



National Audit Office

Departmental Overview

The performance of the Ministry of Defence 2013-14

DECEMBER 2014

Our vision is to help the nation spend wisely.

Our public audit perspective helps Parliament hold government to account and improve public services.

The National Audit Office scrutinises public spending for Parliament and is independent of government. The Comptroller and Auditor General (C&AG), Sir Amyas Morse KCB, is an Officer of the House of Commons and leads the NAO, which employs some 820 employees. The C&AG certifies the accounts of all government departments and many other public sector bodies. He has statutory authority to examine and report to Parliament on whether departments and the bodies they fund have used their resources efficiently, effectively, and with economy. Our studies evaluate the value for money of public spending, nationally and locally. Our recommendations and reports on good practice help government improve public services, and our work led to audited savings of £1.1 billion in 2013.

Contents

Introduction

Aim and scope of this briefing 4

Part One

About the Department 5

Part Two

Developments in this Parliament 14

Part Three

Recent NAO findings
on the Department 27

Appendix One

The Department's sponsored
bodies at 1 April 2014 43

Appendix Two

Results of the Civil Service
People Survey 2013 44

Appendix Three

Publications by the NAO on the
Department since April 2013 46

Appendix Four

Cross-government reports of
relevance to the Department 47

Introduction

Aim and scope of this briefing

- 1** The primary purpose of this report is to provide the House of Commons Defence Committee with a summary of the Department's activity and performance since September 2013, based primarily on published sources, including the Department's own accounts and the work of the National Audit Office (NAO).
- 2** Part One focuses on the Department's activity over the past year. Part Two examines developments in this Parliament. Part Three concentrates on NAO analyses of activity over the last year.
- 3** The content of the report has been shared with the Department to ensure that the evidence presented is factually accurate.

Part One

About the Department

The Department's responsibilities

1.1 The Ministry of Defence (the Department) is both a Department of State and a military headquarters. It is responsible for providing the military capability necessary to deliver the government's objectives and for defining future military requirements. The principal activity of the Department is to deliver security for the people of the United Kingdom and the overseas territories by defending them, including against terrorism, and to act as a force for good by strengthening international peace and stability.

1.2 The Defence Vision is "to continue to protect our country and help to project its values and interests abroad by delivering versatile, agile and battle-winning Armed Forces, working effectively with each other, directed and supported by a professional Ministry of Defence, with people ready to lead, accept responsibility and spend wisely, protecting our security in a changing world". The Department's priorities for 2013-14 reflect the Defence Vision, which are:

- to succeed in Afghanistan;
- to continue to fulfil their standing commitments;
- to succeed in other operations they are required to undertake;
- to transform Defence by;
 - restructuring the Armed Forces and their capabilities;
 - implementing the Defence Operating Model;
 - delivering Defence in the most effective, efficient and sustainable way.¹

¹ Ministry of Defence, *Annual Report and Accounts 2013-14*, HC 764 November 2014.

How the Department is organised

1.3 In 2013-14, the Department consisted of the armed services, civilian staff, and support and infrastructure functions (**Figure 1** on pages 8 and 9). The Department's activities were managed through:

- Seven principal bodies, known as Top Level Budgets (Navy Command, Army Command, Air Command, Joint Forces Command, Defence Infrastructure Organisation, Defence Equipment and Support, and Head Office & Corporate Services);
- Three Trading Funds (Defence Support Group, the Defence Science and Technology Laboratory and the UK Hydrographic Office); and
- Three Executive non-departmental public bodies (National Army Museum, National Museum of the Royal Navy, and Royal Air Force Museum).

1.4 The Department is led by the Permanent Under Secretary (the most senior civilian in the Department), Jon Thompson, and the Chief of the Defence Staff, General Sir Nicholas Houghton. They are supported by a number of senior officials; both military and civilian (**Figure 2** on page 10).

1.5 The Defence Board is the main corporate board and the highest committee in the Department. It is the main decision-making body for non-operational matters. It is responsible for achieving the Defence Vision and for providing senior level leadership and strategic management. It is chaired by the Defence Secretary and comprises senior executive members of the Department, external independent members, and the Minister for the Armed Forces (who deputises when the Defence Secretary is not present). The 5 executive members are the Permanent Under Secretary, the Chief of the Defence Staff, the Vice-Chief of Defence Staff, the Chief of Defence Materiel, and the Director General Finance. The board has four positions for non-executive board members (NEBMs), one of whom acts as lead non-executive. The board met 9 times in 2013-14.

1.6 There are 3 subcommittees of the Defence Board:

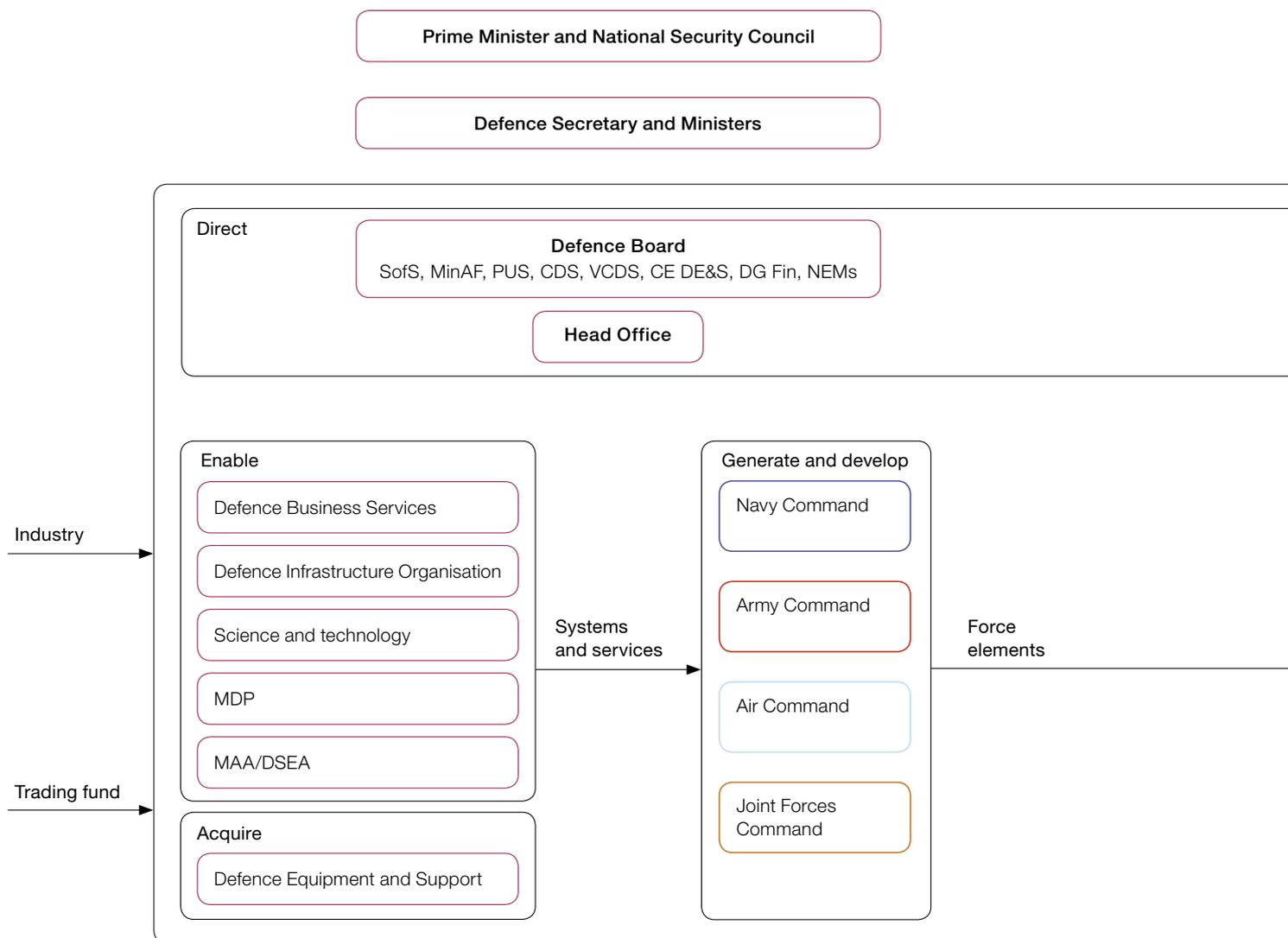
- the Investment Approvals Committee is responsible for considering major investment proposals on behalf of the Defence Board, in accordance with delegations from HM Treasury. On particularly complicated, innovative, risky or contentious projects the Committee makes recommendations to ministers;
- the Defence Audit Committee reviews and challenges the adequacy of internal controls and processes to deal with managing risk across defence and reviews the outputs from assurance providers; and
- the People Committee supports the board in overseeing appointments and the processes for managing the careers of senior military officers and senior civil servants, including managing talent, behaviour, and incentives.

Where the Department spends its money

1.7 The Department's gross operating costs for 2013-14 were £38.6 billion (**Figure 3** on page 11). The Department's major areas of expenditure are described below.

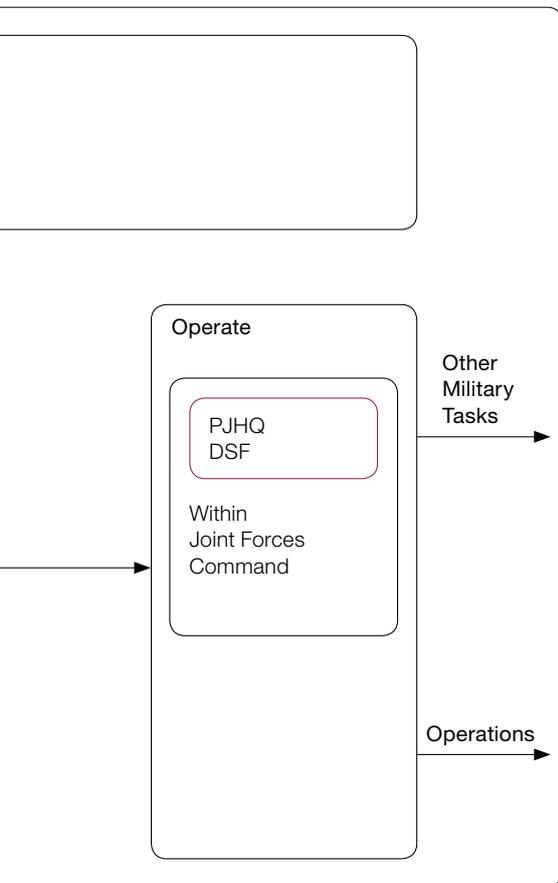
- **Staff.** As at 1 April 2014, the Department employed around 165,860 full-time Service personnel and a further 62,500 civilian staff. Staff costs for these 2 groups were £9.2 billion and £2.4 billion respectively, accounting for some 30% of the Department's total resource spending.
- **Equipment Acquisition.** In 2013-14, the Defence Equipment and Support organisation delivered new equipment valued at £5 billion. This included £0.2 billion of Urgent Operational Requirements (UORs) – equipment procured urgently for a specific military operation. Such UORs are paid for out of the Treasury Reserve rather than from the Defence budget.
- **Major Projects.** In 2013-14, the Department was responsible for delivering major projects with a whole-life cost (excluding exempt projects, where exemptions were made on grounds of national security, or where the publication of data would harm the ability to secure value for money for the taxpayer) of £135.8 billion. The 5 projects and programmes with the largest procurement costs were: Nuclear Warhead Capability Sustainment Programme with a cost of £21.9 billion, Typhoon Fighter Aircraft at a cost of £20.1 billion; Complex Weapons with a cost of £16 billion, Joint Strike Fighter with a cost of £15.3 billion; and the Astute Submarine Fleet at a cost of £9.9 billion.
- **Major Operations.** The Department's most significant activity in 2013-14 was the support of military operations in Afghanistan. During 2013-14, the Department spent £1.9 billion on the net additional costs of operations in Afghanistan, which it received in addition to its core budget. These additional costs included operational allowances for staff on deployment, and inventory consumed on operations.
- **Pensions.** The Department also administers and contributes to the Armed Forces Pension Scheme, which in 2013-14 paid £4.1 billion, including lump sums on retirement, to around 424,000 retired veterans. In 2013-14, the Department's employer pension contributions totalled some £1.9 billion. The scheme had a total liability of £129.5 billion as at 31 March 2014, an increase of £11.5 billion on the previous year, of which £8.4 billion related to actuarial losses caused primarily by a change in the assumptions used to forecast pension liabilities following a formal revaluation.

Figure 1
How the Department is organised



Notes

- 1 SofS = Secretary of State; MinAF = Minister for the Armed Forces; PUS = Permanent Under Secretary; CDS = Chief of Defence Staff; VCDS = Vice Chief of the Defence Staff; CE DE&S = Chief Executive of Defence Equipment and Support and Chief of Defence Materiel; DG Fin = Director-General Finance; NEMs = Non-Executive Members; MDP = MoD Police; MAA = Military Aviation Authority; DSEA = Defence Safety and Environment Authority; PJHQ = Permanent Joint Headquarters; DSF = Directorate of Special Forces.
- 2 The National Security Council (NSC) is the main forum for setting national security strategy across Departments of State (including MOD) and other parts of the government. The NSC meets every week, is chaired by the Prime Minister and attended by the Defence Secretary and, if necessary, the CDS.
- 3 On 1 April 2014 following DE&S becoming a Bespoke Training Entity, the position of Chief of Defence Materiel (CDM) became the Chief Executive of DE&S (CE DE&S).
- 4 Trading Funds are organisations owned by a government department that mainly finance new operations from income generated through trading activity.



Enable and allow defence to work properly by providing supporting services.

Acquire the equipment, systems and other items our armed forces need.

Generate and develop our armed forces so that they are ready for operations.

Operate our armed forces at home and overseas.

Direct policy, military operations and our contribution to national security at the strategic level, as well as direct rules and standards applying to the whole organisation.

Account for and report on defence activity and spending to Parliament and the public.

Force elements – units and formations that are held ready for use on operations.

Defence Business Services – provides services including civilian HR, service personnel and veterans, finance, security vetting, and knowledge and information.

Defence Infrastructure Organisation – Provides infrastructure support for the armed forces by building, maintaining and servicing what the men and women who serve our country need to live, work, train and deploy on operations.

Ministry of Defence Police (MDP) – civilian police force operating within defence.

Military Aviation Authority (MAA) – regulates aviation safety.

Defence Safety and Environmental Authority (DSEA) – regulates safety and environmental protection for those conducting defence activity in compliance with the Secretary of State's policy statement on safety, health, environmental protection and sustainable development.

Permanent Joint Headquarters (PJHQ) – responsible for the planning and execution of UK-led joint, potentially joint and multinational operations, and for exercising operational command of UK Forces assigned to multinational operations led by others.

Directorate of Special Forces (DSF) – provides a joint special operations task force headquarters and is headed by the Director of Special Forces.

Joint Forces Command – ensures joint capabilities, such as medical services, training and education, intelligence, and cyber-operations, are efficiently managed and supported.

Figure 2

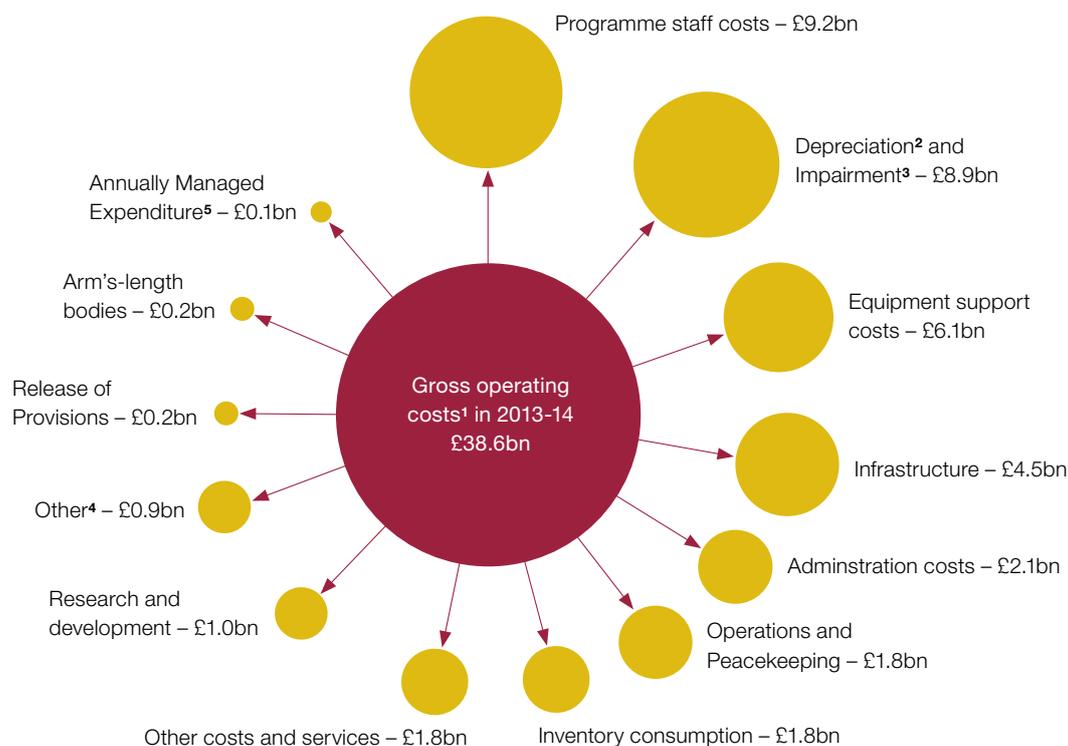
The most senior members of the Department

Military		Civilian	
Title	Role	Title	Role
Chief of the Defence Staff	Main military adviser to the government. As the military strategic commander, he is responsible for how operations are carried out.	Permanent Under Secretary	Head of the Department. He leads on policy advice to ministers and is responsible for overseeing a balanced financial position.
Vice Chief of the Defence Staff	Chief of Defence Staff's deputy for operational matters and acts as the Chief Operating Officer for the armed forces element of the business.	Chief Executive of Defence Equipment and Support	Head of Defence Equipment and Support. He is the Process Owner for the logistics process and has overall responsibility for the Department's acquisition, procurement and commercial activities.
First Sea Lord and Chief of Naval Staff	The professional head of the Royal Navy. He is responsible to the Secretary of State for the fighting effectiveness, efficiency and morale of the Naval Service.	Chief Scientific Adviser	Ensures the main decisions made by ministers, senior officials and the armed services are informed by high-quality, expert scientific advice and analysis.
Chief of the General Staff	The professional head of the British Army. He is responsible to the Secretary of State for generating a balanced and integrated Army capability, and for maintaining the fighting effectiveness, efficiency and morale of the Army.	Director-General Finance	Owns the control framework, chairs the Investment Approvals Committee and shares line management of the Top Level Budgets' Directors of Resources with the Top Level Budget holder.
Chief of the Air Staff	The professional head of the Royal Air Force. He is responsible to the Secretary of State for its fighting effectiveness, efficiency and morale.		
Commander of Joint Forces Command	Manages allocated joint capabilities from the 3 armed services. He reports to the Chief of Defence Staff, and is accountable to the Permanent Under Secretary.		

Source: The Ministry of Defence

Figure 3

Where the Department spent its money in 2013-14

**Notes**

- 1 Gross operating costs includes both cash and non-cash (such as depreciation and impairment) costs which have been recognised through the Statement of Comprehensive Net Expenditure. The Department has also spent £7.5bn of capital expenditure in 2013-14, and these assets are capitalised on the Department's Statement of Financial Position. Capital costs are therefore excluded from Figure 3.
- 2 Depreciation is a measure of the wearing out, consumption or other reduction in the useful life of a fixed asset whether arising from use, passage of time or obsolescence through technological or market changes.
- 3 An impairment loss is the amount by which the carrying amount of an asset exceeds its recoverable value.
- 4 Other includes War Pensions Benefit and Global Conflict Pool – Resource, the Department's contribution to global conflict prevention.
- 5 Annually Managed Expenditure (AME) is additional budget that is spent on items that it is difficult for government departments to predict accurately or control eg pensions.

Source: Ministry of Defence, *Annual Report and Accounts 2013-14*, HC 764, November 2014

1.8 The Department obtained a Supplementary Estimate in February 2014.² It reduced the capital budget by £1.9 billion from £9.8 billion to £7.9 billion and increased the resource budget by £1.7 billion from £38.7 billion to £40.4 billion. As detailed in paragraph 2.4, the Department also made use of budget flexibility to transfer £800 million from 2013-14 to the following 2 years. This budget exchange was undertaken for a number of reasons, including changes to the profile of liabilities and redundancy payments and re-profiled expenditure in capital programmes (**Figure 4**).

1.9 The Department's February 2014 Supplementary Estimate also included a request for £1 billion of non-cash expenditure. This was to cover higher than anticipated forecast asset impairment, charges for Defence Equipment and Support and an allowance to reflect revaluations for Defence Infrastructure Organisation asset holdings.³ The changes resulted in a net increase in the Department's 2013-14 revenue budget and a decrease in its capital budget. Nevertheless, the Department's annual accounts reported an underspend of £2.98 billion against its final resource budget (both DEL and AME) and £448 million against its final capital budget (both DEL and AME).⁴ On the resource budget, the underspend was largely due to uncertainty over the impairments the Department would need to make. On the capital budget, the underspend is in part due to the release of capital provisions.

2 Supply Estimates are the means by which the government seeks authority from Parliament for its own spending each year. In the course of a financial year the government may need to ask Parliament for additional resources, capital and/or cash by means of a Supplementary Estimate.

3 An impairment loss is the amount by which the carrying amount of an asset exceeds its recoverable value.

4 The Departmental Expenditure Limit (DEL) is the budget that is allocated to and spent by government departments. Annually Managed Expenditure (AME) is additional budget that is spent on items that it is difficult for government departments to predict accurately or control eg pensions.

Figure 4

Main and supplementary estimates 2013-14 with an analysis of the Department's 2013-14 underspend

	Resource Departmental Expenditure Limit ¹ (RDEL) (£m)	Capital Departmental Limit (CDEL) (£m)	Resource Annually Managed Expenditure ² (AME) (£m)	Capital Annually Managed Expenditure (AME) (£m)
Main estimates	36,076	9,754	2,651	0
Switch from CDEL to RDEL	1,200	(1,200)		
RDEL budget exchange	(100)			
CDEL budget exchange		(700)		
Reduction in operational funding as requirement lower than forecast	(360)	(35)		
Switch from Resource AME Provision to Capitalised AME Provision			(50)	50
Other government department budget transfers	(17)	22		
Other net changes	1000			
Total change in supplementary estimates (see below)	1,722	(1,913)	(50)	50
Revised estimate	37,798	7,841	2,601	50
Spend	36,448	7,572	963	(129)
Underspend/(Overspend)	1,350	269	1,638	179
Reasons for underspend include:				
● Non cash RDEL depreciation and impairment lower than forecast	1,055			
● Reduction in operations expenditure to mainly reflect the drawdown from Afghanistan	264	165		
● Favourable movement on provisions that had previously been provided for by the Department				179
● Removal of modified historic cost accounting from assets under construction; and non cash impairment that did not materialise and impairment reversals that created a negative charge against budgets.			1,637	
● Sum of other variances	31	104	1	

Notes

1 The Departmental Expenditure Limit (DEL) is the budget that is allocated to, and spent by, government departments.

2 Annually Managed Expenditure (AME) is additional budget that is spent on items that it is difficult for government departments to predict accurately or control eg pensions.

3 Totals may not sum due to rounding.

Sources: Ministry of Defence, *Annual Report and Accounts 2013-14*, HC 764, November 2014

Part Two

Developments in this Parliament

Changes to the Department's spending since 2010

Spending Review 2010 and Strategic Defence and Security Review

2.1 In 2010, the Spending Review and the Strategic Defence and Security Review, jointly determined the Department's priorities for reducing personnel numbers and spending over a 5-year period.^{5,6} In the Strategic Defence and Security Review the Department announced plans to reduce armed forces personnel numbers by 17,000 by 2015 (**Figure 5**). In 2011, the Department then announced plans for a further reduction of 12,000 in the size of the Army to around 82,000.

2.2 The Department has used measures such as compulsory redundancies, voluntary exits and reduced recruitment to meet its personnel reduction targets. The armed forces redundancy programme launched in 2011 is currently at its fourth and final stage. Some 11,000 personnel have been selected for redundancy in the first 3 groups of redundancies (**Figure 6**). In total, the redundancy programme is expected to result in a total of 12,000 redundancies across the 3 services by March 2015. As at 1 April 2014, the full time trained strength of the UK Armed Forces was 150,890, made up of 30,510 in the Naval Service, 87,180 in the Army and 33,210 in the Royal Air Force.⁷

2.3 The Department has also been working to reduce its number of civilian staff by 25,000 to 60,000 by 2015. In July 2011, an announcement confirmed that between 2015 and 2020, there would be a further reduction of 7,000 civilians. To achieve this reduction a separate redundancy programme for civilian staff was initiated. As at 1 April 2014, there were 62,500 civilians in the Department, 23,350 (27%) fewer than in April 2010.

5 HM Government, *Securing Britain in an Age of Uncertainty: The Strategic Defence and Security Review*, Cm 7948, October 2010.

6 The Strategic Defence and Security Review is a strategic review of the UK's military and security policy which takes place every 5 years.

7 Figures have been rounded to the nearest 10 in the source data. Rounding has been applied to totals and subtotals separately, hence a difference of 10 when subtotals are combined.

Figure 5

Planned reductions in size of the armed forces, as in the 2010 Strategic Defence and Security Review (SDSR)

Total trained service personnel	Pre-SDSR	SDSR plans for 2015 (% change from pre-SDSR number)	SDSR assumptions for 2020 (% change from pre-SDSR number)
Royal Navy	35,000	30,000 (-14%)	29,000 (-17%)
Army	102,000	95,000 (-7%)	94,000 (-8%)
Royal Air Force	38,000	33,000 (-13%)	31,500 (-17%)
Total	175,000	158,000 (-10%)	154,500 (-12%)

Source: 2010 *Strategic Defence and Security Review*

Figure 6

Redundancies from the armed forces

Redundancy group	1	2	3	4	Total to date
Date announced	Sep 2011	Jun 2012	Jun 2013	Jun 2014	
Number of applicants	2,300	3,440	6,210	1,450	13,400
Personnel selected for redundancy	2,860	3,760	4,450	1,060	12,130
Percentage of redundancies that were voluntary	62	72	84	72	

Source: Ministry of Defence

2.4 The 2010 Spending Review set out the Department's budget for the period 2010-11 to 2014-15. **Figure 7** shows actual outturn (2011-12 to 2013-14) and planned outturn (2014-15) against the Spending Review forecasts from 2010 and 2013. Over the last 4 years the Department has consistently underspent its forecast capital budget. The Department carried forward £1.2 billion of unused resources from 2012-13 to future years as part of the budget exchange process and has agreed with HM Treasury to carry forward £800 million from 2013-14 to the following 2 years. This comprises budget exchange of £100 million of resource expenditure to be utilised in 2014-15 and £700 million of capital expenditure to be utilised in 2015-16 (see Figure 4). These budget exchanges do not count towards the reductions set out below.

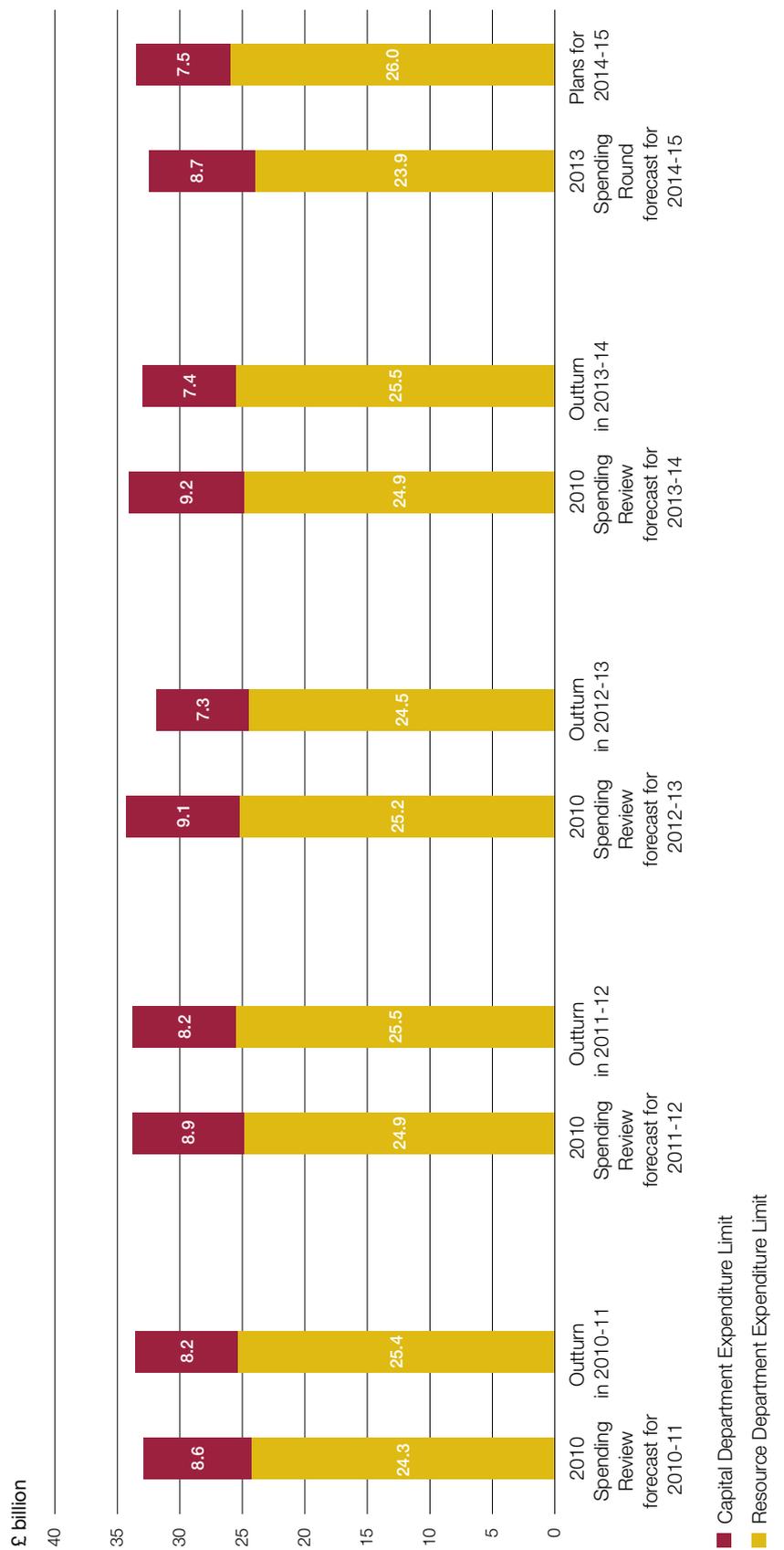
Spending Round 2013 and Autumn Statement 2013

2.5 The 2013 Spending Round, published in June 2013, set out the Department's budget settlement to 2015-16. Its budget (excluding depreciation and Annually Managed Expenditure) was allocated at £32.7 billion for 2014-15⁸ and £32.6 billion for 2015-16. As part of this settlement the Department agreed to make savings of £1 billion in 2015-16, including around £750 million from contract renegotiations.

2.6 The Autumn Statement reported a 1.1% reduction in resource budgets to generate savings of £1.1 billion across government in 2014-15 and £1 billion in 2015-16. As a result, the Department's budget was reduced by a further £277 million in 2014-15 and by £272 million in 2015-16. Figure 7 shows the Department's budget since 2010-11 as per the Spending Review of 2010 and the Spending Round 2013, and the outturn in each year.

8 This balance comprises of the Department's Resource Departmental Expenditure Limit (DEL) budget. It excludes the following costs that are also scored in the Department's gross operating costs: Depreciation and impairment (£10 billion), Resource Annually Managed Expenditure such as provisions and war pension benefit costs (£2.6 billion) and Additional cost Operations (£2.6 billion). Figures have been taken from the 2013-14 Supplementary Estimate.

Figure 7
Changes to the Department's budget



Note

1 The Resource Departmental Expenditure Limit excludes depreciation and amortisation. The outturn figures exclude non-cash expenditure, spend relating to Operations and Peacekeeping, and non-departmental public bodies. This is to reflect outturn figures which are comparable to the Spending Review and Spending Round forecasts. It should be noted that the Department's budget changes throughout the year, notably through the Main and Supplementary Estimates.

Source: Ministry of Defence

Policy and delivery: progress with ongoing changes and planned future challenges

The Department is implementing a number of structural and operational changes

Transforming Defence

2.7 Following the 2010 Strategic Defence and Security Review and Lord Levene's Defence Review, the Department launched multiple transformation programmes in response to the changing priorities of defence.^{9,10} These priorities included the need to balance the defence budget and to avoid historic issues associated with an unaffordable equipment programme. The transformation requires the restructuring of the Armed Forces and their capabilities including rebuilding the Armed Forces Covenant, developing a New Employment Model and transforming the role of the reserve forces. The Department also updated its operating model on 1 April 2014 and as part of this update it has delegated greater levels of budget responsibility to the individual commands. The Department has stated that the new operating model is based on:

- simple structures;
- fair and transparent delegation of responsibility to those best able to deliver;
- strong organisational leadership, coupled with practical business skills;
- a culture of innovation and efficiency, removing needless process and flushing out bureaucracy; and
- joined-up corporate thinking and behaviour, placing the best interests of defence at the heart of our business.

2.8 The Department's September 2013 report on progress against the 14 key recommendations made by Lord Levene in his review showed its assessment of progress against the recommendations.¹¹ The Department reported that many of the recommendations had been implemented or that implementation was under way. In November 2013, Lord Levene reported to the Department in his second annual review that substantial progress has been achieved by the Department in implementing the recommendations in his review.¹² However, Lord Levene expressed concerns that a decision was still required on the future of the Defence Equipment and Support. The Department subsequently announced in December 2013 that Defence Equipment and Support would become a bespoke trading entity from 1 April 2014 (see paragraph 2.10).

⁹ Ministry of Defence, *Securing Britain in an Age of Uncertainty: The Strategic Defence and Security Review*, October 2010.

¹⁰ In 2010, the Secretary of State asked Lord Levene to undertake a review of how defence was structured and managed. The key driver for the review was the Department's over-extended programme which it was believed had been caused, at least in part, by the Department's management structure and behaviours.

¹¹ Ministry of Defence, *Progress against Defence Reform report recommendations*, September 2013.

¹² Ministry of Defence, *Defence Reform: second annual review*, November 2013.

2.9 The Department is also in the process of reforming its armed forces and changing their structure with the aim of making them more flexible and cost effective. This initiative, known as Future Force 2020, also aims to increase the reserve component of the Armed Forces and improve their integration with regular forces. **Figure 8** overleaf sets out the main developments in the Department since 2010.

Reform of Defence Equipment and Support

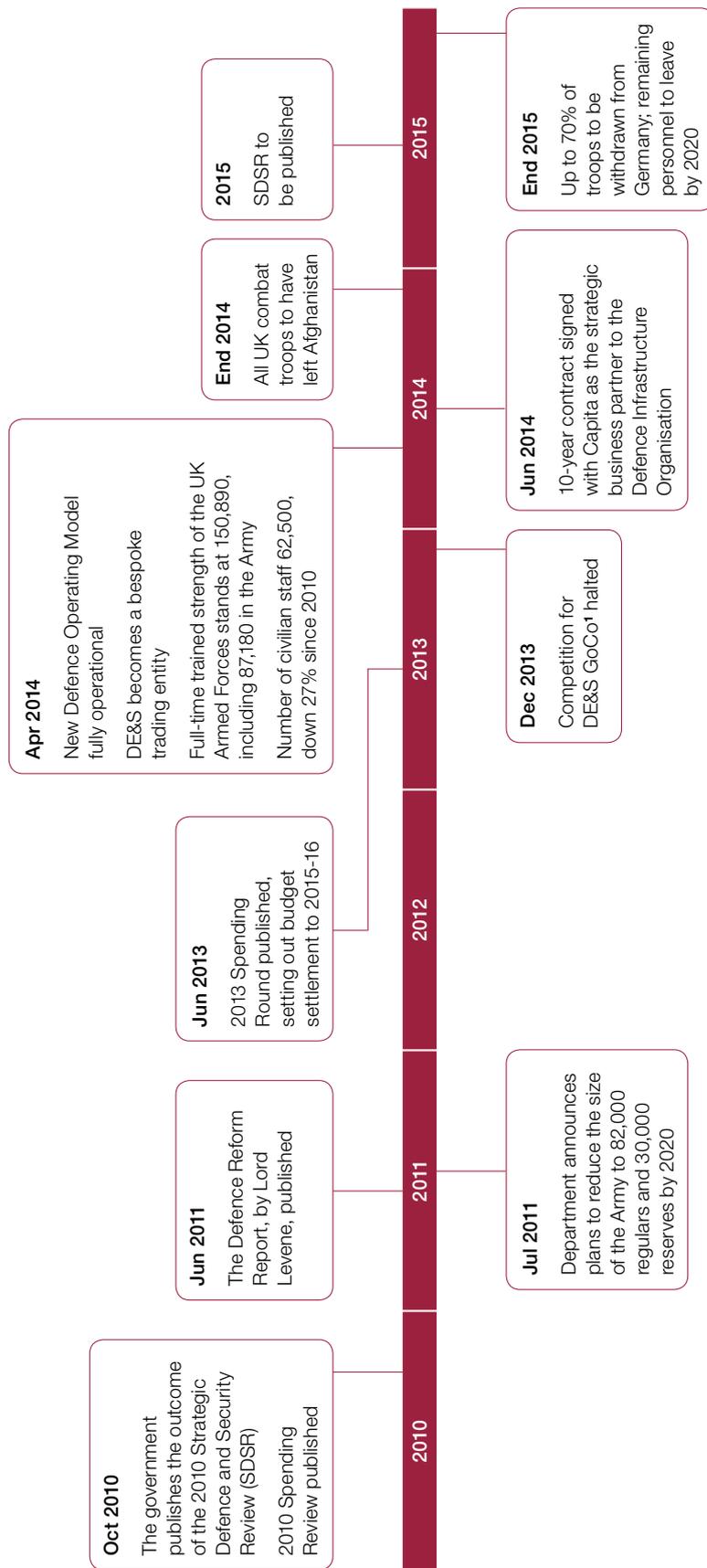
2.10 Defence Equipment and Support is responsible for the procurement of military equipment and maintaining it on behalf of the UK's Armed Forces. As part of a bid to make Defence Equipment and Support a more cost-effective organisation, on 1 April 2014, it became a bespoke trading entity: an arm's-length body of the Ministry of Defence. The Department had originally planned for Defence Equipment and Support to adopt the 'Government-owned, Contractor-operated' (GoCo) model and started a competition to select an industry contractor. This process was abandoned in December 2013 after only one bid was received.

2.11 The entity is seeking to address long-standing weaknesses at Defence Equipment and Support. In November 2014, the Department let contracts with the private sector to provide project and programme management expertise and a human resources function. A contract to develop improved management information is due to be signed in summer 2015. The entity has also been given significant freedoms and flexibilities, agreed with HM Treasury and the Cabinet Office, in relation to how it recruits, rewards, retains and manages its staff. The entity is developing new governance and oversight structures. An independent Chair was announced in June 2014, and when fully developed the governance and oversight structure is expected to include non-executive directors able to hold the Defence Equipment and Support executive board to greater account. The Department established the Chief Executive at Defence Equipment and Support as an accounting officer, directly responsible to Parliament for the stewardship of Defence Equipment and Support resources.

Withdrawal from Afghanistan

2.12 The redeployment of troops and the return of approximately £4 billion of equipment from Afghanistan remained one of the Department's main logistical challenges in 2013-14. The role of UK troops evolved from leading combat operations to training, advising and assisting their Afghan counterparts. On 26 October 2014, Camp Bastion was handed over to the Afghan National Security Force, ahead of UK forces ceasing operations in Helmand on 27 October. The Department has stated that it expected to return around 3,345 vehicles and major equipment (including approximately 50 fixed wing aircraft and helicopters) and around 5,500 twenty foot equivalent units worth of materiel to the UK between 1 October 2012 and the end of the operation. The Department expected the cost of the redeployment phase to be approximately £325 million.

Figure 8
Major developments since 2010



Note
1 'Government-owned, Contractor-operated organisation'. An organisation providing equipment and or services to government but outside the government boundary; ring-fenced as a private sector entity.

Drawdown from Germany

2.13 The Department's overseas estate includes garrisons and training facilities in Germany. In the 2010 Strategic Defence and Security Review, the Department announced plans to withdraw the 20,000 troops based in Germany, with half returning by 2015. The process was sped up in the Army Basing Plan announced in March 2013, which envisages all but 4,400 troops back in the UK by the end of 2016.¹³ Those remaining personnel are currently planned to return to the UK in 2018-19. In January 2014, the Department announced a £51 million contract to build new homes for soldiers and families returning from Germany. The investment is in addition to the £1.8 billion announced in March 2013 for the regular Army Basing Plan. The contract will see the construction of 346 new homes at Beacon Barracks in Stafford. The construction is expected to be completed by summer 2015.

Defence Infrastructure Organisation

2.14 The Defence Infrastructure Organisation (DIO) has established a new organisational structure. In June 2014, it appointed Capita as its Strategic Business Partner, under a 10-year contract worth around £400 million.¹⁴ Capita took up this role in September 2014. The Department expects the partnership to help create a sustainable, efficient and professional organisation, and considers that it represents a significant step forward. The Department estimates the contract could realise savings of approximately £300 million over the next 10 years.

The 2015 Strategic Defence and Security Review

2.15 The Cabinet Office has led the initial preparatory work towards the planned 2015 Strategic Defence and Security Review, which will enable consideration of whether any shifts in policy, approach or capabilities may be required in order to protect national security. In support of this process, the Department is undertaking a programme of research and activity to understand the future strategic context, examine policy options and to test the continued validity of the Department's planned size, shape and structure of the Armed Forces in the future, known as Future Force 2020.

¹³ Hansard HC 25 March 2013, col. 65WS.

¹⁴ A formal partnership through which Capita will share skills and knowledge with DIO.

Independent assessments of the Department's performance

2.16 The Major Projects Authority's second annual report was published in May 2014. This report included a delivery confidence rating, as defined in **Figure 9**, for the government's major projects. The number of major projects across government has increased from 191 in the 2012-13 report, to 199 in the 2013-14 report. Of these projects, the Department has the largest number (40 projects) with a whole life cost (excluding exempt projects, where exemptions were made on grounds of national security, or where the publication of data would harm the ability to secure value for money for the taxpayer) of £135.8 billion. Compared to 3 red rated projects in 2012-13, only 1 project (the Queen Elizabeth Class Aircraft Carriers) was rated red in 2013-14. Both the Watchkeeper surveillance system and the Defence Core Network Systems programme have been reduced from a red to a red-amber rating.

Staff attitudes

The Civil Service People Survey

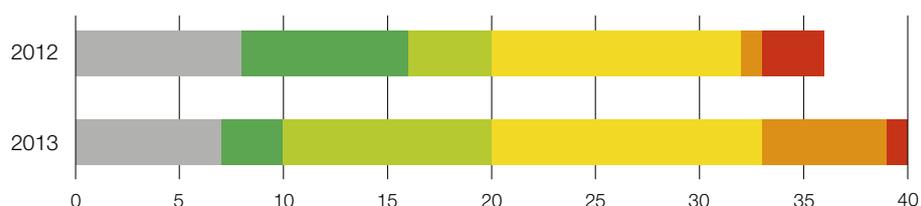
2.17 The government has conducted its Civil Service People Survey annually for the past 5 years. The most recent survey was carried out during October 2013.¹⁵ Continuing our practice in past briefings, we summarise here the views of the Department's staff on a number of key issues, and compare them to benchmarks for the civil service as a whole and to the prior year results (**Figure 10** on page 24). Detailed results for all departments are reproduced at Appendix Two.

2.18 As part of the annual survey, each department receives an engagement index assessing the level of staff engagement. This is determined by the extent to which staff speak positively of the organisation, are emotionally attached and committed to it, and are motivated to do the best for the organisation. In 2013, the Department (excluding agencies) achieved an engagement index of 54%, 2 percentage points higher than the previous survey but 4 percentage points below the 2013 civil service average.

¹⁵ *Civil Service People Survey 2013*, February 2014.

Figure 9
The Delivery Confidence Assessment of Projects

Ministry of Defence



- **Green** Successful delivery of the project on time, budget and quality appears highly likely and there are no major outstanding issues that at this stage appear to threaten delivery significantly.
- **Amber/green** Successful delivery appears probable, however, constant attention will be needed to ensure risks do not materialise into major issues threatening delivery.
- **Amber** Successful delivery appears feasible but significant issues already exist, require management attention. These appear resolvable at this stage and, if addressed promptly, should not present a cost/schedule overrun.
- **Amber/red** Successful delivery of the project is in doubt, with major risks or issues apparent in a number of key areas. Urgent action is needed to ensure these are addressed, and whether resolution is feasible.
- **Red** Successful delivery of the project appears to be unachievable. There are major issues with project definition, schedule, budget, quality and/or benefits delivery, which at this stage do not appear to be manageable or resolvable. The project may need re-scoping and/or its viability reassessed.
- **Grey** Exempted.

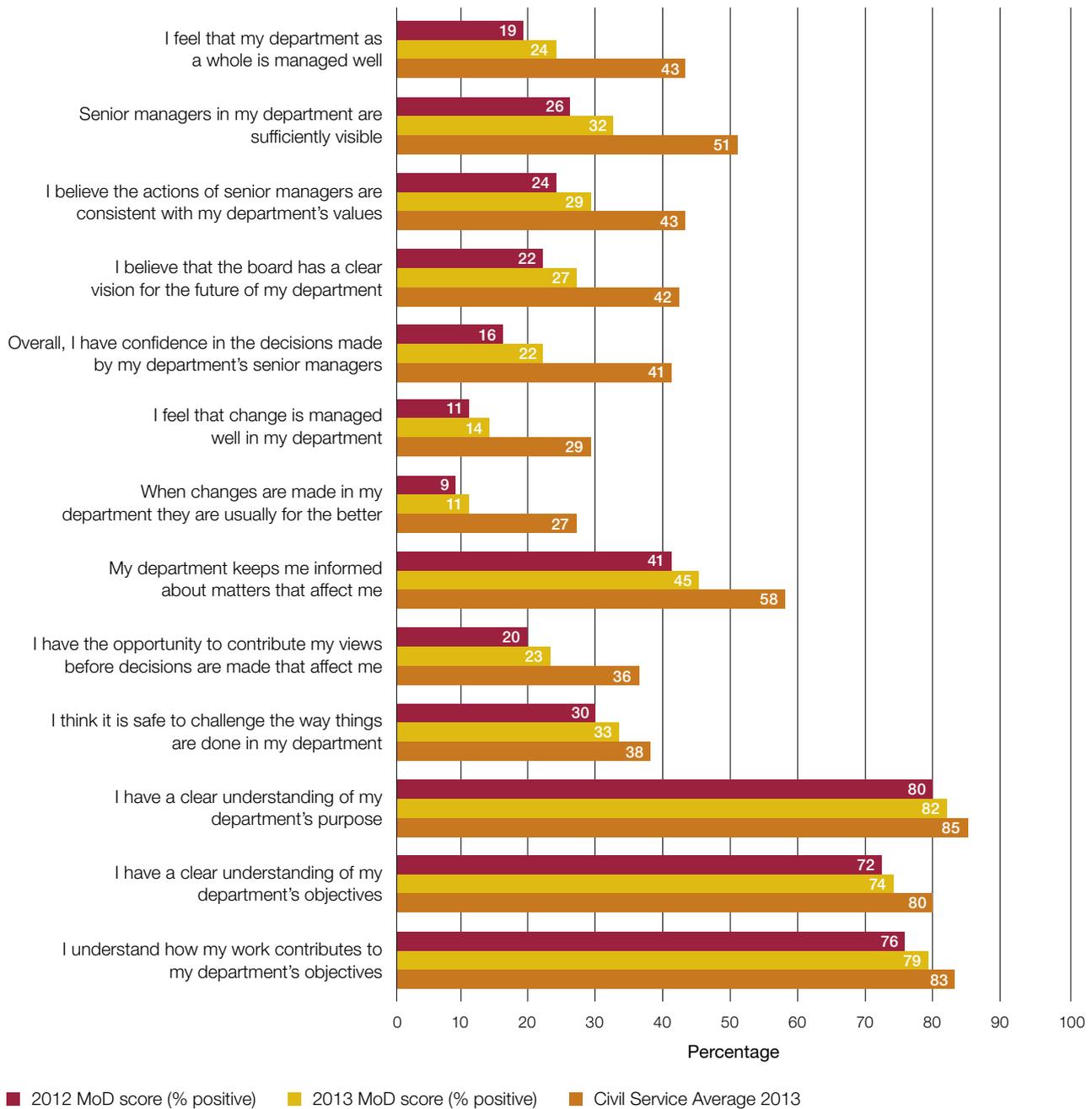
	Exempted ¹ (grey)	Green	Amber/ green	Amber	Amber/red	Red	Total
2012	8	8	4	12	1	3	36
2013	7	3	10	13	6	1	40

Notes

- 1 This refers to data not published by departments, in accordance with the agreed transparency policy. See page 18 of source report.
- 2 As projects being delivered by departments change from year to year, the above figure does not show a comparison between the same projects.

Source: Major Projects Authority Annual Report 2013-2014

Figure 10
2013 Civil Service People Survey: Ministry of Defence



Notes

- 1 The score for a question is the percentage of respondents who strongly agree or agree to that question.
- 2 The 2013 benchmark is the median % positive across all organisations that participated in the 2012 Civil Service People Survey. The difference between the Department and the civil service (Appendix Two) may differ due to rounding.

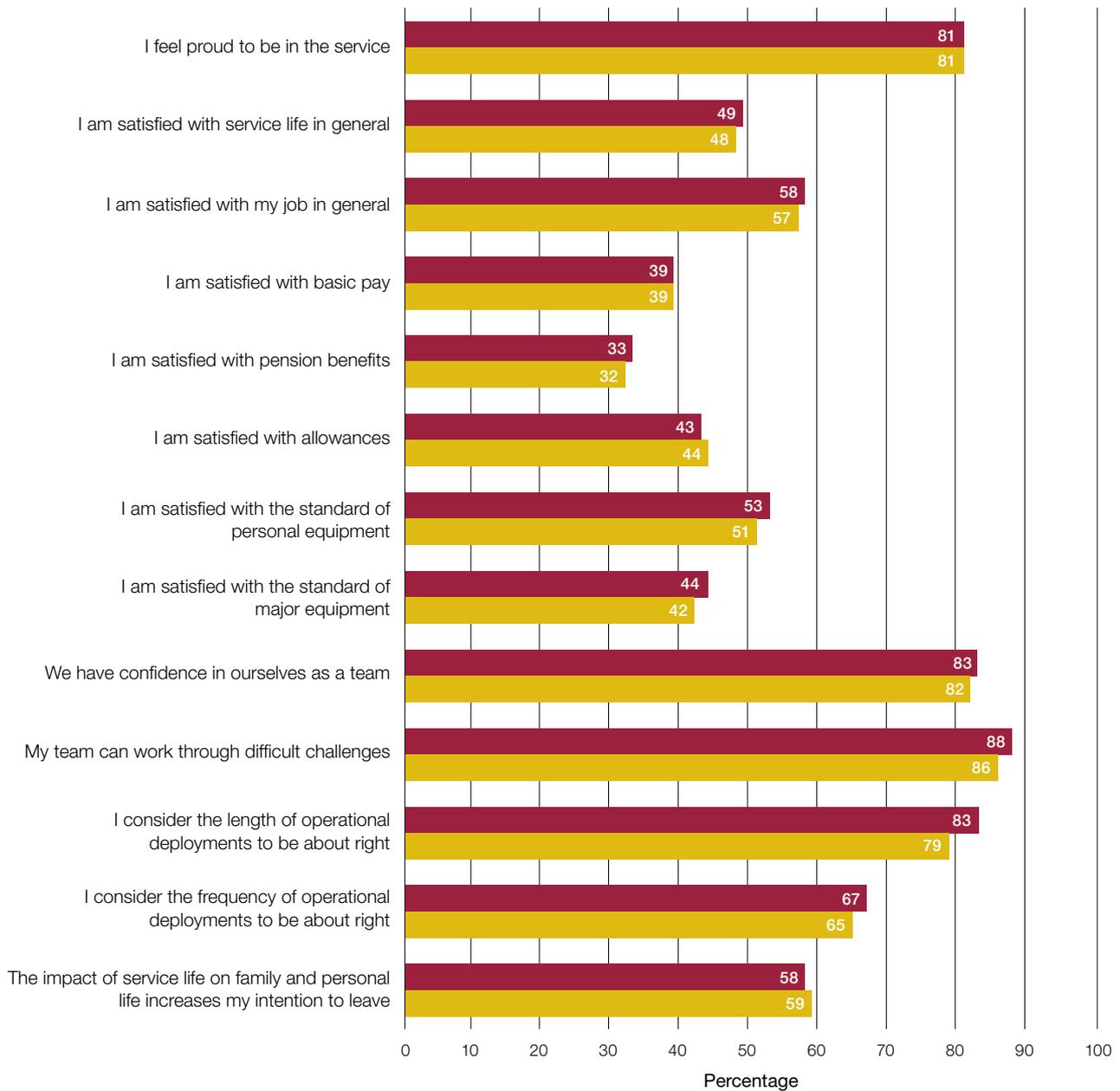
Source: *Civil Service People Survey 2012*, February 2013. *Civil Service People Survey 2013*, February 2014

Armed Forces Continuous Attitude Survey

2.19 In addition to the standard questions asked of civil servants, the Department collects information annually on military personnel through the Armed Forces Continuous Attitude Survey. The survey collates information about service personnel's attitudes on key aspects of service life, such as satisfaction and morale, commitment, demands on the individual, remuneration, and service living accommodation. The Department states that it uses the information from the survey to focus attention where it is most needed to make further improvements in the future. The latest report was published in May 2014.¹⁶

2.20 Some of the key findings are presented in **Figure 11** (overleaf) and show a large majority of personnel continue to report feeling pride in the service and have a high level of confidence, both in themselves and as a team. In 2014, 86% of respondents felt that their team could work through difficult challenges, which was a similar proportion to previous surveys. In contrast, there was a fall in the reported satisfaction of service life and the job in general. Only around one-third of those surveyed reported they were satisfied with the basic pay and pension benefits. There has also been a small increase in respondents indicating that the impact of the service on family and personal life has increased their intention to leave; rising from 58% in 2013 to 59% in 2014.

Figure 11
Key findings from the Armed Forces Continuous Attitude Survey 2014



■ 2013 ■ 2014

Notes

- 1 The scores above show the percentage of respondents who either agreed with that statement, or are satisfied with that particular issue.
- 2 The impact of service life on family and personal life has consistently been the main factor associated with intention to leave the service.

Source: Ministry of Defence, *Armed Forces Continuous Attitude Survey*, July 2013; Ministry of Defence, *Armed Forces Continuous Attitude Survey*, May 2014

Part Three

Recent NAO findings on the Department

Our audit of the Department's accounts

3.1 The NAO's financial audits of government departments and associated bodies are primarily conducted to allow the Comptroller and Auditor General (C&AG) to form an opinion of the truth and fairness of the accounts. In the course of these audits, the NAO learns a great deal about government bodies' financial management and sometimes this leads to further targeted pieces of work which examine particular issues. In this section, we look at the outcome of our most recent financial audit on the Ministry of Defence and its bodies.

3.2 The Department's 2013-14 accounts were signed by the C&AG on 21 November 2014.¹⁷ The signing of the accounts was delayed until after Parliament's summer recess to allow the Defence Infrastructure Organisation time to analyse and reconcile approximately £2.7 billion of assets initially classified as being under construction. The matter has been discussed in the Governance Statement of the Department.

3.3 The C&AG qualified his opinion on the 2013-14 Department Accounts, due to material errors arising from accounting policies which do not fully comply with required accounting standards on lease type arrangements. He also qualified his opinion in relation to two aspects of inventory and non-current asset capital spares which stem from previous qualifications in 2012-13. The Department has made a significant effort to provide sufficient evidence to support the year-end balance in respect of non-current asset capital spares and current asset inventories as at 31 March 2014, however, this work could not differentiate between impairments genuinely arising from activity in year and those impairments arising from an impairment event which should have been accounted in prior years. Consequently the C&AG had to qualify the comparative figures in respect of the prior year; and on the charge made to the Statement of Comprehensive Net Expenditure (SoCNE) for 2013-14 due to the absence of an accurate opening balance.

3.4 The C&AG also qualified his opinion on the comparative figure, in relation to net operating expenditure, due to disagreeing in 2012-13 with the Department's accounting treatment applying impairment in respect of the Germany estate.

¹⁷ Ministry of Defence, *Annual Reports and Accounts 2013-14*, HC 764, November 2014.

Accounting for lease-type arrangements

3.5 For a fifth successive year the Department has not complied with the accounting requirements for determining whether a contract contains a lease and consequently the Department is likely to have excluded a material value of assets and liabilities from its Statement of Financial Position. Contracts may contain leases when they provide the Department with exclusive or near-exclusive use of the assets and capability. For example, where shipyards are used exclusively on defence contracts.

3.6 Since the C&AG's last report the Department has engaged technical support from consultants to review its existing contracts. It has identified that additional management information from suppliers is required to improve financial management around supplier assets and provide the Department with sufficient information to make appropriate adjustments to the accounts. Without this the impact on the accounts cannot be quantified to allow for compliance with the accounting standard. The Department has not maintained the records, nor has it obtained the information required to do so. In agreement with HM Treasury, the Department has decided not to obtain more detailed information on the grounds that obtaining this would not represent value for money. The Department is now considering further work in respect of the application of the accounting requirement to new contracts.

Valuation of non-current assets and inventory

3.7 In response to previous reports where the Department has been qualified on inadequate evidence to support its valuation of military equipment, the Department has implemented a systematic impairment review process to assess the value of write down required across all inventory the Department holds. This process sufficiently evidenced that impairment actions were properly considered; appropriate accounting actions had been taken; and that adjustments were made to the valuation of inventories and capital spares held at 31 March 2014. These changes resulted in an unqualified opinion in respect of the valuation of non-current asset capital spares and current asset inventories as at 31 March 2014. This is the first time the Department has had an unqualified audit opinion on its inventory and capital spares holdings since 31 March 2008.

3.8 The Department has had a history of qualifications covering various aspects of the approximately £15 billion of current and non-current assets held on its inventory systems.¹⁸ The last in a series of long-standing qualifications in this area has now been removed and it is appropriate to consider the Department's progress and current position in respect of inventory. The C&AG has reported further on these matters as part of his report on the 2013-14 accounts of the Department.

¹⁸ The National Audit Office reported on the Department's management of the defence inventory in June 2012. See report, Comptroller and Auditor General, *Managing the defence inventory*, Session 2012-13, HC 190, National Audit Office, June 2012.

3.9 Over the past 5 years, there have been sustained improvements in accounting for assets held on inventory systems:

- In 2008-09, the C&AG limited the scope of his opinion due to significant inaccuracies in the recording of inventory on the warehouse management systems. This qualification was lifted in 2011-12, after the Department made substantial improvements in its stock checking and recording procedures at its depots. The results of the audit and the Department's own validation processes in 2013-14 have confirmed that the Department has sustained its efforts in establishing improved inventory control.
- In 2009-10, the C&AG limited the scope of his opinion due to material unexplained discrepancies between the depot warehousing systems and the main accounting systems. The Department deployed significant resource to undertake quarterly reconciliations across the systems which allowed the conclusion of no further material discrepancies in 2011-12. The small reconciliation difference in 2013-14 (maximum estimated net error of £12 million) demonstrated the Department's continued attention to this key control.

3.10 The key challenges which lie ahead for the Department in this area are:

- Systems – The Department remains constrained by ageing legacy warehouse and inventory systems which require a high level of manual intervention to ensure data integrity.
- Inventory checking procedures – A number of isolated warehouse locations had significant inventory discrepancies, but the C&AG noted these were under investigation by the Department.
- Inventories held off-system – The Department's internal auditors noted that improvements are still required to the impairment consideration of off-system non-current asset capital spares and inventory holdings, particularly in respect of assets in industry.
- Changes to the business – The Department plans to close the Dülmen depot in Germany in 2015 which will require disposal or transfer back to the UK of £0.8 billion book value of non-current asset capital spares and inventory. The Department is also progressing the transformation of its Logistics and Commodities Services and should ensure adequate controls and records are maintained in the depots affected by these changes.
- Embedding good practice – The Department needs to ensure it embeds the good practice in assessing the fair value of inventory items and that these principals become part of the normal course of business.

Governance Statement – Significant Control Risks

3.11 In the 2013-14 Governance Statement, the Department outlined its significant risks and issues and described how it was dealing with them. The Defence Board's main risk discussions during the year were based on monitoring its identified strategic risks which included:

- that we do not have the right numbers of people with the right skills;
- that we cannot generate future leadership;
- that we do not retain the confidence and commitment of our people, causing them to leave;
- the withdrawal from Afghanistan;
- that Transforming Defence does not deliver the required ways of working;
- the delivery of operational capability;
- risks to information, including from cyber attack; and
- from a disruptive event, such as a flu epidemic or terrorist attack.

3.12 The Defence Board has also recognised the need to ensure that the management information it receives continues to improve as well as the timeliness, quality and conciseness of board papers. The Defence Audit Committee which is a subcommittee of the board, has continued to focus its efforts on how effectively the Department manages risk and concluded that the quality of risk management was continuing to improve although there were still areas that presented a number of challenges; including the implementation of the Materiel Strategy and the setting up of the new Defence Equipment and Support organisation. The Defence Audit Committee concluded the Department should focus on ensuring compliance in key areas and setting targets for delivery of improvements.

3.13 Overall the opinion provided by the Head of Defence Internal Audit was 'limited assurance'. In particular, Defence Internal Audit found that:

- in certain areas, policy and processes lacked clarity of rules combined with an absence of assurance requirements and inadequate management checks and management information;
- the Department has defined an operating model in *How Defence Works*, but more work is required to define in detail the control and assurance framework to support it.¹⁹ Moving accountability away from the centre through the delegated model and to business partners further compounds risks to the Department;

¹⁹ Ministry of Defence, *How Defence Works*, September 2014.

- the Department is undergoing considerable transformation, including a reduction in resources without an assessment on the impact on the control environment. In the case of the Defence Infrastructure Organisation, the reduction of resources has led to a weakening of the control environment;
- Top Level Budgets are operating risk management systems to meet their needs and these have evolved separately and differ in many ways. Further work is required to move to a common enterprise risk management system; and
- weaknesses have been identified in a number of other areas, the most notable being in contract management, where further work is required to implement an effective end-to-end contract management process.

3.14 The Significant Control Risks reported in the Governance Statement included:

- **Finance Skills in Defence Equipment and Support**

In 2012-13, it was reported that the Defence Equipment and Support finance skills shortages were resolved but would remain a concern until the conclusion of the Materiel Strategy. The Materiel Strategy has since led to the creation of a bespoke trading entity with significant freedom to recruit staff with the appropriate levels of skills and qualifications.

- **Transforming Defence**

The Department has previously expressed concerns about the structural changes being undertaken leading to a lack of clarity in roles and responsibilities. The Department has taken steps through the creation of Defence Authorities and greater focus on assurance.

- **Defence Infrastructure Organisation – Assets under Construction**

The NAO audit identified concerns about the substantiation of £2.7 billion balance previously disclosed by Defence Infrastructure Organisation as Assets under Construction. The outcome was a write-off of £267 million and adjustment to the annual accounts with the control issues identified through the audit process providing a focus for management action in improving the quality of the control environment in 2014-15.

- **Tax Arrangements of Senior Public Sector Appointees**

As a result of HM Treasury's review of the Tax arrangements of Public Sector Appointees, departments must exercise governance over senior appointments where the appointees are not engaged on departmental payrolls and departments have an obligation to ensure that such appointees are paying the appropriate amount of tax and national insurance. The Department did not undertake the necessary tax compliance checks in a timely manner in 2012-13 and is now seeking retrospective assurance from all senior off-payroll appointees and is verifying the evidence received – and enhancing departmental governance arrangements for all off-payroll appointments.

- **Suitably Qualified and Experienced Personnel**

The Department depends on a wide range of suitably qualified and experienced personnel to deliver defence outputs. The Defence Board is continuing to take a close interest in both the short-term pressures on key skills and trades, known as 'pinch-points' (which are reported monthly), and the longer-term viability of arrangements to recruit and retain the people needed in future. It is supervising the development and implementation of strategies to deal with these issues.

- **Management Information and Information Systems**

The Department recognises that timely, accurate, and consistent management information is critical to the effective management of defence and that this relies on a robust landscape of information systems and networks over which they work. The move to the delegated operating model has accentuated existing concerns about the robustness of the Department's management information and information systems; and Lord Levene highlighted this issue in his second annual review of Defence Reform.²⁰ There are also continuing concerns about the performance of specific information systems projects.

- **Fuel Depots**

The Oil and Pipelines Agency reported that it had been served with Enforcement Actions as a result of a historical lack of investment in both asset integrity and regulatory compliance relating to the 6 oil fuel depots based in the UK that it manages.

Our audits of the Department's effectiveness and value for money

3.15 The NAO's work to test the effectiveness and value for money of government spending in 2013-14 included a number of projects which focused on the Department. The principal findings of these are summarised below.

The Equipment Plan 2013 to 2023 and The Major Projects Report 2013

3.16 The *Equipment Plan 2013 to 2023* and *The Major Projects Report 2013* were published alongside one another in February 2014.^{21,22} The same data is analysed in different ways to produce evidence for each report. While our study of the *Equipment Plan* reviews the Department's ability to forecast the cost and delivery schedule of its projects, the *Major Projects Report* analyses the Department's ability to manage its projects against approved time, cost and capability milestones.

²⁰ Ministry of Defence, *Defence Reform: second annual review*, November 2013.

²¹ Comptroller and Auditor General, *Equipment Plan 2013 to 2023*, Session 2013-14, HC 816, National Audit Office, February 2014.

²² Comptroller and Auditor General, *The Major Projects Report 2013*, Session 2013-14, HC 817-I, National Audit Office, February 2014.

The Equipment Plan 2013 to 2023

3.17 The Department's 10-year Equipment Plan sets out its forecast expenditure plans to provide and support the equipment required by the Armed Forces to meet the objectives of the National Security Strategy and the Strategic Defence and Security Review. The plan covers a budget of £164 billion (**Figure 12** overleaf). The Equipment Plan is split between equipment procurement and support expenditure, which in 2013-14 combined to form 40% of the Department's planned spending.

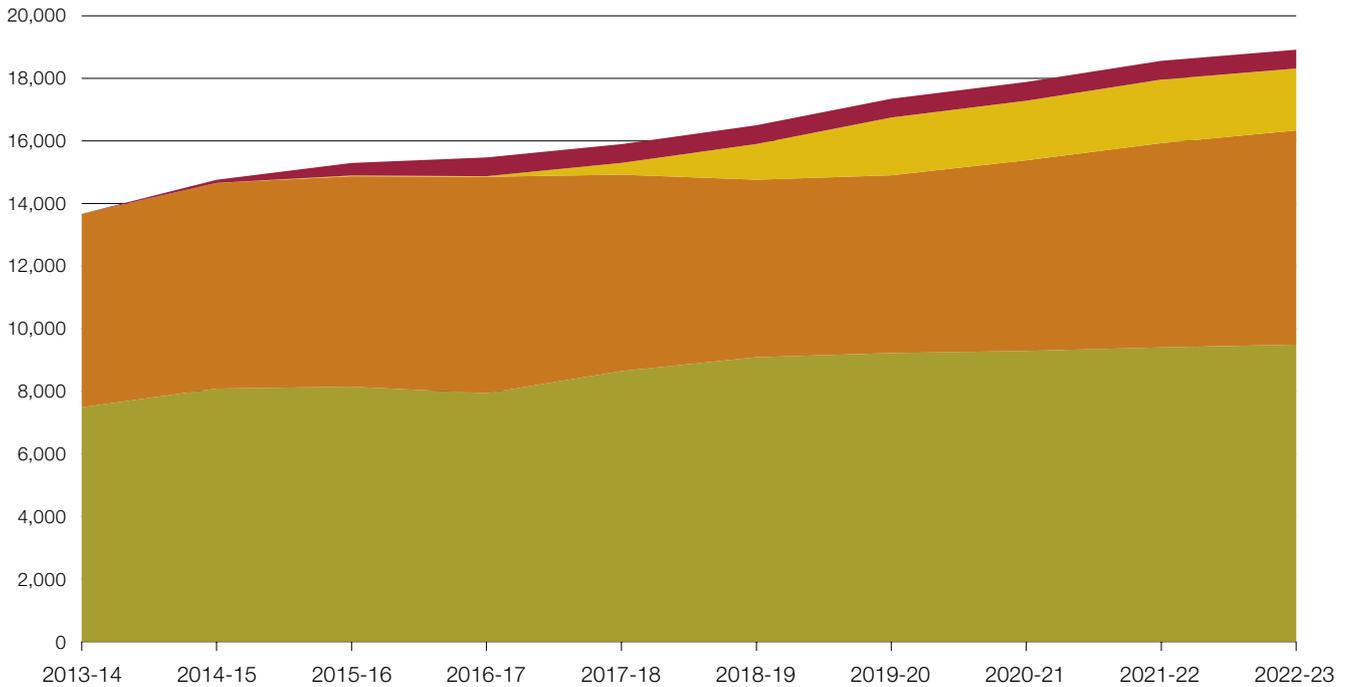
3.18 This was our second review of the assumptions used to compile the Equipment Plan, covering the period 2013 to 2023. We found that the assumptions about the affordability of the Equipment Plan had not changed since our previous report in January 2013.

3.19 We intended to extend the scope of our January 2013 report to examine the assumptions underpinning the Equipment Support Plan, which makes up just over half of the Equipment Plan's budget (£87 billion). However, the Department was unable to provide evidence to support the accuracy of these costs. It has committed to providing this information in time for our report on the Equipment Plan 2014 to 2024.

3.20 Our report on the Equipment Plan 2013 to 2023 concluded that the Department's work to address the affordability gap and to lay the foundations for future stability appears to have had a positive effect on its ability to maintain an affordable Equipment Plan. However, it will take several years before we can judge whether this progress can be sustained. The most significant risk to affordability is the budget relating to equipment support costs, which the Department has not subjected to the same level of scrutiny as the procurement costs. There was also a £1.2 billion gross underspend on the Equipment Plan in 2012-13 and the Department did not fully understand the reasons for this or the impact on the Department's ability to deliver the Equipment Plan on time and on budget.

Figure 12Breakdown of planned spending on the *Equipment Plan 2013 to 2023*

£ million



- Contingency (£m)
- Unallocated budget (£m)
- Equipment Procurement Plan budget (£m)
- Equipment Support Plan budget (£m)

	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23	Total
Equipment Support Plan budget (£m)	7,488	8,086	8,147	7,937	8,645	9,088	9,222	9,291	9,401	9,491	86,796
Equipment Procurement Plan budget (£m)	6,179	6,572	6,724	6,916	6,277	5,672	5,680	6,090	6,527	6,844	63,482
Unallocated budget (£m)	0	0	25	19	375	1,140	1,846	1,903	2,030	1,980	9,319
Contingency (£m)	0	100	400	600	600	600	600	600	600	600	4,700
Total (£m)	13,668	14,758	15,295	15,472	15,897	16,501	17,348	17,884	18,559	18,914	164,297

Notes

- 1 The budget allocated to the Equipment Plan is not the same as reported in the *Equipment Plan 2012 to 2022* because of the adjustments that the Department has made to its plans and forecasts as part of the 2013 budgeting cycle.
- 2 In addition to the £8.4 billion unallocated budget there is £919 million in the final year of the planning period which the Department has earmarked for, but not yet allocated to, future long-term equipment requirements.
- 3 The values given here represent the budget allocated by the Department.
- 4 Values have been rounded to the nearest £ million.

Source: National Audit Office analysis of Ministry of Defence data

3.21 The subsequent Committee of Public Accounts report recommended that:

- the Department should establish processes to improve its data at project level, covering project progress and spending against forecast to understand the principal causes of any under or overspend on its Equipment Plan;
- the Department should complete its work on its support costs to provide accurate data to the NAO in time for it to report to Parliament on the whole of the Equipment Plan for 2014 to 2024;
- the Department should ensure all project teams are applying good practice in cost and risk modelling to help develop its understanding of aggregate risk across the Equipment Plan. It should set out clearly, and quantify, what the contingency is intended to cover;
- in its annual statement to Parliament on the affordability of the Equipment Plan, the Department should report on its progress against its assumed efficiency savings in major programmes; and
- the Department should pursue all options to enable it to meet its skills requirements at the best value for taxpayers, including engaging with, and learning from, other departments (such as the Department of Energy & Climate Change and the Department for Transport) that are experiencing similar gaps in critical areas.

The Major Projects Report 2013

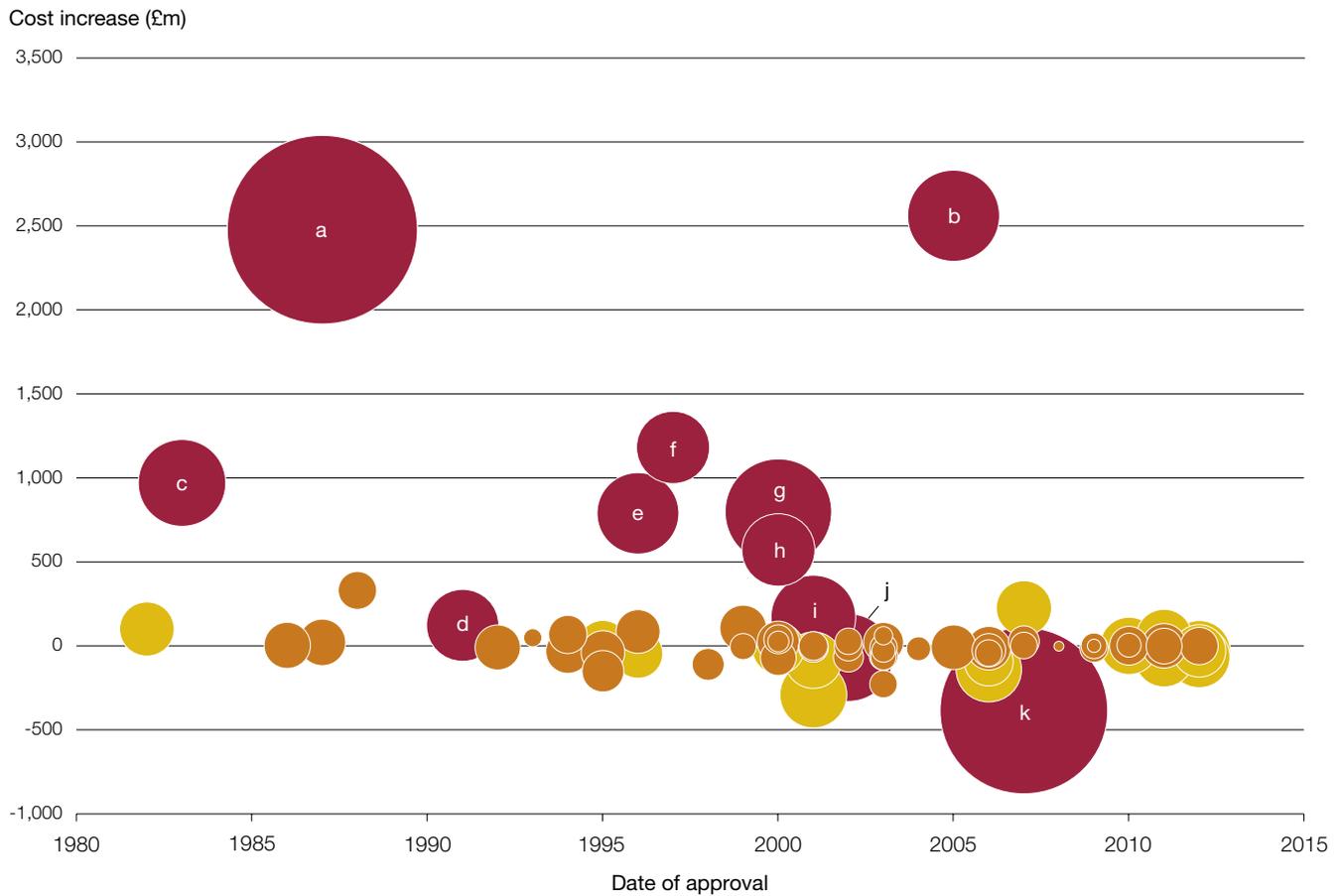
3.22 Each year the Department presents a report on its major projects to Parliament. The report sets out the cost, time and performance of the largest defence projects where the Department has taken the decision to invest, together with some information on the largest projects where it has not yet taken the decision to invest. Our report presents our analysis of the data and our findings.

3.23 Our Major Projects Report 2013 found that there was a net cost increase of £708 million across the 11 projects covered in our analysis in 2012-13. The main driver for this was a £754 million cost increase on the Queen Elizabeth Class Aircraft Carriers following the conclusion of the Department's negotiations with industry in November 2013. With the exception of the Carriers, the Department's management of major projects during 2012-13 had resulted in no significant cost increases and minimal delays in comparison to previous years. However, there remains a legacy of large complex projects that continue to have a significant impact on the portfolio as a whole, with larger projects suffering greater cost increases while smaller projects suffer little or no cost growth (**Figure 13** overleaf).

Figure 13

Project cost increases by size of approval

Projects with larger approval values generally suffer greater cost growth while smaller projects have suffered little or no cost growth



- Approval value of more than £2 billion
- Approval value of more than £1 billion but less than £2 billion
- Approval value of less than £1 billion

- | | |
|---|------------------------------------|
| a Typhoon (aircraft) | g Type 45 (ship) |
| b Queen Elizabeth Class aircraft carriers | h A400M (aircraft) |
| c Merlin HM Mk 1 (helicopter) | i Attack Helicopter Apache |
| d Challenger 2 (tank) | j Skynet 5 (satellite) |
| e Nimrod MRA 4 (aircraft) | k Future Strategic Tanker Aircraft |
| f Astute Boats 1-3 (submarine) | |

Notes

- 1 Future Strategic Tanker Aircraft is a private finance initiative deal spanning 27 years, which includes the whole-life costs rather than just the procurement cost as with all other projects above.
- 2 Sizes of individual bubbles are proportional to project cost.

Source: National Audit Office analysis of Departmental data

3.24 As part of its efforts to ensure that its Equipment Plan is affordable (see paragraph 3.11), the Department is seeking to reduce the cost of some of its major projects by introducing different procurement methods. The portfolio approach introduced by the Department for its procurement of complex weapons, whereby a number of interrelated weapons projects are managed as a portfolio rather than independently, is expected to bring financial benefits of £1.2 billion through the avoidance of cost in the period 2010 to 2019. However, cost increases, delays and changes to the scope and volume of the complex weapons programme could put these benefits at risk. This could have a significant destabilising effect on the Department's ability to balance its budget in the years to come.

Army 2020

3.25 In July 2011, the then Secretary of State for Defence announced plans for an army of 120,000 personnel by 2020. The Department later clarified that this total would consist of around 82,000 regulars and 30,000 reserves, with an additional 8,000 reserves to be in training at any one time to maintain the 30,000 reserves. This is a reduction of 20,000 regulars and an increase of 11,000 trained reserves from pre-2010 levels. The Department projected that this revised force size would enable the Army to achieve savings of £10.6 billion between 2011-12 and 2021-22. It subsequently removed these savings from the Army's budget for that period. The Army's programme to implement the required changes became known as Army 2020.

3.26 Army 2020 is an ambitious programme and means the Army must develop a force with a new size and adaptable structure that is able to respond to unexpected threats. The transition to Army 2020 will involve coordination of several activities over the next 6 years, and beyond, to ensure that the new Army structure operates as planned. These include:

- changing the Army's structure by merging and moving units;
- introducing new equipment;
- returning UK troops from Germany and combat operations in Afghanistan; and
- recruiting, training and integrating an increased number of reserves into a single integrated army.

3.27 The NAO report, *Army 2020*, examined the development of the Army 2020 changes and the Army's progress in implementing them.²³ The report also investigated the main risks to the successful realisation of Army 2020 and its dependencies with wider defence change programmes.

3.28 We found the Army was ahead of its target to reduce the size of the regular Army to around 82,000 and deliver the staffing savings required by its reduced budget. The Army had also identified and planned the structural changes needed to set up Army 2020. However, we found the Department did not fully assess the value for money of its decision to reduce the size of the Army. The Department also did not test whether increasing the trained strength of the Army Reserve to 30,000 was feasible and its recruitment targets for reserves were not underpinned by robust planning data.

3.29 Recruitment of both reserve and regular soldiers was behind the requirement set by the Army for 2013-14 putting Army 2020 staffing targets at risk of being achieved. The Department is taking mitigating actions to improve recruitment, such as offering financial incentives to Army Reserve recruits, but it is too early to say how effective these will be.

3.30 Recruitment performance was affected by the Department's failure to provide critical ICT infrastructure to the Army's recruiting partner – Capita. This meant Capita could not run the recruitment process as it had planned and the Army could not implement its performance regime. Recruitment software scheduled for launch in March 2013 has been delayed until summer 2015, causing the Army increased operational costs of around £1 million a month.

3.31 The Army has made progress in implementing structural changes and reducing the size of the regular Army, but the transition to the new Army structure comes with some significant risks. If not mitigated, they could significantly affect value for money and the Army's ability to achieve its objectives. A key risk to successful delivery of Army 2020 is the full integration of regulars and reserves into a single force structure, which will require a significant behavioural change. The Army plans to improve integration through joint training and pairing reserves with regular units, to prepare for paired deployment on operations.

3.32 The NAO review and subsequent Committee of Public Accounts report recommended that:²⁴

- the Department should reassess its targets for recruiting reserves, and establish clear trigger points for enacting contingency measures if recruitment and retention rates are not improved;
- the Army should seek to better understand the factors that are affecting recruitment performance. It needs to comprehend the relative effect of each of these factors, and how it can influence them, if it is to address them successfully;

- the Department should evaluate the options available to it to address any gaps in military capability, assess their potential short-term and long-term impact on the Army, and develop a strategic contingency plan to respond; and
- the Department should ensure that it is able to hold Capita to account for its performance in delivering the Army recruitment contract, by finalising and agreeing an interim performance regime.

The Department in a cross-government context

3.33 In addition to our work on individual departments, the NAO increasingly looks at performance across government, in order to understand how different departments measure up on important issues. Of the cross-government reports we have published in the last year, 3 have included substantial coverage of the Ministry of Defence.

Making a whistleblowing policy work

3.34 A clear and accessible whistleblowing policy is vital during cost reductions to protect the public purse from waste as well as improve trust in public institutions. We included the Department in a review of 39 whistleblowing policies across government, and subsequently in a review of the systems, structures and behaviours essential for implementing an effective whistleblowing policy.²⁵ The Department was rated satisfactory to excellent across 5 categories when setting a positive environment for a whistleblowing policy. It did however score poorly on providing access to independent advice when supporting whistleblowers. The Department is addressing this by undertaking a fundamental review of its policy and the arrangements in place for staff to report a concern.

Confidentiality clauses and special severance payments

3.35 In June 2013, we undertook an investigation into the use of confidentiality clauses and special severance payments across government.²⁶ Confidentiality clauses and special severance payments can often be in the best interest of both employee and employer. However, it is important that they should not be used to prevent people from raising issues of public interest, to reward failure or avoid management action, disciplinary processes, unwelcome publicity or reputational damage. The investigation concluded that there is lack of transparency, consistency and accountability in how the public sector uses compromise agreements and that little is being done to change this situation.

²⁵ National Audit Office, *Government whistleblowing policies*, January 2014.

²⁶ Comptroller and Auditor General, *Confidentiality clauses and special severance payments*, Session 2013-14, HC 130, National Audit Office, June 2013.

3.36 The investigation found that over the 3 years to 31 March 2013, HM Treasury had approved special severance payments totalling £1.6 million relating to the Department, ranging from £3,000 to £120,000 (**Figure 14**). By comparison, special severance payments across all departments ranged from £250 (HM Revenue & Customs) to £266,000 (Department of Health) with totals ranging from £110,000 (Department for Energy & Climate Change) to £11 million (Department of Health).

3.37 In October 2013, we undertook a follow-up investigation covering 5 government departments, including the Ministry of Defence.^{27,28} Our findings highlighted particularly the need for: better guidance on the use of confidentiality clauses and special severance payments; and improved transparency and oversight to identify and address patterns of behaviour. At the time of publication of the report, the Department had started to analyse all of its severance payments. It planned to understand where these cases were originating from, to inform risk management across the Department. It had published revised guidance on confidentiality clauses clarifying that they should not try to prevent individuals from making protected disclosures. The guidance now states that managers should seek legal advice before finalising any agreements.

Financial management in government

3.38 The government is forecast to spend £720 billion in total in 2013-14 and is part way through a significant programme of fiscal consolidation, incorporating both spending reductions and tax increases. We found that there have been signs of improvement in financial management in government, as well as greater recognition of the strategic importance of the finance profession. There is positive progress in:

- leadership of the finance profession;
- significant financial management processes; and
- management information.²⁹

3.39 As part of the spending reductions the Ministry of Defence is undertaking the defence transformation programme to become more efficient and effective. Other departments are also implementing reforms including: Universal Credit, the Work Programme, pension reform and the implementation of health reforms.

3.40 The finance profession now has a greater senior presence in government, with qualified accountants occupying a range of senior posts. For example, the Permanent Under Secretary in the Ministry of Defence is a qualified accountant, as is the Permanent Secretary of the Department for Communities and Local Government.

²⁷ The departments were the Ministry of Defence, the Department of Health, the Department for Culture, Media and Sport, the Department for Education, and the Department for Communities and Local Government.

²⁸ Comptroller and Auditor General, *Confidentiality clauses and special severance payments – follow up*, Session 2013-14, HC 684, National Audit Office, October 2013.

²⁹ Comptroller and Auditor General, *Financial management in government*, Session 2013-14, HC 131, National Audit Office, June 2013.

Figure 14

HM Treasury's special severance payment approvals in the 3 years to 31 March 2013

Departmental group ¹	Number of cases	Total value £	Maximum £	Minimum £	Median £
Business, Innovation & Skills	40	1,119,254	95,376	500	20,563
Cabinet Office	17	642,092	137,737	1,900	23,055
Communities and Local Government	10	127,524	40,000	1,000	11,500
Culture, Media & Sport	56	1,405,090	145,000	300	16,125
Energy & Climate Change	4	114,850	80,000	10,000	12,425
International Development	6	414,083	140,000	12,000	76,480
Work & Pensions	102	2,408,663	181,470	600	15,000
Environment, Food & Rural Affairs	21	727,502	140,625	925	27,560
Education	57	1,647,003	225,000	300	7,500
Transport	23	1,195,386	156,682	2,340	37,500
Foreign & Commonwealth Office	6	245,280	130,320	1,350	28,403
HM Revenue & Customs	20	571,600	160,000	250	11,000
HM Treasury	17	430,951	96,400	1,000	13,200
Health ²	484	11,158,923	266,000	250	13,700
Home Office	40	1,137,359	225,000	525	8,000
Justice	83	2,940,258	250,000	500	26,657
Defence	51	1,559,742	120,000	3,000	17,500
Other departments	16	511,376	175,908	1,000	23,500
Maximum/Minimum/Median			266,000	250	15,000
Total	1,053	28,356,936			

Notes

- 1 Departmental figures include approved payments for bodies within departmental groups, and non-ministerial departments related to the sector.
- 2 This includes NHS foundation trusts which are in the health sector but not accountable to the Department of Health.
- 3 This table is presented to give an overview of approvals within departmental groups. As they represent differing numbers of employees and departures, it is not appropriate to compare the figures between groups.

Source: National Audit Office analysis of HM Treasury's data

NAO work in progress

3.41 Reforming Defence Acquisition – The Ministry of Defence has a range of programmes to change the way in which the Department operates, and to implement the Strategic Defence and Security Review. As one of a series of reports on elements of defence transformation, we are examining progress in reforming Defence Equipment and Support, including the progress in improving the efficiency of the organisation, the management of the reform strategy and the way forward.

3.42 Strategic financial management in the Ministry of Defence – Through another of our series of reports on defence transformation, we are examining how effectively the Department is managing its key financial risks, and the progress that it has made in implementing its new operating model.

3.43 Major Projects Report and Equipment Plan Review – Each year the NAO reports to Parliament on: the affordability of the Ministry of Defence's 10-year plan to procure and support military equipment through review of the reasonableness and consistency of the assumptions on which the plan is based; and an analysis of the Ministry of Defence's largest procurement projects to provide an update to Parliament on their progress against cost, time and performance targets.

3.44 UK Military Flying Training System (UK MFTS) study – The Ministry of Defence has signed a 25-year contract with industry to implement the UK Military Flying Training System. The system aims to provide trained pilots for all 3 Armed Services. The NAO will examine areas such as: progress with implementation; costs and benefits; contract set-up and contract management; and overall management of the flying training system.

Appendix One

The Department's sponsored bodies at 1 April 2014

Executive non-departmental public bodies

National Museum of the Royal Navy
National Army Museum
Royal Air Force Museum

Advisory non-departmental public bodies

Advisory Committee on Conscientious Objectors
Armed Forces' Pay Review Body
Central Advisory Committee on Pensions and Compensation
Defence Nuclear Safety Committee
Defence Scientific Advisory Council
Independent Medical Expert Group
National Employer Advisory Board
Nuclear Research Advisory Council
Review Board for Government Contracts
Scientific Advisory Committee on the Medical Implications of Less-Lethal Weapons
Veterans Advisory and Pensions Committees

Public Corporation

The Oil and Pipelines Agency

Other bodies

Advisory Group on Military Medicine
Defence Academy of the United Kingdom
Defence Sixth Form College
Defence, Press and Broadcasting Advisory Committee
Fleet Air Arm Museum
Military Aviation Authority
Reserve Forces' and Cadets' Associations
Royal Marines Museum
Royal Navy Submarine Museum
Service Complaints Commissioner
Service Prosecuting Authority

Agencies operating as Trading Funds

Defence Science and Technology Laboratory
Defence Support Group
UK Hydrographic Office

Source: www.gov.uk/government/organisations

Appendix Two

Results of the Civil Service People Survey 2013

Survey question (% 'strongly agree' or 'agree')	Ministry of Defence (excluding agencies)	Civil service benchmark
Leadership and managing change		
I feel that my department as a whole is managed well	24	43
Senior managers in my department are sufficiently visible	32	51
I believe the actions of senior managers are consistent with my department's values	29	43
I believe that the board has a clear vision for the future of my department	27	42
Overall, I have confidence in the decisions made by my department's senior managers	22	41
I feel that change is managed well in my department	14	29
When changes are made in my department they are usually for the better	11	27
My department keeps me informed about matters that affect me	45	58
I have the opportunity to contribute my views before decisions are made that affect me	23	36
I think it is safe to challenge the way things are done in my department	33	38
Organisational objectives and purpose		
I have a clear understanding of my department's purpose	82	85
I have a clear understanding of my department's objectives	74	80
I understand how my work contributes to my department's objectives	79	83

Notes

- 1 These are summary results of the Civil Service People Survey 2013. Not all question scores have been included.
- 2 The score for a question is the percentage of respondents who strongly agree or agree to that question.

Source: *Civil Service People Survey 2013*, available at: www.civilservice.gov.uk/about/improving/employee-engagement-in-the-civil-service/people-survey-2013, accessed 28 August 2014

Appendix Three

Publications by the NAO on the Department since April 2013

Publication date	Report title	HC number	Parliamentary session
11 June 2014	Army 2020	HC 263	2014-15
13 February 2014	The Major Projects Report 2013	HC 817	2013-14
13 February 2014	Equipment Plan 2013 to 2023	HC 816	2013-14
16 September 2013	Departmental Overview: The performance of the Ministry of Defence 2012-13	N/A	2013-14
9 August 2013	Ministry of Defence Data Assurance 2012-13	N/A	2013-14
16 July 2013	Report of the Comptroller and Auditor General on the 2012-13 Accounts of the Ministry of Defence	HC 30	2013-14
10 May 2013	Carrier Strike: the 2012 reversion decision	HC 63	2013-14

Appendix Four

Cross-government reports of relevance to the Department

Publication date	Report title	HC number	Parliamentary session
16 July 2014	The 2013-14 savings reported by the Efficiency and Reform Group	HC 442	2014-15
18 March 2014	Making a whistleblowing policy work	HC 1152	2013-14
7 February 2014	Progress on public bodies reform	HC 1048	2013-14
4 February 2014	Major Projects Authority Annual Report 2012-13 and government project assurance	HC 1047	2013-14
8 October 2013	Confidentiality clauses and special severance payments – follow up	HC 684	2013-14
17 July 2013	Certificate and Report of the Comptroller and Auditor General: Whole of Government Accounts 2011-12	HC 531	2013-14
21 June 2013	Confidentiality clauses and special payments	HC 130	2013-14
13 June 2013	Financial Management in government	HC 131	2013-14
17 April 2013	The Efficiency and Reform Group	HC 956	2012-13
13 March 2013	Cabinet Office and HM Treasury – Integration across government	HC 1041	2012-13
27 February 2013	Improving government procurement	HC 996	2012-13
12 February 2013	The UK cyber security strategy: Landscape Review	HC 890	2012-13
31 October 2012	Certificate and Report of the Comptroller and Auditor General: Whole of Government Accounts 2010-11	HC 687	2012-13
25 September 2012	A snapshot of the use of Agile delivery in central government	Available at: www.nao.org.uk/publications/1213/use_of_agile_delivery.aspx	
20 June 2012	The effectiveness of internal audit in central government	HC 23	2012-13

Publication date	Report title	HC number	Parliamentary session
2 May 2012	Assurance for major projects	HC 1698	2010–2012
20 March 2012	The Government Procurement Card	HC 1828	2010–2012
15 March 2012	Managing early departures in central government	HC 1795	2010–2012
2 February 2012	Cost reduction in central government: summary of progress	HC 1788	2010–2012
29 November 2011	Certificate and Report of the Comptroller and Auditor General: Whole of Government Accounts 2009-10	HC 1601	2010–2012
13 July 2011	Identifying and meeting central government's skills requirements	HC 1276	2010-11
14 October 2010	Central government's use of consultants and interims	HC 488	2010-11
19 July 2010	Progress with VFM savings and lessons for cost reduction programmes	HC 291	2010-11

Where to find out more

The National Audit Office website is
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