testing equipment, forcing upon MoD a reluctant acknowledgement of its true costs.

Measuring management performance, as McKane does, in terms of year-on-year changes in forecast costs and timescales makes matters worse. At best, it encourages project management to postpone declaration of the truth as to likely costs and dates. At worst, it encourages 'de-scoping' in which more and more money is spent on less and less capability.

McKane does mention the need to improve the standards of time and cost estimating within MoD. However, to do so is one of the ritual elements of most reports on procurement reform. Like its precursors, it will remain no more than a pious sentiment unless an answer can be found to a vital question. How are those able to forecast costs accurately to be encouraged and protected in doing so, when producing a realistic forecast at the start of a project will be labelled as 'obstructive' and be decidedly career limiting? Upon this, McKane is silent.

### Daydreams of Commerce

Much of the McKane report is founded upon the assumption that industry is well versed in bringing complex major projects to fruition on time and within budget. It is a pity that MoD did not test this hypothesis before adopting it so enthusiastically. It would not have had far to look before finding reason to doubt the wisdom of MoD imitating commercial practice. It could have sufficed simply to reflect upon how often defence suppliers have been co-opted into the conspiracy of optimism. No firm is forced into accepting a contract. At the start of every project there is a firm willingness, nay eagerness, to accept the job at a price or on a schedule that proves so often subsequently to be far too ambitious.

In the USA, a carefully conducted study<sup>2</sup> in 1986 compared percentage cost overruns relative to forecasts at the initiation of 49 highways projects, 49 water projects, 59 public buildings, 12 very large construction projects, 29 process plants and 30 weapon system projects. The average cost overrun for the weapons projects was less than that for any other of the categories examined, save for highways projects. At that time, UK and USA experiences were very similar.

Thus, before so-called 'smart' procurement, defence did better than civil industry in forecasting the costs of major projects. If matters are different now, the remedy is not that of having MoD ape

industry, but that of reversing what have been found to be mistaken changes in MoD procurement practice.

In like vein, it is to be hoped that, when seeking whom to appoint to the new non-executive positions on the Investment Appraisals Board, MoD does not favour persons practised in the arcane skills of accountancy or in occupying numerous lucrative positions in the City. Rather, they should seek those with an extensive knowledge of the defence industry worldwide and of its history and products. Such persons, setting what they were told into the context of trends in the actual costs of past projects, would soon find much to challenge amongst the forecasts upon which MoD bases its current procurement programme. However, to succeed in improving present decision-making, such persons would also need strong backing at the political level – backing that values a soundly constructed procurement programme above lobbying, internal and external, on behalf of cherished, if unaffordable, projects.

### Transient Responsibilities

Upon one thing, all can agree. This is that, when the acquisition phases of major projects last for 20 years or more, it must be detrimental to their management that leaders of project teams remain in post for a mere three years upon average. That can only exacerbate the tendency for their conduct of the project to be judged not upon the achievement of value for money in the items eventually procured, but upon much shorter-term criteria. When a project has six, seven or more leaders before its success or failure is properly known, credit or blame for that outcome attaches to none of them. For each, 'success' comes to mean getting the project past whatever review point falls within their brief tenure. Success becomes synonymous with contributing to the conspiracy of optimism.

McKane notes the exacerbation of this problem by the rapid turnover of military personnel in procurement positions. For them, in one area central to procurement, a mere two years is not even the current average tenure, but a target of uncertain attainability. The military should reconsider why they occupy such posts at all. Obviously, they are needed to specify what equipment is required. However, it is

difficult to see justification for their involvement beyond that. What is there in their training or experience that fits them to deal with the technical and financial complexities of procurement? Are such matters not dealt with best by civilian specialists?

The military should give serious thought to such questions. After all, in the end it is they who may have to pay the ultimate price if a deficient procurement system delivers to them equipment that is less good than it might have been.

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### Conclusion

The McKane report has identified again serious deficiencies within the current UK defence procurement system. However, these will not be cured until MoD abandons the flawed assumptions upon which supposed remedies are based. Until then, while the diagnosis may be good, the prognosis must remain bleak. ■

### Editor's Note:

*Philip Pugh quotes figures from the National Audit Office's Major Projects Review 2005 as he was writing before the National Audit Office's Major Projects Report 2006 was published. A short review of the 2006 report is at page 102.*

### NOTES

- <sup>1</sup> *Enabling Acquisition Change; An Examination of the Ministry of Defence's Ability to Undertake Tough Life Capability Management*, UK Ministry of Defence, June 2006
- <sup>2</sup> *Improving the Military Acquisition Process – Lessons from Rand Research*, R-3373-AF/RC, The Rand Corporation, 1986