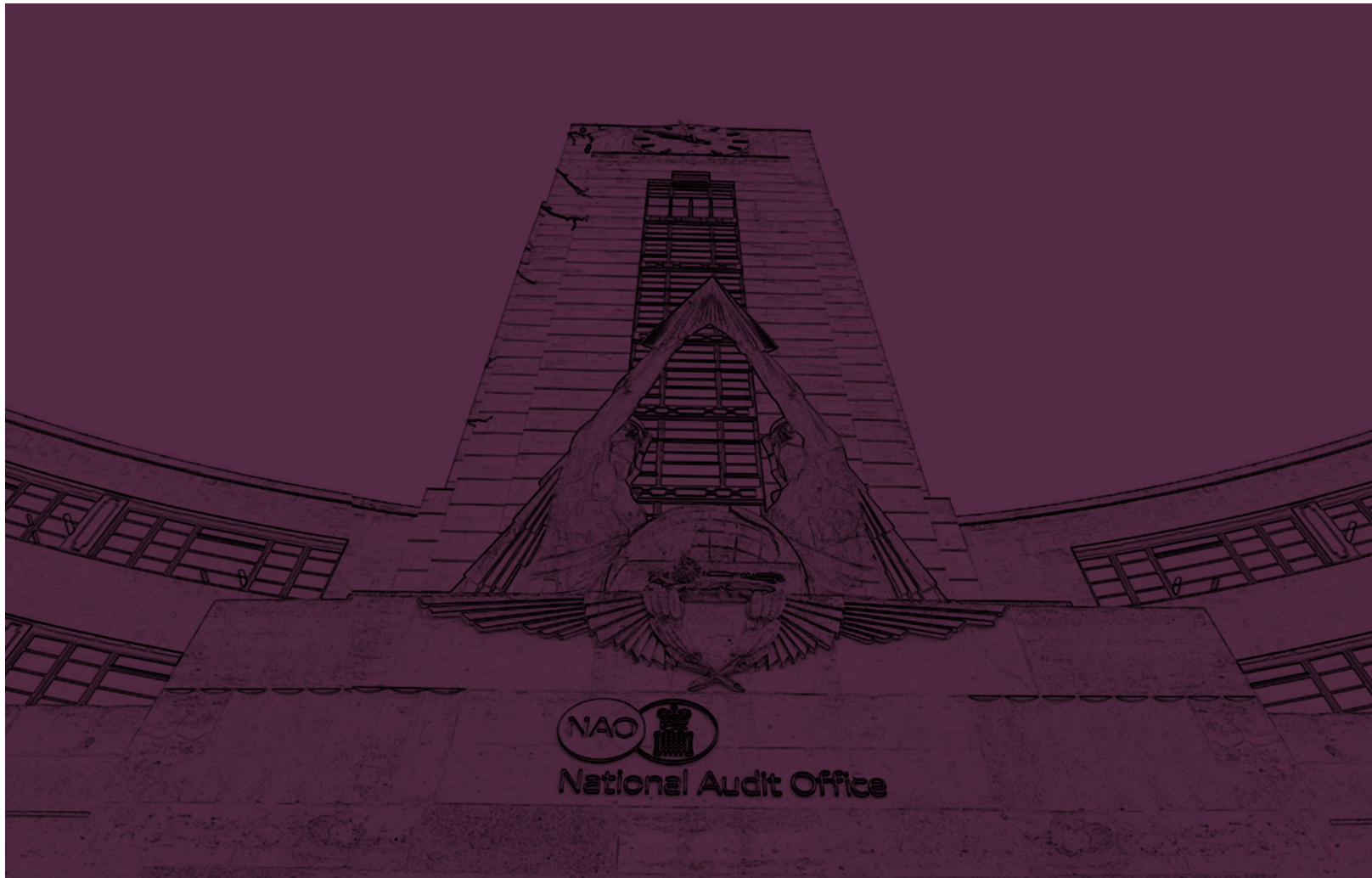




Ministry of Defence

October 2016



If you would like to know more about the National Audit Office's work on the Ministry of Defence, please contact:

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The National Audit Office (NAO) 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. 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 £1.21 billion in 2015.

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Departmental Overview 2015-16

Ministry of Defence

Executive summary

This Departmental Overview summarises what the Ministry of Defence (the Department) does, its performance in 2015-16, and the future challenges it will face in 2016-17. The content of the report has been shared with the Department to ensure that the evidence presented is factually accurate.

Part One sets out some facts about the Department.

- In 2015-16 total Defence spending on equipment, personnel, infrastructure and operations was £35.1 billion.
- The Strategic Defence and Security Review (SDSR) in November 2015 set out the government's National Security Strategy for the coming five years, and how it will be implemented. The SDSR made a number of commitments:
 - **Budget** – An increase in the Department's budget by 3.1% in real terms to 2019-20 as part of the government's commitment to spend 2% on GDP on Defence.
 - **Savings** – Savings of £9.2 billion and to reinvest this in the Defence budget.
 - **People** – Change the balance of military and civilian personnel, with a target to reduce civilian personnel by 30% and a commitment to maintain the size of the armed forces and increase the size of the reserve forces. The SDSR announced the Joint Force 2025 (JF25) concept, which is an evolution of Future Force 2020 (FF20). The JF25 force of around 50,000 aims to provide Defence with the ability to be able to deploy more quickly and for longer periods, and make best use of new technology.
 - **Equipment** – An increase in spending on Defence equipment and equipment support by £12 billion over previous plans, to an estimated £178 billion over the next decade (2016–2026)
 - **Estate** – The Department is introducing a footprint strategy to set out how it will rationalise the Defence estate. It aims to invest in key defence sites, and reduce the built estate by 30%, releasing public sector land for 55,000 new homes to support wider government objectives.

Part Two sets out our findings from our work on the Department.

- The Comptroller and Auditor General qualified his opinion on the 2015-16 departmental accounts for a seventh successive year as the Department has not complied with the accounting requirements for determining whether contracts it holds contain a lease, for example sole use of a shipyard. Consequently, the Department is likely to have excluded a material value of assets and liabilities from its Statement of Financial Position.
- We have seen weaknesses in adherence to HM Treasury and Cabinet Office regulatory frameworks as demonstrated in the breach of contract approval limits at the Defence Infrastructure Organisation (DIO) and the need for retrospective approvals to avoid a qualification. This has led to a £31.6 million fine from HM Treasury and a reduction in DIO's delegated spending limits.
- The Department has recognised weaknesses in its control environment and is implementing a programme to develop its internal control and assurance framework, supported by an annual assurance process and revision of its risk management framework.
- Commercial and contract management continues to be an area of focus for the Department, and it has been working on implementing the recommendations from its commercial capability review. Our Service Families Accommodation study highlights poor performance from the contractor. This has had an effect on service morale, as demonstrated by the results of the annual armed forces attitude survey where satisfaction has fallen noticeably among those living in this accommodation, with a decrease of seven percentage points to 50% in 2016.
- The new commitments set out in the SDSR will increase the pressure on the Department to manage existing challenges to affordability. As a result, the Department has now committed funding that it was previously holding back for future capability improvements ('headroom'), there is reliance on yet-to-be-identified savings, and further cost uncertainty.

Part Three looks ahead to future challenges.

- The Department has a number of major developments on the horizon, its major tasks being to successfully implement the plans set out in the 2015 SDSR:
 - **Major equipment projects and programmes** – The aircraft carriers are due to come into service in 2018 with Carrier Strike capability due to be operational from 2020. The Department is also committed to building the new fleet of four Successor Ballistic Missile Submarines.
 - **Transformation** – Much of the Department is undergoing transformation. The Defence Equipment & Support organisation (DE&S) has a target to be 'match fit' by 2017; the DIO has to set out and implement its strategy for rationalising the Defence estate.
 - **People** – The Department will need to manage the transition to a new workforce composition, with a reduction in civilian personnel, an increase in reserves and maintaining the level of the armed forces. Initiatives such as the Future Accommodation Model (to make a new accommodation offer to help more personnel live in private accommodation and meet their aspirations for home ownership) and the New Employment Model (includes pay and allowances, accommodation, training and education, and terms of service) aim to revise the offer to the armed services with an eye on recruitment and retention.
 - **Military capability** – Future priorities for the Department include retaining a continuous at sea nuclear deterrent; bringing the aircraft carriers and F35 jets into service; developing JF25; and operating within a context of increased risks and threats faced by the UK including threats from terrorism, the resurgence of state-based threats, the impact of technology and the erosion of the rules-based international order.

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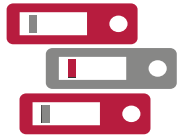
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In November 2015 government published its National Security Strategy and Strategic Defence and Security Review. This highlighted the changing and increasingly uncertain international context in which the Department operates, and its response to this.



In January 2016 the Department published a further report by Lord Levene on Defence

Reform implementation. He highlighted key achievements as: creating a new and smaller Defence Board, a reduced Head Office, important changes in the management of the services and stronger financial management.



A £1.3 billion contract was

awarded for the design and remaining build, test and commissioning activities on the fifth Astute class submarine, Anson. It is scheduled to leave for sea trials in 2020.



The National Shipbuilding Strategy, (expected in autumn

2016), is intended to place UK shipbuilding on a sustainable long-term footing. It will look at how to build a new complex warship on a regular schedule and maximise export opportunities in order to deliver capable ships and value for money, as well as maintaining jobs and skills. Sir John Parker has been appointed as the Independent Chair of the Strategy.



MPs debated the UK's nuclear deterrent on 18 July 2016. The motion to retain an independent minimum credible nuclear deterrent was agreed to after a division (Ayes 472 votes, Noes 117 votes).



The Footprint Strategy (expected in autumn 2016) will set out the Department's approach to rationalising its estate, which is a vital part of balancing its budget.

Key facts



£35.1 billion annual spend in 2015-16



£178 billion estimated cost of the Defence Equipment Plan 2016–2026



2% proportion of GDP government has committed to spending on defence¹



£9.2 billion savings commitment to reinvest into Defence budget



Employs **140,430** military staff² and **56,240** civilian staff³



27,270 trained volunteer Maritime, Army and RAF reserves

Note

- 1 Represents cash Resource DEL and Capital DEL for investment.
- 2 Figure accurate at 1 April 2016 and represents Full-Time Trained Strength which is the element of the UK Armed Forces comprising trained UK Regular Forces, trained Gurkhas and a number of Reserve Forces personnel filling Regular posts while serving on Full-Time Reserve Service. It does not include mobilised reservists.
- 3 Figure accurate at 1 April 2016 and includes all permanent and casual civilian personnel, Royal Fleet Auxiliaries, Trading Funds, locally engaged civilians and DE&S Trading Entity.

Source: Ministry of Defence Annual Report and Accounts 2015-16

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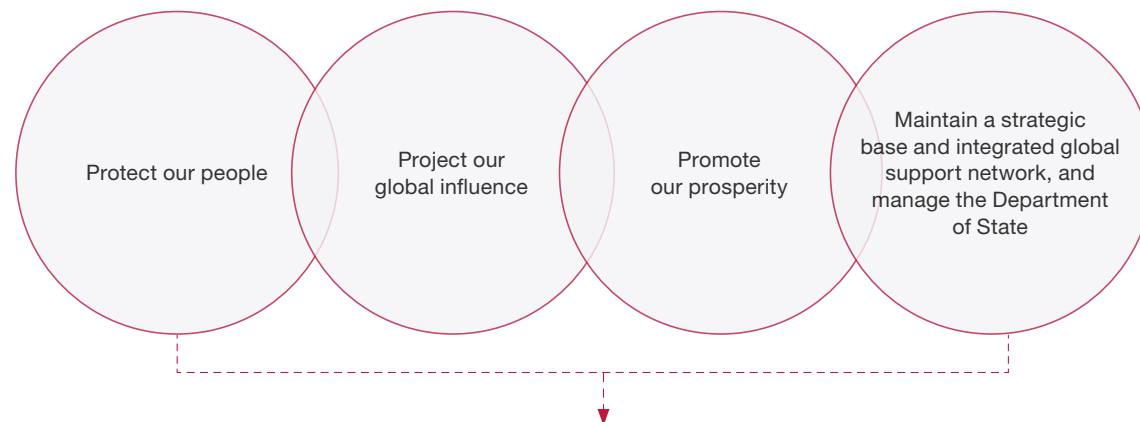
The Ministry of Defence is both a Department of State and a military headquarters, responsible for providing the military capability necessary to deliver the government's objectives and defining future military requirements. The principal activity of the Department is to deliver security for the people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

Vision:

The first duty of government is to defend our country and to keep our people safe. Our national security and our economic security go hand-in-hand. Our strong economy provides the foundation to invest in our security and global influence, which provides more opportunities at home and overseas to increase our prosperity. In a more dangerous world, we have chosen to use our hard-earned economic strength to support our Armed Forces and give them what they need to help keep Britain safe. We will increase defence spending every year and continue to meet NATO's target to spend 2% of GDP on defence for the rest of the decade. In the 2015 Strategic Defence and Security Review we set out a plan for stronger defence with more ships, more planes, more troops at readiness, better equipment for Special Forces, and more for cyber. We will protect our people, territories, value and interests, at home and overseas, through strong Armed Forces and in partnership with allies, to ensure our security and safeguard our prosperity.

[Ministry of Defence Single Departmental Plan 2015–2020](#)

Strategic objectives



The Department of State and the Armed Forces carry out six core functions:

- 1 **Direct** policy, military operations and its contribution to national security at the strategic level, as well as direct rules and standards applying to the whole organisation.
- 2 **Operate** Armed Forces at home and overseas.
- 3 **Generate and develop** Armed Forces so that they are ready for operations.
- 4 **Acquire and support** the equipment, systems and other items our Armed Forces need.
- 5 **Enable** defence to work properly by providing support services.
- 6 **Account** for and report on Defence activity and spending to Parliament and the public.

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Single Departmental Plan 2015–2020

Along with all central government departments, the Ministry of Defence published its Single Departmental Plan for the period 2015 to 2020. The plan sets out what the Department aims to do against each of its strategic objectives, as well as commitments to greater efficiencies, and participation in cross-government activity.

Strategic objectives	Commitments in the 2015–2020 Single Departmental Plan	
Protect our people	<ul style="list-style-type: none"> Pursue a comprehensive political and military strategy to defeat Daesh. Retain the Trident continuous at sea nuclear deterrent to provide the ultimate guarantee of our safety and build the new fleet of four Successor Ballistic Missile Submarines. Bring both of our new aircraft carriers, HMS Queen Elizabeth and HMS Prince of Wales, into service so that one is always available. 	<ul style="list-style-type: none"> Develop proposals to ensure that the Armed Forces can operate effectively overseas and are not subject to persistent legal claims that undermine their ability to do their job. Continue to invest in our cyber-defence capabilities. Maintain the size of the regular armed services and not reduce the army to below 82,000. Deliver on our commitment to expand the reserve forces to 35,000.
Project our global influence	<ul style="list-style-type: none"> Remain at the forefront of the NATO Alliance and support other multilateral organisations. Strengthen our defence partnerships in the Gulf and Asia. Work with our partners to address threats to UK security, including the spread of nuclear, chemical and biological weapons, pandemic diseases, the illegal drugs trade, piracy and organised crime. 	<ul style="list-style-type: none"> Collect, process, exploit and disseminate strategic intelligence and insights. Sustain the framework to enable effective UK defence engagement. Help to shape the international security environment. Strengthen the rules-based international order including through conflict prevention, capacity-building and counter-proliferation. Continue close and enduring work with our allies and partners.
Promote our prosperity	<ul style="list-style-type: none"> Releasing surplus land to support new housing. Promote defence exports with UK Trade & Investment. Spend 1.2% of the core Defence budget on science and technology. Increase the proportion of spend with small and medium enterprises (SMEs) to 25% by 2020. 	<ul style="list-style-type: none"> Launch a defence innovation initiative to remain in step with our allies and ahead of our adversaries. Contribute to the wider UK's skills agenda. Continue to seek value for money in defence procurement, recognising the important contribution that the UK defence industry makes to our prosperity. Increase the number of cadet units in schools.
Maintain a strategic base and integrated global support network, and manage the Department of State	<ul style="list-style-type: none"> Implement the SDSR. Spend £178 billion over 10 years on equipment and support. Provide more opportunities for talented people from all communities and walks of life to serve their country by increasing our recruitment of female and Black, Asian and Minority Ethnic (BAME) personnel by 15% and 10% respectively. 	<ul style="list-style-type: none"> Implement the accepted recommendations of Lord Ashcroft's Veterans' Transition Review on the way the nation fulfils its obligations to veterans. Work to address hearing loss among veterans. Help more servicemen and women to buy their own home through our £200 million Forces' Help to Buy scheme. Continue to support the unsung heroes of the armed forces community: the partners and families of those who serve by supporting the implementation of the Armed Force Covenant and the wider armed forces community, families and veterans.

Source: [Ministry of Defence Single Departmental Plan 2015–2020](#)

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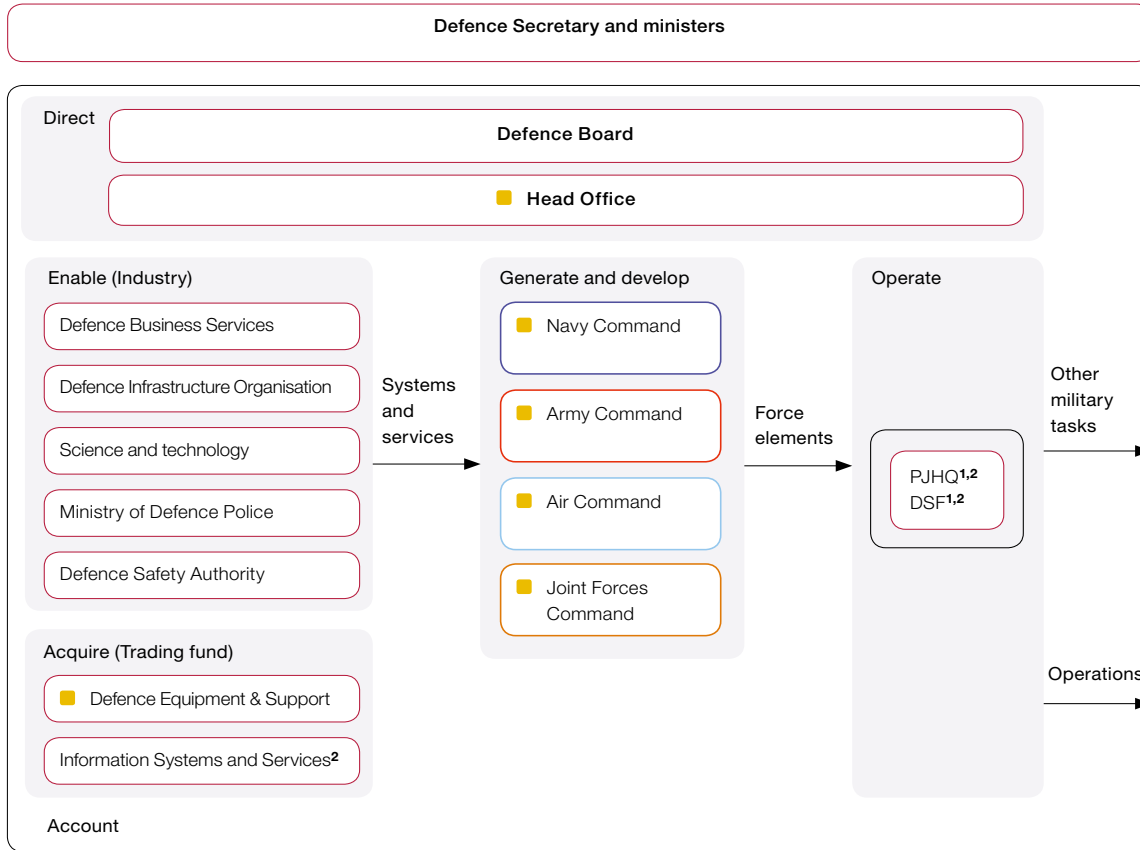
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How the Department is organised



■ Acquisition system

Notes

- 1 PJHQ = Permanent Joint Headquarters; DSF = Directorate of Special Forces.
- 2 Within Joint Forces Command.

Source: Ministry of Defence Annual Report and Accounts 2015-16, Ministry of Defence, [How Defence Works](#), December 2015

The Defence Council is chaired by the Secretary of State for Defence and provides the formal legal basis for defence in the UK through a range of powers over the Armed Forces and, in particular, their command and administration. The Defence Council does not take part in the strategic direction and oversight of defence, which is provided by the Defence Board.

Stephen Lovegrove took over the post of Permanent Secretary from Jon Thompson on 25 April 2016. The permanent secretary is the government's principal civilian advisor on defence, has primary responsibility for policy, finance and business planning, and is the Departmental Accounting Officer. In January 2016 the Queen approved the appointment of **Air Chief Marshal Sir Stuart Peach** to take over from General Sir Nicholas Houghton as the next Chief of the Defence Staff in July 2016. The Chief of Defence Staff (CDS) is the professional head of the Armed Forces and principal military advisor to the Secretary of State and the government.

The Defence Board is the senior committee in Defence, chaired by the Secretary of State. It is supported by three sub-committees:

- the Investment Approvals Committee – which considers major investment decisions on behalf of the Defence Board.
- the Defence Audit Committee – which reviews and challenges the adequacy of internal controls and processes to manage risk.
- the People Committee – which provides direction, guidance and oversight on all matters to do with defence people and training issues.

The Defence Infrastructure Organisation comprises around 4,500 employees. It is responsible for building, maintaining and servicing the infrastructure needed to support defence. This includes providing service family accommodation, managing the defence training estate, and overall managing 4,000 sites worldwide.

The Defence Equipment & Support organisation comprises around 11,100 people. It is now classified as a bespoke trading entity, and an arm's-length body of the Ministry of Defence. It is responsible for managing large defence projects to buy and support the equipment and services that the Royal Navy, British Army and Royal Air Force require to operate effectively.

The new **delegated operating model** originated from Lord Levene's 2010 Defence Reform Review, and became fully operational on 1 April 2014. Under this model, Defence is organised into six 'Top-Level Budgets' (TLBs): The four Commands, Head Office and corporate services, and the DIO. The head of each TLB is personally accountable for the performance of their organisation.

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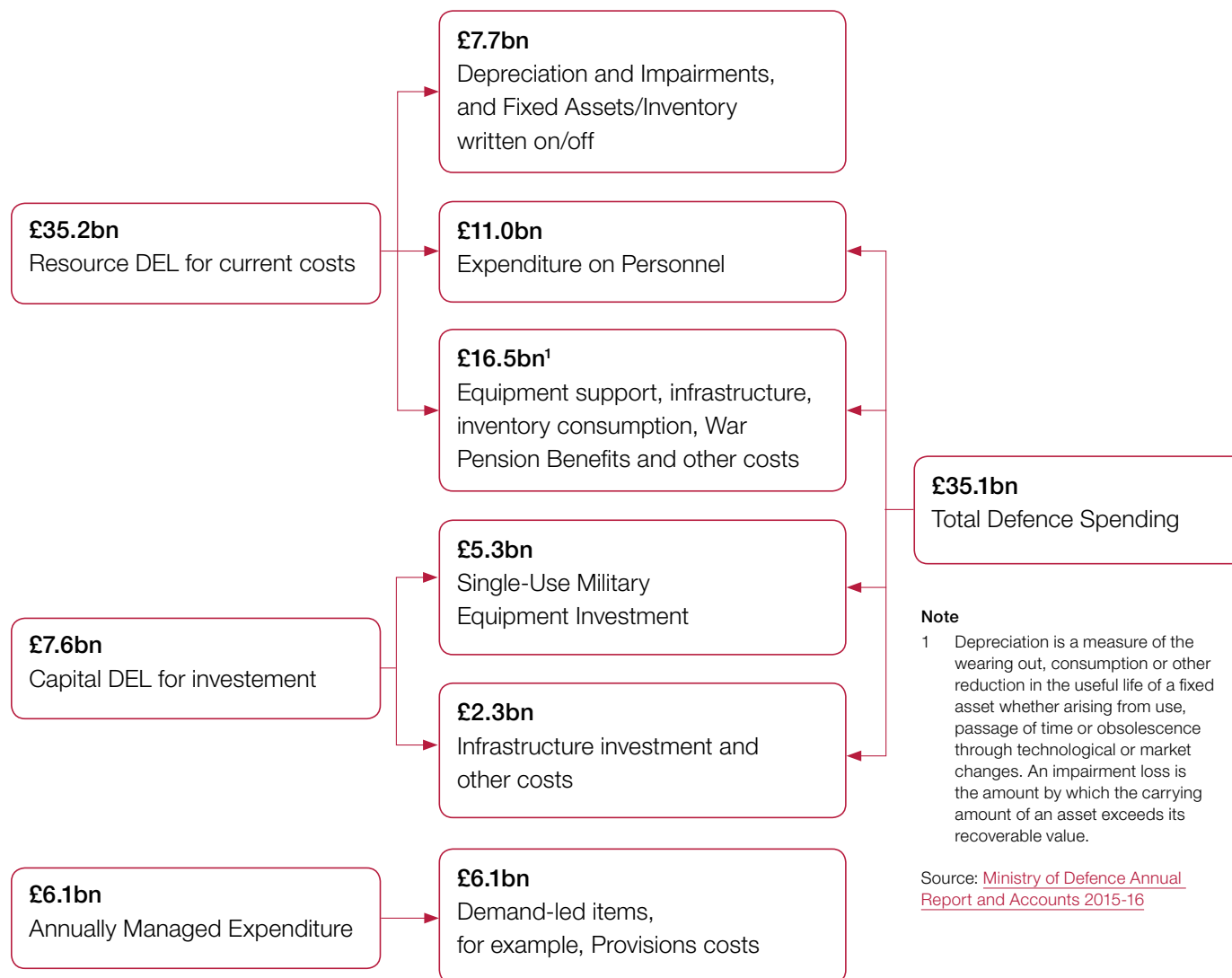
Where the Department spends its money

Total defence spending was £35.1 billion in 2015-16

Total Defence Spending is the Department's spend on areas such as Personnel, Equipment and Equipment Support.

It does not include accounting treatments such as depreciation of assets including buildings and equipment, or Annually Managed Expenditure (AME) which is 'demand-led' spend not easily controlled by the Department. AME encompasses spend on provisions (largely nuclear decommissioning provisions) as well as financial derivative movements.

When depreciation and AME are included, the total is £48.9 billion. This is known as 'Total Defence Outturn'



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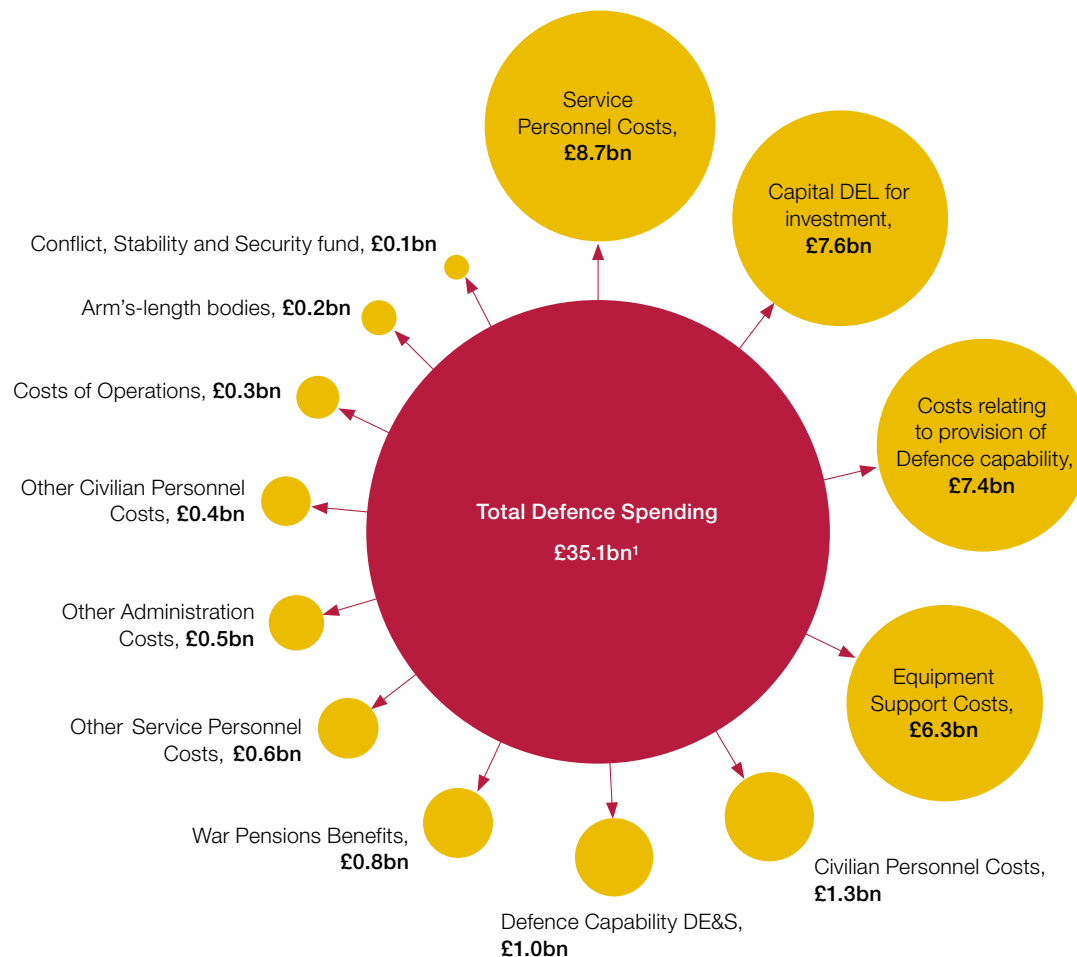
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Where the Department spends its money *continued*



Note

- 1 Total Defence Spending represents cash Resource DEL and Capital DEL for investment.
- 2 Numbers may not add up to the total due to rounding.

Source: Ministry of Defence Annual Report and Accounts 2015-16

Service Personnel Costs – includes pay, pensions and allowances for Military Personnel (RDEL).

Capital DEL for Investment – the capital investment that the Department has made in military equipment and other capital items, that provide long-term benefit for the Department (CDEL).

Equipment Support Costs – the cost of supporting the capital investment items that the Department has purchased for the long-term (RDEL).

Costs of Operations – relates to the cost of military operations, which are reported separately as operations funding is provided in 'pools' to the Department for use on operations that arise (RDEL).

Costs relating to the provision of Defence Capability – includes the cost of using inventory items by the Department, Research and Development and miscellaneous costs and services for which the Department incurs expenses. It is offset by income the Department receives (RDEL).

Civilian Personnel Costs – includes pay, pensions and allowances for Civilian Personnel (RDEL).

Defence Capability DE&S – relates to the cost of implementing the Department's Equipment Plan (RDEL).

War Pension Benefits – cost of pension contributions for staff in the War Pensions Benefit scheme (RDEL).

Other Administration Costs – cost of administration not related to direct frontline service provision (RDEL).

Other Civilian and Service Personnel Costs – includes the staff costs incurred in relation to central government administration (RDEL).

Arm's-length bodies – relates to the Grant in Aid funding that the Department provides to bodies within its accounting boundary (RDEL).

Conflict, Stability and Security Fund – relates to expenditure into a cross-government fund set up to tackle conflict and instability overseas (RDEL).

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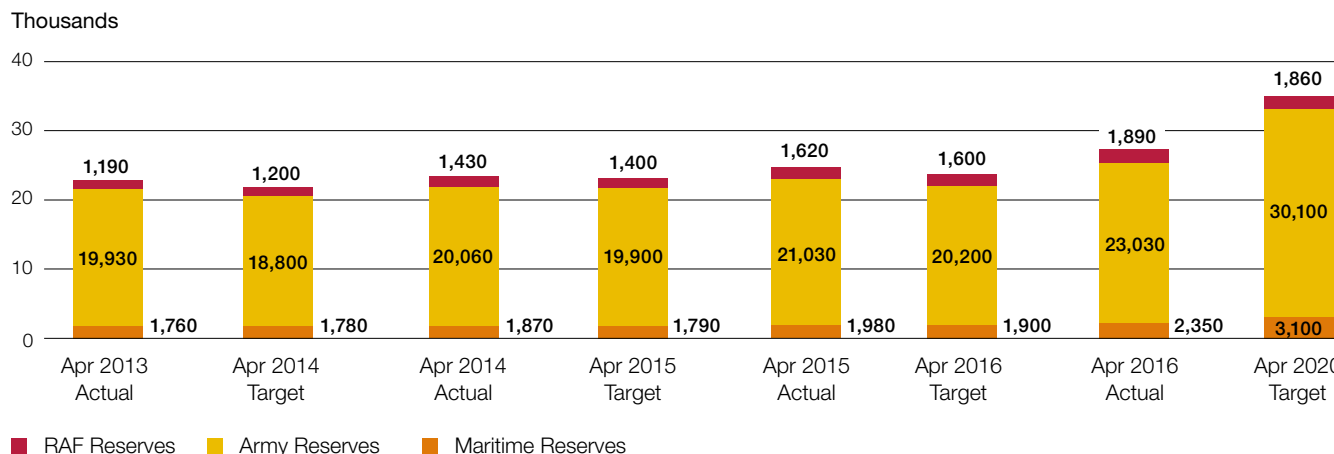
Achieving and sustaining the appropriate size of military and civilian personnel with the right skills to deliver its objectives is a major challenge for the Department.

In its [Single Departmental Plan](#), the Department has made commitments to:

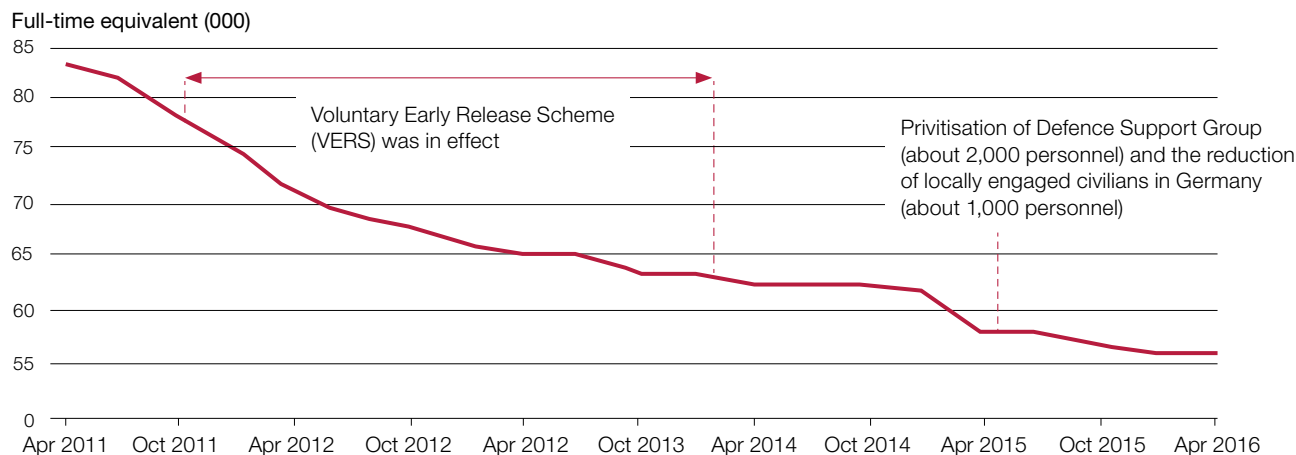
- maintain the size of the regular armed services and not reduce the army to below 82,000; and
- expand the reserve forces to 35,000.

The civilian workforce has been falling continuously for many years, in particular during the period of the Voluntary Early Release Scheme between 2011 and 2014 (bottom right). The SDSR set an objective of reducing the civilian workforce by 30% to 41,000 by the end of this Parliament.

Trained strength of the future reserves 2020 Volunteer Reserves against annual targets



Ministry of Defence departmental civilian personnel strength (full-time equivalent)



Source: Ministry of Defence Annual Report and Accounts 2015-16, Ministry of Defence Single Departmental Plan 2015–2020

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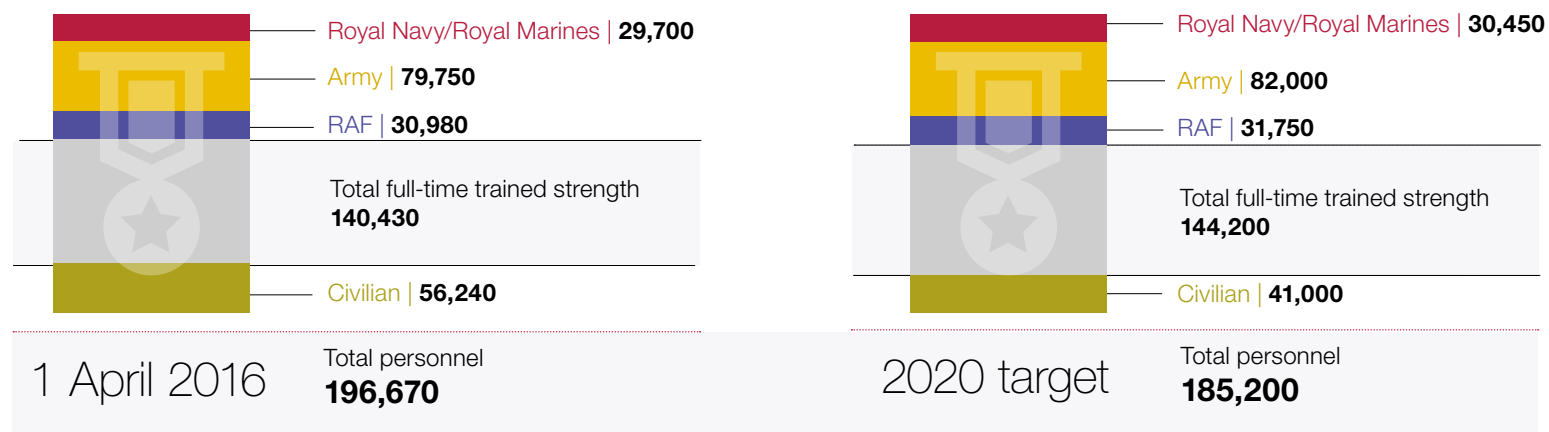
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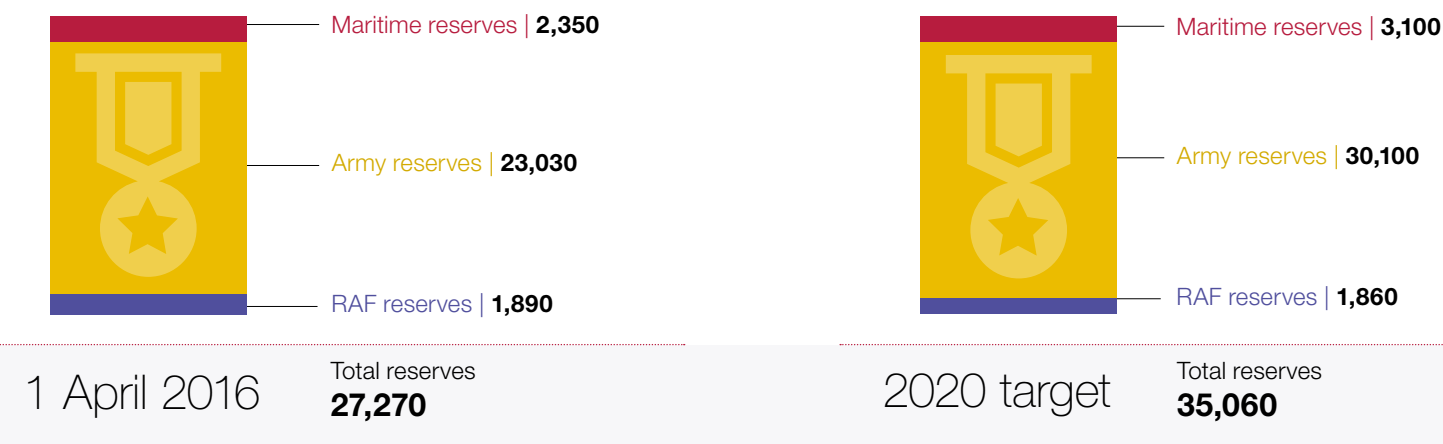
Military and civilian personnel *continued*

Trained Military personnel and civilians

Military full-time trained strength and civilians



Future reserves 2020 – volunteer reserves trained strength



Source: Ministry of Defence Annual Report and Accounts 2015-16, Ministry of Defence Single Departmental Plan 2015–2020

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2015 Strategic Defence and Security Review

The 2015 Strategic Defence and Security Review

The [2015 Strategic Defence and Security Review](#) (SDSR) sets out four particular challenges which are likely to drive UK security priorities for the coming decade.

They have both immediate and longer-term implications:

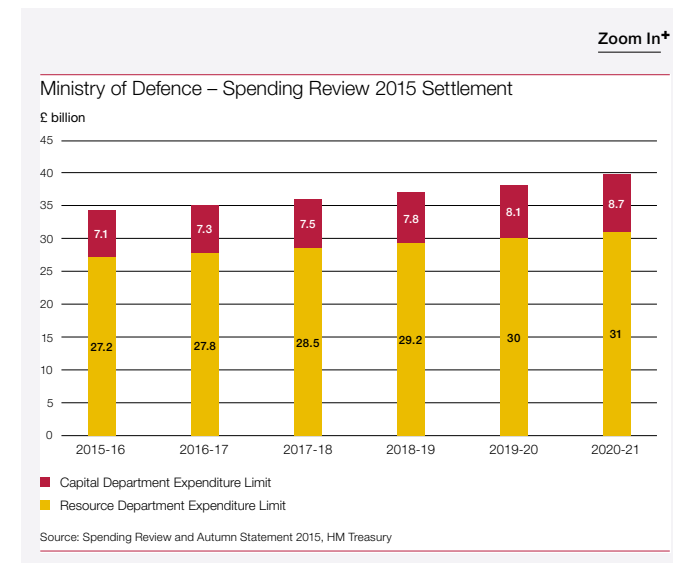
- 1 The increasing threat posed by terrorism, extremism and instability.
- 2 The resurgence of state-based threats; and intensifying wider state competition.
- 3 The impact of technology, especially cyber threats; and wider technological developments.
- 4 The erosion of the rules-based international order, making it harder to build consensus and tackle global threats.

The 2015 SDSR represented the government's five-year forward look, assessing the challenges facing the UK and the government's response, while meeting wider government objectives.

The [Ministry of Defence's settlement at the 2015 Spending Review](#) funds the SDSR in full.

This includes:

- increasing the Department's budget by 3.1% in real terms to 2019-20 as part of the government's commitment to spend 2% of GDP on defence. In the summer Budget 2015 the government confirmed that it would maintain the NATO 2% target, and committed to a growth in the Defence budget of 0.5% above inflation each year of this Parliament;
- an investment of £1.2 billion over 10 years to ensure a Queen Elizabeth Class aircraft carrier is able to deploy with 24 jets on board from 2023, as well as investing almost £2 billion in UK Special Forces. As a result of new investments the 10-year Equipment Plan will rise from £166 billion to £178 billion (7.2%);
- £2.1 billion from the Joint Security Fund to fund and deliver the SDSR commitments in full, maintaining the current personnel levels of the Armed Forces and building four new submarines to renew the nuclear deterrent; and
- savings of £9.2 billion, including £2 billion from military and civilian pay restraint, £2.1 billion from improved commercial terms in the Equipment Plan, and reprioritisation of £2 billion of existing funding, all of which will be reinvested to fund the SDSR commitments.



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Introduction to the Financial Audit

Purpose of the Financial Audit

The National Audit Office's (NAO's) financial audit is primarily conducted to allow the Comptroller and Auditor General to form an opinion on the truth and fairness of the accounts of the Department and its arm's-length bodies, and the regularity of the expenditure and income reported therein. In the course of these audits, however, the NAO learns a great deal about the Department's financial management and other aspects of the Department's control framework.

Timeliness of reporting

The [Department's 2015-16 accounts](#) were laid before Parliament on 14 July 2016. This was the second consecutive year that the accounts were laid before the summer recess, representing sustained improvement in the Department's accounts production process.

On 1 April 2014, DE&S became an agency of the Department and began operating as a Bespoke Trading Entity. As such, it prepared its own accounts for the first time. Due to the complexities involved in establishing an accounting boundary between DE&S operating and equipment programme activities and weaknesses in the departmental financial management, the first accounts presented were qualified and not laid until 17 December 2015. Given the limited time before then and the close of the 2015-16 financial year, DE&S decided that the 2015-16 accounts would also be laid

post-summer recess, and publication is scheduled for autumn 2016. The 2015-16 accounts of the Department's other arm's-length bodies were laid to timetable.

The Comptroller and Auditor General's opinions

The Comptroller and Auditor General (C&AG) qualified his opinion on the 2015-16 departmental accounts for a seventh successive year as the Department has not complied with the accounting requirements for determining whether the contracts it holds have the features of a lease. 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 or predominantly on defence contracts.

The Department has previously decided, in agreement with HM Treasury, not to implement the accounting standard for existing contractual arrangements given the complexity, time and considerable costs it would involve. It has decided, however, to improve compliance for new single contracts affecting a single site going forward, and intends this to act as a pilot to allow it to further understand the challenges and resources required to improve compliance.

The C&AG qualified his opinion on the 2014-15 DE&S Accounts on the basis that limited evidence was provided to verify: external private sector support costs, such as technical expertise, in the Statement of Comprehensive Net Expenditure; and the related trade and other payables balance in the Statement of Financial Position.

DE&S is aiming to improve financial management systems, processes and controls in response to this, but has recognised that there remains a credible risk that the improvements it is striving to achieve may not be suitably developed to secure an unqualified audit opinion on the 2015-16 financial statements.

The 2015-16 accounts of the Department's other arm's-length bodies whose audits have concluded have received unqualified audit opinions (see [Appendix Three](#)).

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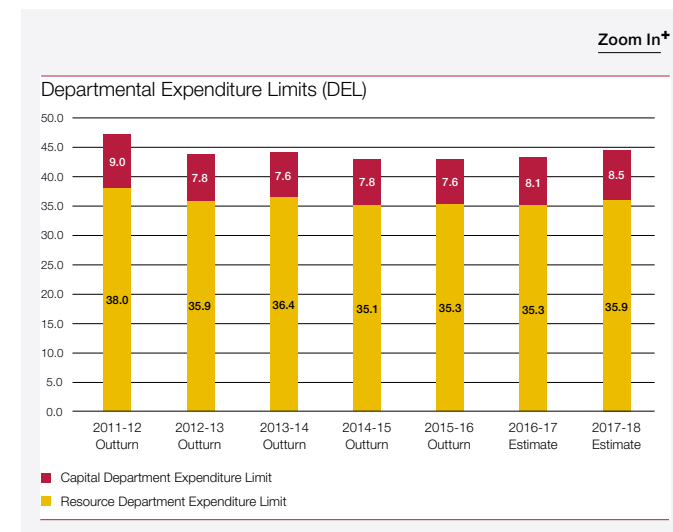
The Department's budget

The budget that is allocated to and spent by government departments is known as the Departmental Expenditure Limit (DEL). Like other government departments, the Department has been operating within a strict budget during 2015-16 and has had to accommodate a reduction of budget of around £500 million during the year in order to meet the government's overall budgetary targets.

The Department's historic pattern of underspend on Resource DEL has continued in 2015-16, being £1 billion against a voted amount of £36.3 billion (2.7%). However, the pressure on the Capital DEL budget was much higher, with an underspend of £47.8 million against a voted amount of £7.6 billion. The Department, with the agreement of HM Treasury, flexed £660 million of funding from RDEL to CDEL as part of its Supplementary Estimate. In addition, and in recognition of future funding pressures, the Department sought to bring forward capital investment and sought permission from HM Treasury to score a proportion of profit from asset sales to CDEL to help fund these transactions.

In addition to its DEL spending, the Department also manages Annually Managed Expenditure (AME), additional budget allocated to departments which is spent on items which may be unpredictable or not easily controlled. The pattern of AME spending in 2015-16 mirrored that of DEL, with a Resource AME underspend of £2 billion against a voted amount of £8.1 billion and a much smaller Capital AME underspend of £70.8 million against a voted total of £100 million.

While the Department did not exceed any of its Parliamentary control totals in 2015-16, budgetary pressure is likely to continue going forward.



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Provision for future costs

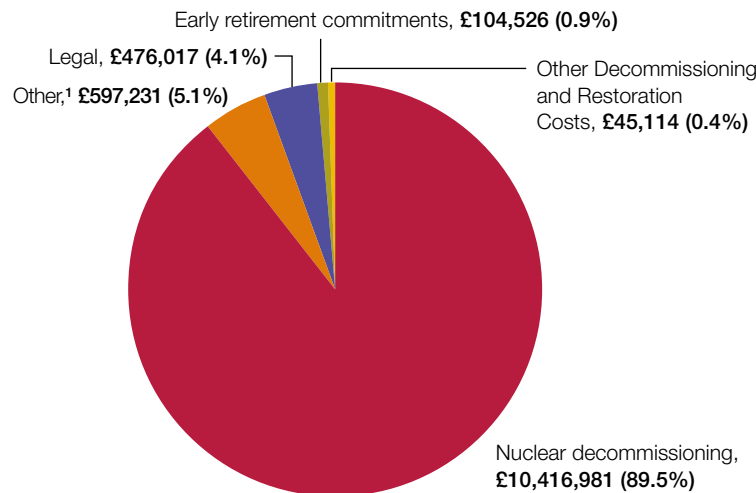
Provision is made in financial statements for a range of future costs, reflecting the future liability and financial commitments generated by decisions already made.

The Department holds a number of provisions totalling £11.7 billion – the most significant of these are its provisions for nuclear decommissioning liabilities (£10.4 billion). These liabilities arise as a result of the Department's nuclear programme and include decommissioning costs primarily from the operation and maintenance of the country's nuclear submarine fleet.

During 2015-16, following previous NAO recommendations, the Department undertook a review of its nuclear decommissioning liabilities. This review identified that these liabilities were previously understated by £691 million. As this matter was deemed significant to the accounts as a whole, an adjustment was made to restate the balance reported in the previous year's accounts. The Department had planned for this restatement by seeking additional non-budget voted resource expenditure as part of its Estimate voted by Parliament.

The restated provision for nuclear decommissioning further increased by £5.7 billion to £10.4 billion in 2015-16; £5.6 billion of this increase was as a result of the change by HM Treasury in the long-term discount rate applied to cash flows due over 10 years – from 2.2% to -0.8% – in effect increasing the cost of payments in future years. A discount rate is applied in order to fairly state the value of a future payment the Department is required to make. The actual increase was lower than the Department had originally envisaged, contributing to the underspend in its Resource AME.

Statement of Financial Position – Provisions



Note

1 £441 million of this balance relates to personal liabilities in respect of Locally Employed Civilians in Cyprus and Gibraltar.

Our audit of the accounts

Findings from our recent value-for-money studies

Relevant findings from recent cross-government reports

Introduction to the Financial Audit

The Department's budget

Provisions for future costs

The Governance Statement

Improving controls and assurance

The Governance Statement

In its 2015-16 Governance Statement, the Department outlined its significant risks and issues and described how it is addressing them.

Areas of Board focus:

- The delivery of operational capability.
- Implementation of the SDSR.
- The Defence Transformation programme and the evolution and strengthening of the delegated model between the front-line commands and the centre, and the ongoing reform of DE&S.
- The governance and management of the Nuclear Enterprise.
- Staff retention, skills, the creation of contingent capability and the roll-out of the New Employment Model.
- The continued development of information technology systems and cyber-security.
- Strengthening contract management, strategic partnerships and commercial skills.
- Estate management and rationalisation.
- Health and safety of the workforce.

Significant Control Risks reported in the Governance Statement:

- Commercial awareness, skills and contract management.
- Progress on the renewal and renovation of the Oil Fuel Depot asset portfolio.
- Spending on estates contracts exceeded HM Treasury and Cabinet Office approval limits resulting in a financial sanction of £31.6 million and a reduction in delegated spending limits.
- Shortcomings in the delivery of the Service Families Accommodation maintenance services contract.
- High senior management turnover in the DIO's executive management team.
- Delay in production of the Footprint Strategy for the future of the Defence estate.
- DIO management information, data quality and a large number of fragile legacy systems.
- Recruitment and retention of staff and shortages in specific skills across the Department.

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Improving controls and assurance

Improving controls and assurance

The Risk and Control Framework

Control environment

The Department's control environment has historically experienced inconsistent application and non-compliance across Top-Level Budget holders (TLBs) and Defence Authorities (DAs). This has in turn contributed to the identification of financial error through the financial audit. The Department has engaged on a programme to develop its Internal Control and Assurance Framework for key financial processes to improve the overall control environment (ICAF). Implementation and testing of the framework is under way, as is the design of controls for wider processes. Also in the year the Department removed the outsourced management insert for its business services, and going forward will explore the extent to which an outsourced shared services model may be appropriate for the provision of financial and wider services.

The Department has also introduced a standard reporting template to support its annual assurance process, covering key governance, risk management and internal control matters for completion by TLBs and DAs. Using these, the Department produces an overall Departmental Annual Assurance Report.

Reflecting the ongoing development of the control framework, the overall assurance level for 2015-16 was one of 'limited assurance'.

Following the implementation of an upgrade to its accounting systems in 2015-16, in the current financial year the Department is aiming to implement a new Contract, Purchasing and Finance system (CP&F), which along with the related data-cleansing exercise, is designed to address a number of the weaknesses in contract management, contributing to improved controls and improved management information.

Defence Internal Audit (DIA)

An annual risk-based programme of internal audit is provided by Defence Internal Audit, covering the Department's strategic and operational risks and key operational processes. Overall, the opinion provided by the Group Head of Internal Audit for 2015-16 was 'limited assurance', the same as in the previous three years. In his annual report he highlighted the following:

- The Department has taken major steps forward in improving its ability to identify, assess and manage risks, with the Defence Board fully engaged, and risk beginning to drive Board agendas across the Department.

- While areas of good control could be found at a business or operational level across the Department, there was still a gap between this and policy and intent at Defence Authority-level.
- Generally, improvements were needed in feedback, oversight and assurance mechanisms.
- Areas of challenge for the Department were commercial management and resilience, and capacity and capability within the workforce.

Evolving risk management framework

A revised risk management framework has been implemented across the Department during the year. This has centred around revised quarterly risk reports that are considered by the Defence Board and which focus on the Board's strategic risks as well as reporting shorter-term delivery risks, and the key risks being managed by TLBs and DAs. This is supplemented by a rolling programme of risk reviews where the Board subjects one strategic risk to a detailed discussion at monthly board meetings.

Our audit of the accounts

Findings from our recent value-for-money studies

Relevant findings from recent cross-government reports

Strategic Financial Management and Service Family Accommodation

Major Projects and Equipment Plan

Impact of the SDR on the Equipment Plan

Findings from our recent value-for-money studies

Strategic Financial Management in the Ministry of Defence **(July 2015)**

The Ministry of Defence's strategy for improving its financial management is delivering results. In 2010 we found that the Department had over-committed and experienced considerable budget changes and uncertainty. To address the gap between its forecast costs and available funding the Department: cancelled some projects; took other equipment out of service earlier than planned; and put in place the Equipment Plan, for buying and supporting equipment over the next 10 years.

Despite this, we found risks remain to the continued balance of the Defence budget. Workforce costs are the Department's biggest area of budget and any small change in the Department's assumptions could impact significantly on overall costs to the Defence budget. The Department's estate is significantly larger than it can afford. It also needs to deliver £6 billion assumed in the future equipment budget allocations. The Department recognises that DE&S and DIO do not currently have the skills they need to deliver what is required of them. DE&S has a transformation programme under way designed to address this.

Service Family Accommodation (June 2016)

Between 2009-10 and 2014-15 the Department invested £886 million in Service Family Accommodation (SFA). In April 2016 the Department assessed that 87% of service family accommodation properties meet or exceed the decent homes standard, the government's minimum standard for all those housed in the public sector.

However, a significant proportion of service personnel were dissatisfied with the standard of their homes. In 2016 only 50% were satisfied with the overall standard, 32% with responses to their maintenance and repair requests, and only 29% satisfied with the quality of this repair work.

The private sector provider CarillionAmey, was awarded a contract in 2014 to maintain SFA. There is a deep level of dissatisfaction with the service provided and at the start of 2016, CarillionAmey received more than 1,000 complaints a month.

The Secretary of State met with the two parent companies in February 2016 to agree an improvement plan. A decision on continuing the contract will be taken later in 2016.

Findings from our recent value-for-money studies *continued*

Major Projects Report 2015 and the Equipment Plan 2015–2025 (October 2015)

The NAO audits the Department’s 10-year Equipment Plan annually. In October 2015 we found that overall costs and performance remained relatively stable over 2014-15. However:

- the Department will need to remain vigilant with regard to uncertainties about future cost increases in high-value projects still at an early stage;
- how the Department manages a small number of very large procurement projects will be crucial to the Plan’s long-term affordability. Projects such as the Astute submarines, Successor and Type 26 Frigates account for a large degree of the possible understatement of costs, and carry significant delivery risks; and
- the Department’s Affordability Statement should be clearer about uncertainties in the costs within the Plan. It does not explain the range of possible cost outcomes across projects, even though it is good practice to recognise risk and uncertainty when forecasting project costs.

Planned spend includes:



Findings from our recent value-for-money studies *continued*

Impact of the Strategic Defence and Security Review on the Equipment Plan (June 2016)

Between 2010 and 2012 the Department focused on closing a £38 billion funding gap in its plans for purchasing equipment and support.

Since 2012 it has published an annual statement on the affordability of its Equipment Plan. This is a 10-year rolling budget for a core programme of key equipment projects (both procurement and support). The Department makes an annual statement to Parliament on whether it can afford to pay for its Equipment Plan.

It is made up of a 'core programme' of key equipment projects where funds have been committed and a 'contingency' – to accommodate rising costs on these projects; and 'headroom' – uncommitted funds.

SDSR 2015 included a number of announcements for additional commitments. These included:

- 2 additional Typhoon squadrons;
- 9 additional F35 Lightning aircraft;

- 9 new Boeing P-8 Poseidon aircraft;
- 20 new Protector armed remotely piloted aircraft;
- an additional £2 billion to Special Forces;
- 2 new strike brigades of up to 5,000 personnel; and
- Apache attack and Chinook support helicopter upgrades.

In advance of our 2016 report on the Equipment Plan, we produced an interim analysis looking at how the SDSR and the funding commitments made in it affected the Equipment Plan.

The SDSR included new spending commitments of £25.6 billion. The figure (on [page 20](#)) shows how the additional commitments will be funded. This includes a new Joint Security Fund for the Armed Forces and the security and intelligence agencies, which the SDSR states will grow to £1.5 billion by the end of this Parliament.

The new commitments set out in the SDSR will increase the pressure on the Department to manage existing challenges to affordability. As a result, the Department has now committed funding that it was previously holding back for future capability improvements ('headroom'). This means that the proportion of the Plan not committed has fallen from 8.3% in 2015 to 2.8% in 2016, giving it far less room to accommodate any new capability in the future.

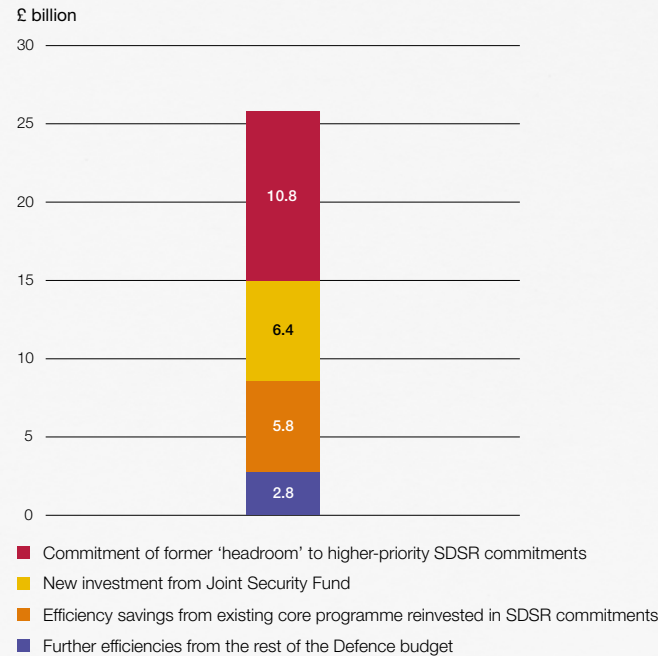
Efficiency savings will be made by a range of actions including improvements delivered by the DE&S transformation programme, implementation of the Single Source Contract Regulations, pay restraint through the 1% cap on public sector pay, and reductions in civilian manpower.

Findings from our recent value-for-money studies *continued*

Our interim analysis concluded that the Department must assure itself that:

- its cost estimates for new commitments are robust;
- it has sufficient controls in place to restrict growth in costs, when there is a risk the Plan is understated by around £5 billion, and with £1.3 billion of the contingency ring-fenced for the procurement of the Nuclear Enterprise (the deterrent and supporting activities); and
- it can identify and track the efficiency savings required to fund new commitments, including the contributions of the DE&S organisation and the Single Source Regulation Office.

Sources of investment for additional SDRS commitments in 2016 Equipment Plan



Note
1 Figures may not reconcile exactly due to rounding differences.

Source: Ministry of Defence



Relevant findings from recent cross-government reports

The NAO reports on strategic issues and themes across government. Given its size, the Ministry of Defence is often a case study in these reports.

Use of Consultants and Temporary Staff (January 2016)

- DE&S in 2013-14 spent £481 million on contractors, technical support staff and other temporary staff in similar specialist roles. They remain employed by external organisations but work day to day supporting the Department, which classifies these resources mainly as external suppliers rather than as temporary staff.
- The Department spends around 10% of its civilian payroll costs on temporary staff and consultants.
- As at May 2015, the Department employed two temporary members of staff earning more than £1,000 a day, for whom total annualised costs would be £462,000.

Key findings on departments' use of consultants and temporary staff:

- Government spending on these staff has reduced significantly since 2010, when strict spending controls were introduced, but is now increasing once more.

- Strategic workforce planning is critical in managing cost pressures, but is under-developed in departments.
- Compliance with departmental approval processes is weak in some departments.
- Departments are generating limited competition for both consultancy and temporary staff assignments.

Investigation into the acceptance of gifts and hospitality (February 2016)

- The Ministry of Defence was one of two departments not to collect information centrally on the acceptance of gifts and hospitality, which does not allow them to look at trends across the Department.
- Officials in DE&S accepted the most hospitality both in frequency and monetary value compared with other government departments. They accepted 5,213 offers of hospitality in the year 2014-15.
- 17% of DE&S officials accepted gifts and hospitality with an estimated value of some £100,000. This compares with 3% of the Department for Business, Innovation & Skills (now the Department for Business, Energy & Industrial Strategy) officials – with a value of £35,000.

- DE&S accepted hospitality from around 600 organisations; the most frequent providers were major defence contractors, including 581 times by BAE Systems.
- The Department follows good practice in requiring officials to record all offers of gifts and hospitality, including those that are declined, and examples given of what is and is not appropriate. However, no prior approval is required, and it is not clear what sanctions would be imposed for breaches of the policy.

Relevant findings from recent cross-government reports *continued*

Government's spending with small and medium-sized enterprises (March 2016)

- The government has set a target of 33% of procurement spend going to SMEs by 2020, an increase on its earlier target of 25%.
- As the Ministry of Defence accounts for around 44% of government procurement spend, reaching this target relies heavily on the Department's performance.
- In 2014-15, 19% of the Department's procurement spend reached SMEs. The other 16 departments collectively reported 33% of spending reaching SMEs.

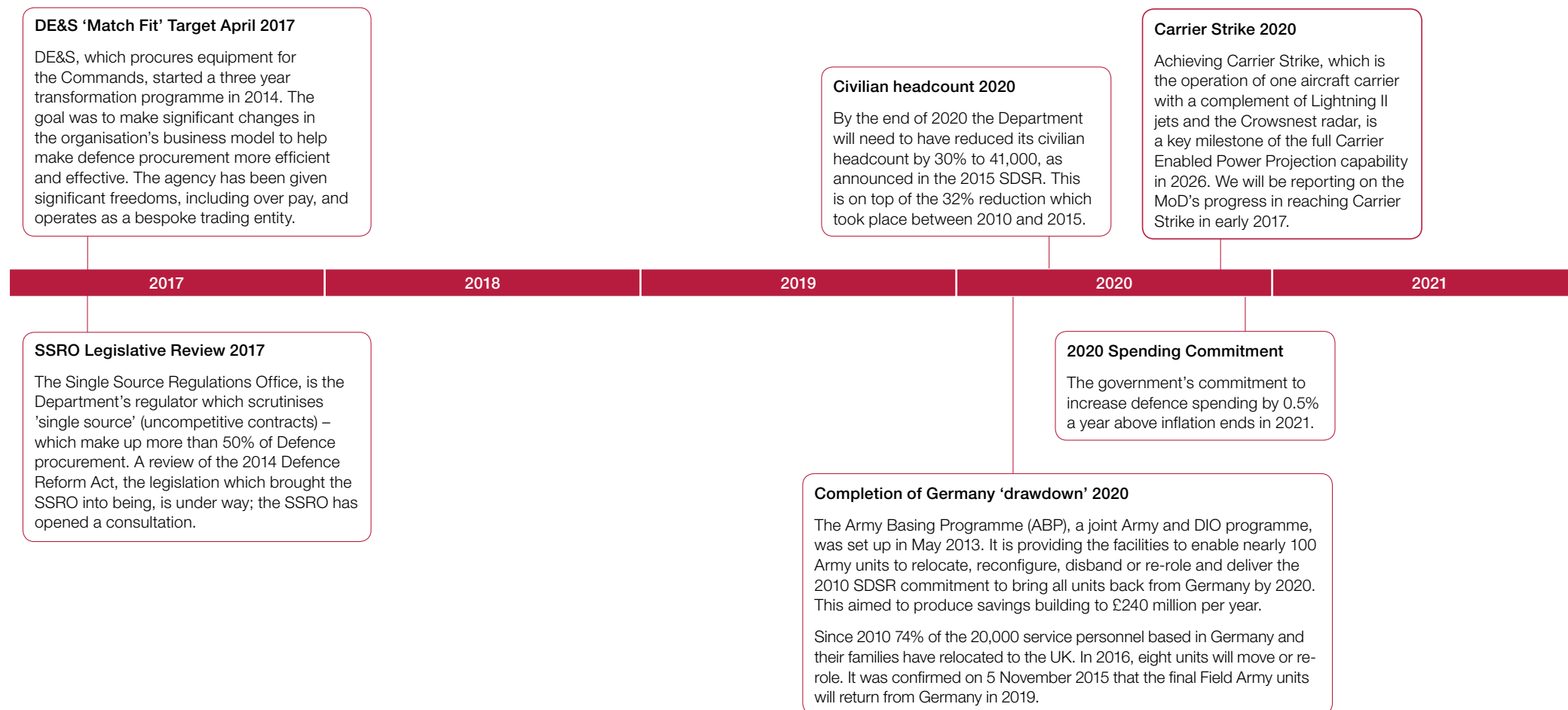
The Department believes it will be challenging to increase its SME spending further but has agreed to achieve 25% by 2020. It has already committed large proportions of its annual spending and is unlikely to be letting many further large contracts during the current Parliament.

Disposal of public land for new homes: a progress report (July 2016)

- The government has set a target of releasing enough surplus public sector land for 160,000 new homes between 2015 and 2020. The 2015 Spending Review also set a wider target of raising £5 billion across government, of which the Ministry of Defence aims to contribute £1 billion, from the sale of surplus land and buildings.
- Defence will make the largest contribution, with a target of releasing enough land with future capacity for 55,000 homes.
- The Defence target will depend on its 'Footprint Strategy', which is expected in autumn 2016. An analysis of this will form part of our forthcoming 'Delivering the Defence Estate' report due in November 2016.

Future defence developments	Project and programme management	Delivering major Defence projects	Infrastructure and Projects Authority	Commercial and Contracting	Workforce capability	Key challenges
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Future defence developments in five-year horizon



Future defence developments

Project and programme management

Delivering major Defence projects

Infrastructure and Projects Authority

Commercial and Contracting

Workforce capability

Key challenges

Project and programme management

In September 2015, the Government's Major Projects Portfolio (GMPP), which includes the biggest and riskiest projects, comprised 143 projects with estimated whole-life costs of £405 billion. Of these, 100 projects are due to be delivered in this Parliament but four have durations of more than 25 years. Some span several departments or seek to meet multiple objectives.

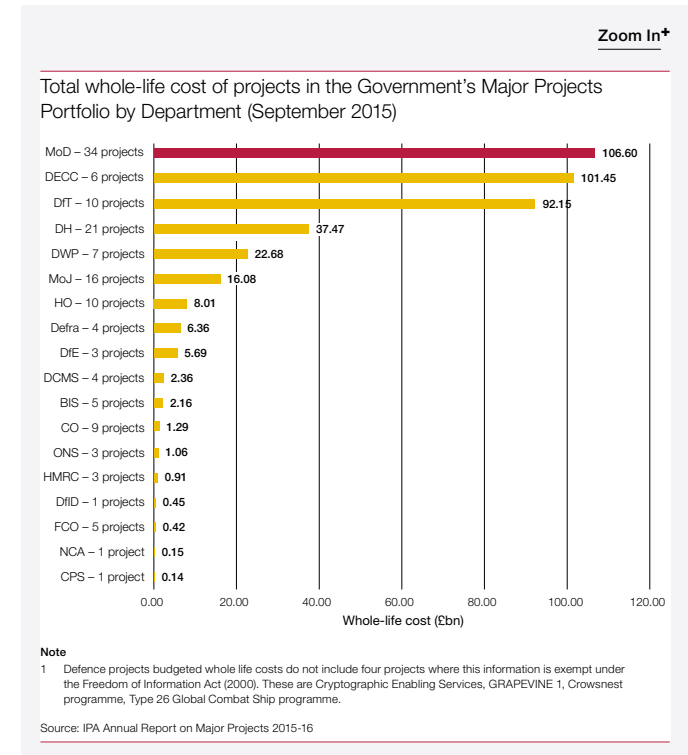
The Ministry of Defence's major projects are the biggest component of the GMPP. Its 34 projects make up almost a quarter of the Portfolio with combined whole-life costs of £107 billion, around 26% of the total value of the Portfolio. Three departments – Ministry of Defence, (the former) Department of Energy & Climate Change (DECC) and Department for Transport (DfT) – accounted for 74% of the portfolio by value.

The Ministry of Defence accounts for the second largest group of projects (after DECC) which left the GMPP (£57 billion of whole-life cost). The largest project was the £20 billion Typhoon programme, which is delivering an agile, multi-role combat aircraft. Contracts have now been placed for 160 aircraft to be delivered in three tranches, which will be overseen by the Department.

The Department has a challenging portfolio of complex projects and programmes to deliver. The majority are large equipment procurements, but there are also large-scale transformation programmes. There are also projects to introduce new systems. Skills shortages in project and programme management, digital and commercial, combined with a lack of capacity to undertake a growing number of projects remains a challenge.

The NAO's work across government on managing major projects and programmes has found the biggest challenges facing the centre of government and individual departments over this Parliament are to:

- encourage departments not to make firm commitments on cost and timescales for delivery before their plans have been properly tested;
- develop an effective mechanism whereby the centre of government can prioritise all major projects according to strategic importance, and capability is deployed to priority areas; and
- make sure departments and the centre of government put in place systems and data which allow proper performance measurement of projects and their corresponding portfolio.

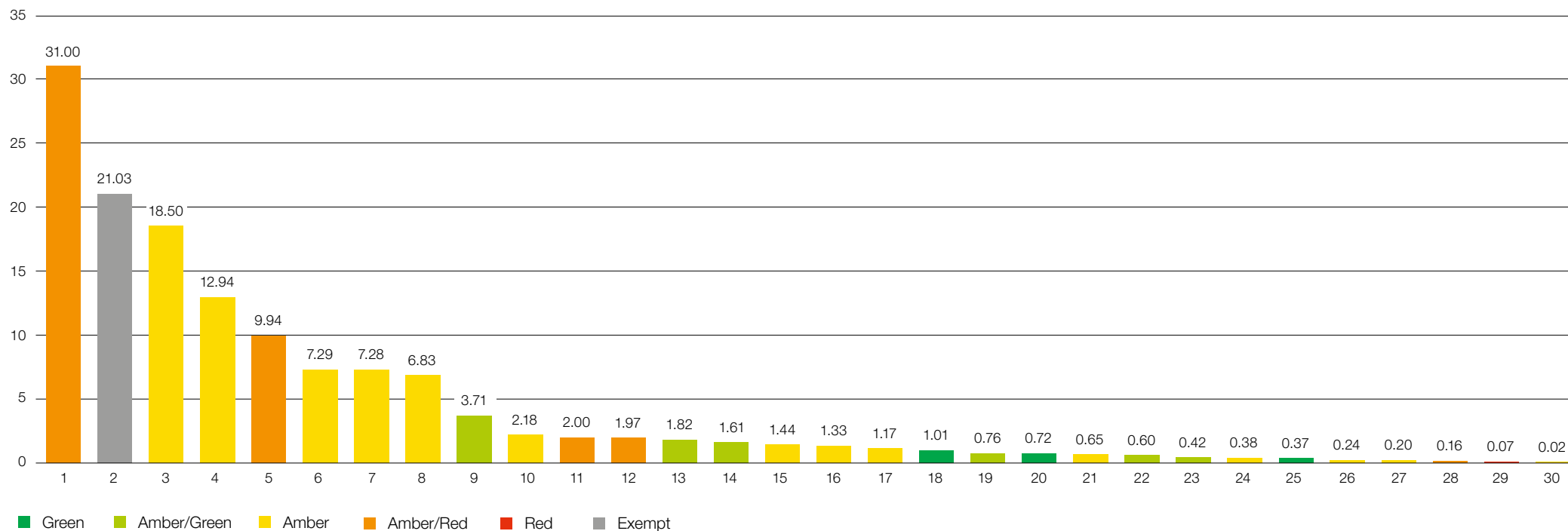


Future defence developments	Project and programme management	Major Defence projects	Infrastructure and Projects Authority	Commercial and Contracting	Workforce capability	Key challenges
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Government Major Projects Portfolio: Defence projects

Total budgeted whole-life costs

£ billion



1 Successor at SSBN; 2 Nuclear Warhead Sustainment Programme; 3 Complex Weapons; 4 Lightning II Programme; 5 Astute Boats 1-7; 6 Queen Elizabeth; 7 Future Beyond Line of Sight; 8 Armoured Cavalry 2025; 9 A400M; 10 Armoured Infantry 2026; 11 Army Reserves Development Programme; 12 Army Basing Programme; 13 MARSHALL; 14 Wildcat Programme; 15 Core Production Capability; 16 GRAPEVINE 2; 17 WATCHKEEPER; 18 CHINOOK (including Project Julius); 19 Airseeker; 20 Merlin Programme; 21 Logistics Commodities Services Transformation; 22 Maritime Sustainment Programme; 23 Spearfish Upgrade Programme; 24 The Material Strategy; 25 PUMA; 26 EMPORIUM; 27 New Employment Model; 28 Contracting, Purchasing and Finance; 29 Operational Information Services; 30 Carrier Enabled Power Projection.

Notes

- 1 Type 26, Crowsnest, Grapevine 1 and Cryptographic Enabling Services total budgeted whole-life costs are not included as data is exempt under Section 43 of the Freedom of information Act (2000).
- 2 Delivery confidence rating for Nuclear Warhead Capability Sustainment Programme is exempt under Section 43 of the Freedom of information Act (2000).

Source: [Ministry of Defence Government Major Projects Portfolio data](#), September 2015

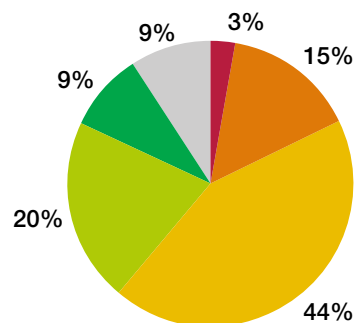
Future defence developments	Project and programme management	Delivering major Defence projects	Infrastructure and Projects Authority	Commercial and Contracting	Workforce capability	Key challenges
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Infrastructure and Projects Authority: Assessment of Defence projects

The figure below shows the movement in ratings of the 18 Defence projects that have remained on the GMPP since the 2012 *Annual Report on Government's Major Projects*. This shows, as expected, that the Delivery Confidence Assessment of individual projects varies over time, and there is a general trend of improvement in ratings as projects move through their lifecycle towards completion.

As of September 2015, only one of the 34 Defence projects was rated Red (Operational Information Services), five were rated Amber/Red (Army Reserve Development Programme; Successor SSBN; Contracting, Purchasing and Finance; Army Basing Programme; Astute Boats 1-7) with the majority (15 projects – 44%) rated Amber. See [Appendix Two](#) for a description of each project.

Defence projects IPA rating September 2015



	2013	2014	2015	2016
Maritime Sustainment Programme	●	●	●	●
Core Production Capacity	●	●	●	●
Merlin Programme	●	●	●	●
Crowsnest Programme	●	●	●	●
PUMA	●	●	●	●
Airseeker	●	●	●	●
Lightning II Programme	●	●	●	●
A400	●	●	●	●
New Employment Model	●	●	●	●
Successor SSBN	●	●	●	●
Wildcat Programme	●	●	●	●
Spearfish Upgrade Programme	●	●	●	●
WATCHKEEPER	●	●	●	●
MARSHALL	●	●	●	●
Complex Weapons	●	●	●	●
Astute Boats 1-7	●	●	●	●
Logistics Commodities Services Transformation	●	●	●	●
Queen Elizabeth Programme	●	●	●	●

Description of delivery confidence assessment (DCA) ratings

- 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.
- Successful delivery appears probable; however, constant attention will be needed to ensure risks do not materialise into major issues threatening delivery.
- Successful delivery appears feasible but significant issues already exist, requiring management attention. These appear resolvable at this stage and, if addressed promptly, should not present a cost/schedule overrun.
- 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 address these problems and/or assess whether resolution is feasible.
- 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 overall viability reassessed.
- Exempt

Source: [IPA Annual Report on Major Projects 2015-16](#), [Ministry of Defence Government Major Projects Portfolio data](#), September 2015

Future defence developments	Project and programme management	Delivering major Defence projects	Infrastructure and Projects Authority	Commercial and Contracting	Workforce capability	Key challenges
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Commercial and Contracting

NAO Commercial Overview

In Spring 2016 the NAO published an [overview](#) of the six themes we see government facing in its management of commercial relationships. These are: government's commercial capability, managing contracted-out service delivery, accountability and transparency, government as one customer, managing markets for public services, and using new commercial models. The main message for departments, other than a general need to improve the management of commercial relationships, is the need to improve commercial capability and to work together across departments to act as one customer.

Commercial capability

Commercial capability remained government's number one priority for the civil service in 2015-16. The Cabinet Office and HM Treasury led a programme of Commercial Capability Reviews across major departments, which were completed in spring 2015 with monthly updates since. The Cabinet Office summarised the common themes across the reviews in its [progress report](#) to the Committee of Public Accounts in December 2015.

The Cabinet Office's progress report also set out how departments would be producing commercial 'blueprints' in 2016. These will set out the commercial capabilities and structures departments need, and plans for delivering that capability. They are expected to be endorsed by department boards. The Ministry of Defence will be required to produce a blueprint in time for the Cabinet Office to report back in January 2017.

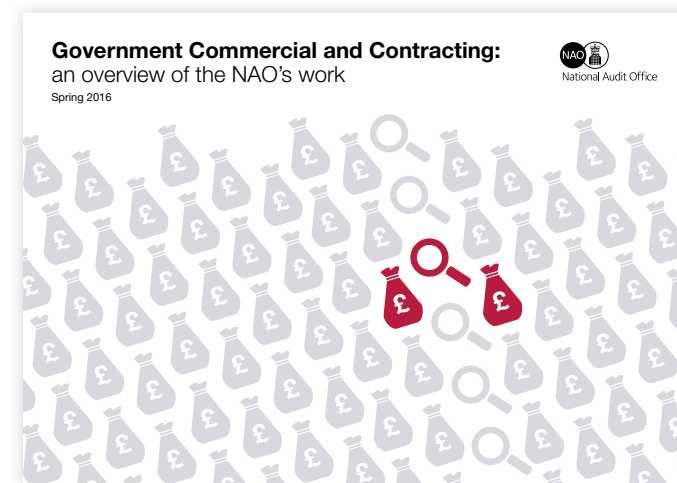
Government's response to the [Committee of Public Accounts' report](#) announced the establishment of the Government Commercial Organisation, which will be a single employer for senior commercial staff across government. Staff are transferring in 2016.

Common themes from departmental Commercial Capability Reviews

- The need to increase the number of senior experienced commercial staff and reduce the need for less-skilled junior staff.
- The need to reduce the high vacancy levels in key commercial functions, through increasing the appeal of the commercial profession in government.
- Ensuring clear lines of accountability for commercial decision-making in all departments, to board and Permanent Secretary level.

- Improving the commercial skills and awareness of non-specialist policy officials, particularly in contract management settings.
- Refocusing of commercial capability away from the procurement process and redirecting commercial resource towards crucial market-shaping and contract management activities.
- Improved coordination of commercial resources across government to direct commercial expertise towards high-risk and high-demand programmes.

Source: Cabinet Office, written evidence to Committee of Public Accounts, December 2015



Future defence developments	Project and programme management	Delivering major Defence projects	Infrastructure and Projects Authority	Commercial and Contracting	Workforce capability	Key challenges
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Commercial and Contracting *continued*

The Defence Commercial Capability Review conducted in 2014 highlighted the need to improve the commercial awareness of non-commercial colleagues (in particular military staff in key acquisition roles). The commercial function across the Department also suffers from a shortage of appropriately skilled professional people, which the Department sees as the most significant risk to delivery. In its Annual Report and in the Cabinet Office's progress review, the Department reports activity undertaken this year to improve its commercial capability:

- Introduction of a Commercial Professionalism Programme.
- New induction, contract management, price and cost analysis and negotiation courses for commercial staff, and commercial awareness courses for non-commercial specialists.
- External recruitment campaigns to bring in staff from other government departments and the private sector, as well as working with the Cabinet Office and wider government to deliver senior civil service (or equivalent) recruitment campaigns. Six senior commercial staff have been recruited through these campaigns.
- New *Contract Management Handbook* issued in April 2016, aligned to new courses and supported by the development and implementation of a Commercial/Contract Management internal control and assurance framework.
- Investment in improving its contract management information. A contract for a new Contracting, Purchasing and Finance system was awarded to IBM/Deloitte in 2015 which aims to, over time, improve visibility for contract owners at all levels.

Future defence developments	Project and programme management	Delivering major Defence projects	Infrastructure and Projects Authority	Commercial and Contracting	Workforce capability	Key challenges
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Workforce capability

To ensure standards of public service are maintained, major projects are delivered and cost reductions are sustainable, all departments must progress faster to develop strategic workforce plans that are integral to the way departments function, reflect our diverse society, and ensure they recruit or develop the critical skills they need.

Strategic workforce planning – minimising the ‘capability gap’

Like any organisation, government needs to have the right people in the right place at the right time and at the right cost to carry out all that it needs to do. Strategic workforce planning is an ongoing process through which an organisation aligns its workforce – its capability – with its priorities to enable it to meet its legislative, regulatory or service requirements as well as its organisational objectives. Planning in this way helps departments identify whether they have a ‘capability gap’, such as a lack of staff with specialist skills. The NAO’s work to date has found that in general departments are weak at strategic workforce planning and departments often lack comprehensive and reliable information on workforce skills. Since 2013 the Chief of Defence People has overseen all the defence workforce including regulars, reserves, civil servants and contractors. A number of major People Change programmes are under way.

Changes in the workforce and its cost

Between 2010 and 2015, most departments reduced their staff numbers, and the number of civil servants (full-time equivalent) reduced by 18%, from 492,010 to 405,570. The Department currently has 196,670 military and civilian personnel, and aims to reduce this to 185,200 by 2020. As part of this, it aims to reduce civilian headcount by 30% to 41,000.

Diversity, equality and inclusion

A diverse workforce that is made up of individuals with a wide range of characteristics and experiences and creating an inclusive and supportive work environment are vital to improving capability. The Department needs a working environment in which staff are motivated, feel

able to contribute and are confident that their talents will be used, regardless of their background or working style. The Department recognises that progress has been slow and that the defence workforce is not representative of society. The table below shows 2016 data (and the military recruitment targets); the proportions have been fairly stable over the past five years.

The Department has seen increase in satisfaction in its People Survey results. In 2015 its Engagement index score was 58% (civil service benchmark 58%). High scores were achieved for ‘organisational objectives and purpose’ (78%), ‘my team’ (77%), ‘my work’ (74%) and ‘inclusion and fair treatment’ (74%), but far lower for ‘leadership’ and ‘managing change’ (30%) and ‘pay and benefits’ (31%).

Percentage of personnel in the UK regular forces and FR20 Volunteer Reserves as at 1 April 2016	Royal Navy/ Royal Marines & Maritime Reserve (%)	British Army & Army Reserve (%)	RAF and RAF Reserves (%)	Target joining by 2020 (%)
Women	9.3	9.0	14.0	15.0
Black, Asian and Minority Ethnic	3.5	10.2	2.2	10.0
Percentage of civilian personnel as at 1 April 2016				
Women (%)	40.6			
Black, Asian and Minority Ethnic (%)	4.2			

Future defence developments	Project and programme management	Delivering major Defence projects	Infrastructure and Projects Authority	Commercial and Contracting	Workforce capability	Key challenges
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Workforce capability *continued*

The capability gap

The Department recognises that it has a shortage of commercial skills. In our strategic financial management report, we found that “although the Commands are building up their capabilities to take on their enhanced role, there remain significant gaps in their skills and expertise in this respect. They continue to develop their understanding of equipment costs, their project, programme and financial management skills, and the service level agreements against which they intend to track the performance of DE&S.”

The Department reports on its ‘Operational Pinch Points’, which are defined as a specialisation or area of expertise where the shortfall in trained strength (officers or other ranks) is such that it has a measurable, detrimental impact on current, planned or contingent operations:

OPP		
Navy	18	A decrease of two since April 2015. The key pinch points relate to engineering roles plus some specialist roles such as warfare specialists.
Army	4	An increase of two since April 2015. The key pinch points relate to logistics roles.
RAF	16	A decrease of three since April 2015. The key pinch points relate to engineering and intelligence roles.

Source: Ministry of Defence statistics

Use of consultants and temporary staff

Consultants and temporary staff can be an important source of capability for departments that are transforming how they do business. However, they can be more expensive than permanent staff. Departments need to use strategic workforce planning to drive down their dependency on consultants and temporary staff.

Of the 17 main departments, the Ministry of Defence was the seventh highest in terms of the amount spent on consultants and temporary staff as a proportion of its permanent staff payroll costs (which were £2,287 million in 2014-15 for civilian staff). It spent the equivalent of 5% of these payroll costs on temporary staff and 4% on consultants. The (former) Department of Energy & Climate Change, the (former) Department for Business, Innovation & Skills, HM Treasury and Cabinet Office were the main departments which spent more on consultants.

Future defence developments	Project and programme management	Delivering major Defence projects	Infrastructure and Projects Authority	Commercial and Contracting	Workforce capability	Key challenges
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Key challenges for the Department



The Department considers that threats to international security have grown in recent years. The 2015 National Security Risk Assessment concluded that risks and threats faced by the UK have increased in scale, diversity and complexity since 2010. These include threats from terrorism, the resurgence of state-based threats, the impact of technology and the erosion of the rules-based international order.



The Department is responsible for around a quarter of projects in the Government's Major Projects Portfolio, many of which are long-term, complex programmes. The Department's portfolio is dominated by a few high-cost projects/programmes, notably the Nuclear Enterprise, but also including Carrier Strike and the Warship programme. These are exceptionally complex, and general deliverability and affordability issues remain throughout.



The Department has reduced its military staff by 19% and its civilian staff by 32% since 2010. Both civilian and military workforce have key shortages of suitably qualified and experienced personnel. The SDSR set out a commitment to reduce the civilian workforce by 30% by 2020. This will be challenging given that civilian staff include specialists in areas such as finance, commercial and programme management, all important areas for the Department to be able to deliver its objectives. The Department is also committed to reshaping its military workforce through its Joint Force 2025 strategy.



The 2015 Budget settlement saw Defence expenditure grow for the first time in 15 years, but the commitment to increase overall and equipment spending in real terms still does not meet needs. Budgetary pressures are likely to be acute in 2016/17, and longer-term affordability rests on achieving unprecedented efficiencies. The Department has committed to delivering £9.2 billion savings by 2020, and the SDSR commitments are dependent upon achieving this.



Much of the Department – civilian and military – is undergoing transformation. DE&S reform remains work in progress, and the Armed Forces Commands are still coming to terms with delegated responsibilities. DIO is to announce plans to reduce the military estate, with implications for government housing and forces accommodation targets, but which also has implications for service morale.

Our work in progress

In the coming months we will publish a number of reports on key aspects of the Department's work. These include our annual examination of the affordability of the Equipment Plan, a major review into how the Department is managing its infrastructure, and a study on one of its largest and most significant equipment programmes.

Equipment Plan 2016–2026

Due to publish autumn 2016

The NAO audits the Department's annual Equipment Plan, which is a 10-year rolling forecast of its equipment procurement and support costs. It makes up around 45% of the total Defence budget. This is the first Equipment Plan since the publication of the 2015 SDSR, and will be the first comprehensive assessment of the stability of the Equipment Plan's costs since the new spending commitments were made.

Cross-government studies

The Department is likely to feature in a number of the NAO's proposed cross-government reports. These are likely to include reports on:

- Crown Commercial Service;
- scientific research across government; and
- civil service capability.

Delivering the Defence estate

Due to publish autumn 2016

Since 2010 the Department has recognised that rationalising its estate and cutting its costs are vital to balancing the Defence budget. The big reductions in the size of the Armed Forces, and government initiatives to release land for housebuilding are additional spurs. The Department has committed to releasing land for 55,000 homes.

We last reported on the estate in 2010 and this report will enable us to update Parliament on how the Department has followed up on our recommendations. We will examine whether the Ministry of Defence has a coherent strategy for rationalising its estate, and whether it has tackled past issues which have prevented it from aligning the estate with its needs.

Delivering Carrier Strike

Due to publish spring 2017

The 'Carrier Strike' capability comprises three elements which need to work together: the Queen Elizabeth Class Carriers, the F35 Lightning II Aircraft and the Crowsnest radar system. Our study will examine whether the Department has effective arrangements in place for delivering Carrier Strike, the Department's confidence in the programmes baselines and forecasts and how it is managing the risks to achieving initial operating capability in 2020.

The Government Major Projects Portfolio: Defence projects

Priorities	Description
A400M	A versatile airlifter able to perform two types of duty: tactical missions and long range strategic/logistic missions.
Airseeker	To sustain the UK's airborne electronic surveillance capability previously provided by the Nimrod R1 aircraft.
Armoured Cavalry 2025	To deliver an integrated multi-role capability that will include the delivery of AJAX and its training solution into service.
Armoured Infantry 2026	To deliver an integrated Armoured Infantry capability that will include the Warrior Capability Sustainment Programme and its training solution into service.
Army Basing Programme	To enable delivery of the Army 2020 force structure, including support to Service Personnel and their families and the provision of required accommodation and infrastructure in the UK, achieving the policy commitment to withdraw the Army from Germany by 2020.
Army Reserve Development Programme	The utilisation of Reservist Units by the Army as part of efficiencies in the Armed Forces laid out in the white paper 'Reserves in the Future Force; Valuable and Valued'.
Astute Boats 1-7	The design, development and manufacture of up to seven Astute-class submarines.
Carrier Enabled Power Projection	The focus is the delivery of a Carrier Strike capability by the end of 2020, which is assessed to be the most technically challenging requirement. The other elements of fighting power (amphibious capability and the support shipping) will be managed as key dependencies.
CHINOOK (including Project Julius)	To enable Chinook aircraft to be generated, operated and sustained to at least 2040 within allocated resources. The programme includes projects JULIUS and NEW BUY, which aim to upgrade the cockpit and deliver additional aircraft respectively.
Complex Weapons	To realise an improved, affordable and dynamically adaptable military complex weapons capability which protects sovereignty and assures Operational Advantage.
Contracting, Purchasing and Finance	Contracting, Purchasing and Finance will provide a single online end-to-end procurement system for all MoD procurement activity. All other processes especially paper-based systems will be either replaced or subsumed.
Core Production Capability	The phased regeneration of the current nuclear core production facilities on the Rolls-Royce site at Raynesway in Derby, the sustainment of the Core Production Capability and the production, development and manufacture of the nuclear reactor cores to meet Pressurised Water Reactor 2 and Successor technical specifications.
Crowsnest Programme	Equips 10 Merlin Mk2 helicopters with an advanced airborne surveillance system to meet the requirement for early threat warning and co-ordination of aircraft.
Cryptographic Enabling Services	To support the Department's information assurance capability.
EMPORIUM	To provide a suite of cost-effective enterprise-wide application hosting capabilities, covering all security domains, to support current and future applications needs.
Future Beyond Line of Sight	To maintain the current satellite communications network and develop a successor capability.
GRAPEVINE 1	To deliver a cost-effective and modern 'New Style of IT' across the Defence estate.
GRAPEVINE 2	To provide Defence's Global Connectivity and Integrated User Service requirements, for example Wide Area Networks, Telephony and Video Conferencing.

The Government Major Projects Portfolio: Defence projects *continued*

Priorities	Description
Lightning II Programme	To deliver a multi-role, carrier-capable aircraft, to be operated jointly by the Royal Air Force and Royal Navy.
Logistics Commodities Services Transformation	The Logistics, Commodities and Services (LCS) Operating Centre in the MoD provides commodity procurement, storage and distribution services for the Armed Forces. This programme is designed to undertake a major reform of the LCS, developing a service of the right size for current military requirements and reducing cost through upgrades to both the inadequate current facilities, and the modernisation of the processes in operation.
Maritime Sustainment Programme	The Military Afloat Reach and Sustainability (MARS) Tankers will replace the current single-hulled tankers operated by the Royal Fleet Auxiliary.
MARSHALL	To provide a Terminal Air Traffic Management capability for Defence that will ensure that core air traffic functions continue to be provided, obsolete equipment is replaced, and new regulatory conditions are met.
Merlin Programme	Updates 30 Merlin Mk1 aircraft to overcome existing and forecast obsolescence to ensure sustainment of the required capability until the planned out-of-service date.
New Employment Model	To design and deliver a New Employment Model for Regular and Reserve Service Personnel that supports Operational Capability while being sufficiently attractive to recruit and retain personnel of the right quality and enables agility through improved organisational efficiency, flexibility and adaptability.
Nuclear Warhead Capability Sustainment Programme	To deliver and sustain the capability (skills, technology, science, personnel, production and support) to underwrite the UK nuclear warhead stockpile now and in the future, including transition to Mk4A and future possible warhead provision.
Operational Information Services	To provide a flexible and robust solution that will deliver operational information services to Land, Air, Maritime and Joint users in the deployed environment.
PUMA	To enable Puma to be generated, operated and sustained out to 2025.
Queen Elizabeth Programme	To deliver two Queen Elizabeth-Class aircraft carriers.
Spearfish Upgrade Programme	To update the UK's submarine heavyweight torpedo. Safety improvements are required to ensure residual risks remain as low as reasonably practicable and improved performance is required against increasingly capable threats.
Successor SSBN	The design, development and manufacture of four Successor SSBN-Class submarines.
The Materiel Strategy	To design, orchestrate and implement transformational change within DE&S, in order that it can operate more effectively and efficiently within a simplified and improved Acquisition System.
Type 26 Global Combat Ship Programme	To deliver an interoperable, survivable, available and adaptable capability that is operable globally within the maritime battle space to contribute to sea control for the Joint Force and contribute to maritime force protection with the flexibility to operate across and within the range and scale of operations.
WATCHKEEPER	WATCHKEEPER is an unmanned aerial vehicle (UAV) that will provide battlefield surveillance and reconnaissance capabilities to the land tactical commander within the Joint Operations environment.
Wildcat Programme	Wildcat has been developed to meet the twin requirements for a dedicated small helicopter for deployment in the Maritime (Surface Combatant Maritime Rotorcraft), and the Littoral and Land environments (Battlefield Reconnaissance Helicopter).

The Department's sponsored bodies

Executive agency

[Defence Electronics and Components Agency](#)¹

[Defence Science and Technology Laboratory](#)¹

[UK Hydrographic Office](#)¹

Executive non-departmental public body

[National Army Museum](#)¹

[National Museum of the Royal Navy](#)¹

[Royal Air Force Museum](#)¹

[Single Source Regulations Office](#)¹

Advisory non-departmental public body

[Advisory Committee on Conscientious Objectors](#)

[Armed Forces' Pay Review Body](#)

[Defence Nuclear Safety Committee](#)

[Independent Medical Expert Group](#)

[National Employer Advisory Board](#)

[Nuclear Research Advisory Council](#)

[Scientific Advisory Committee on the Medical](#)

[Implications of Less-Lethal Weapons](#)

[Veterans Advisory and Pensions Committees](#)

Public corporation

[The Oil and Pipelines Agency](#)¹

Ad-hoc advisory group

[Central Advisory Committee on Compensation](#)

Other

[Advisory Group on Military Medicine](#)

[Defence Academy of the United Kingdom](#)

[Defence Sixth Form College](#)

[Defence and Security Media Advisory Committee](#)

[Fleet Air Arm Museum](#)

[Reserve Forces' and Cadets' Associations](#)

[Royal Marines Museum](#)

[Royal Navy Submarine Museum](#)

[Service Complaints Ombudsman](#)

[Service Prosecuting Authority](#)

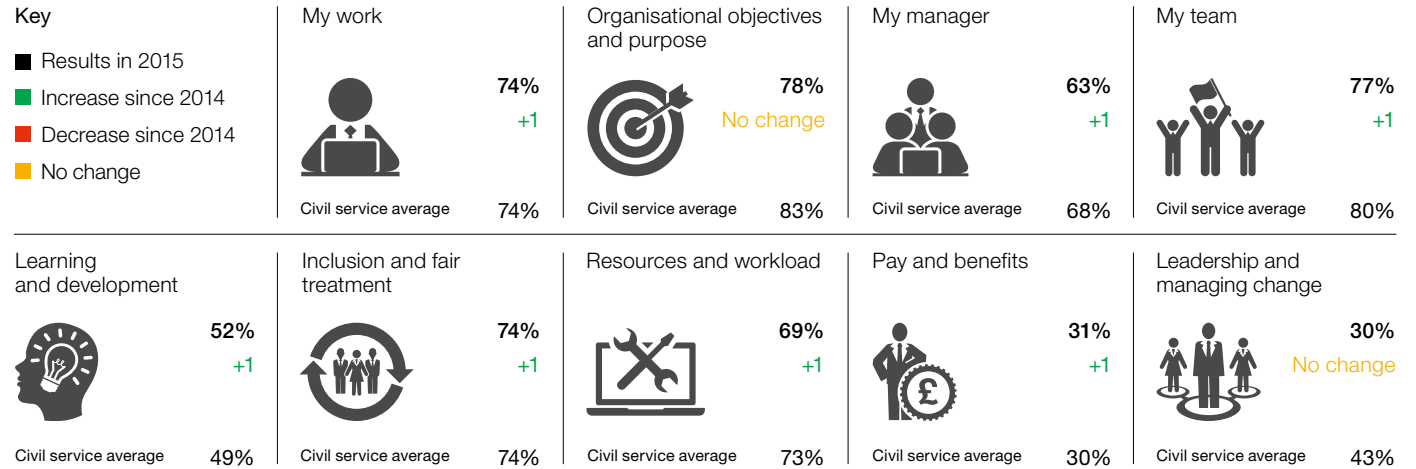
[United Kingdom Reserve Forces Association](#)

¹ Bodies audited by the National Audit Office.

The Civil Service People Survey – Staff attitudes and engagement

The [Civil Service People Survey](#) looks at civil servants' attitudes to and experience of working in government departments. The data shows the percentage of staff surveyed who agreed or strongly agreed with a set of positive statements on their department's performance.

Attitudes of staff in 2015 compared with 2014 – Ministry of Defence



Engagement index 2015 and 2014



Sources: Civil Service People Survey 2015 and 2014

The Armed Forces Attitude Survey

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, morale and pride, 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 2016.

Overall satisfaction and morale

Just under half (46%) of Service personnel are satisfied with Service life in general. This is unchanged since 2015 but remains below the level of satisfaction seen in previous years.

Overall, morale has remained stable since 2012; 40% of personnel currently report high morale. Morale in the Royal Navy has increased since 2015, but this is offset by a decrease in the RAF.

Around 76% of personnel report that they are proud to be in their Service, which is unchanged from 2015. The overall number of personnel who would recommend joining their Service is also unchanged at 45% in 2016; however, in the RAF there have been declines in both pride and in those who would recommend others to join over the past year.

Retention

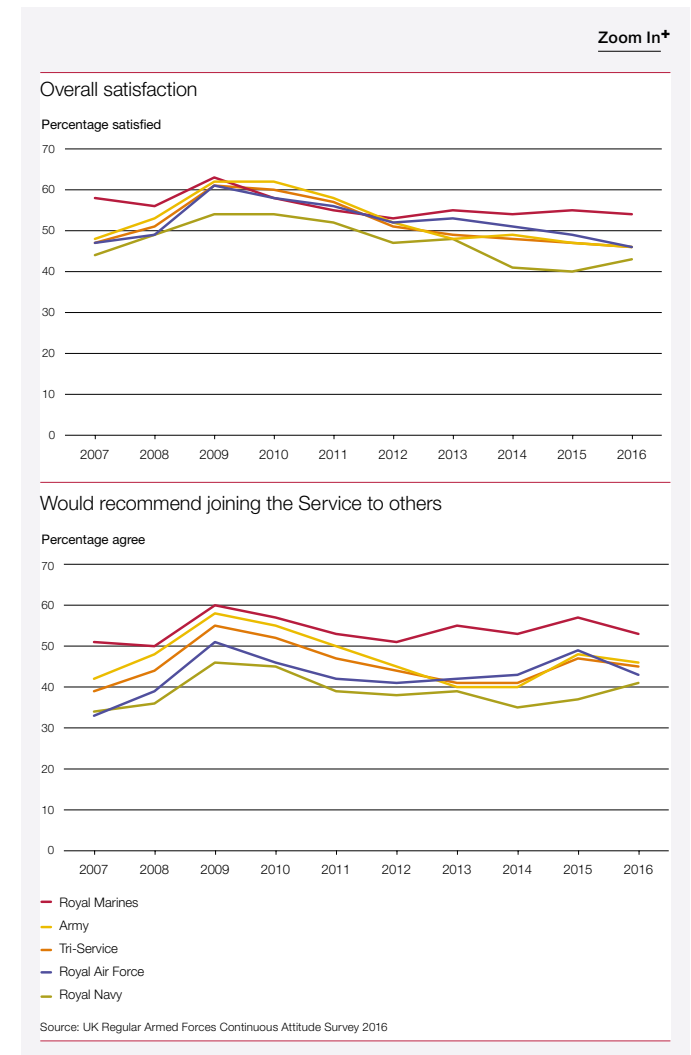
In 2016 job security continued to be the top retention factor, followed by dental and healthcare provision, pension and mental health provision. Around 48% of personnel now cite mental health provision as a retention factor, an increase of 10 percentage points since 2015.

Among those who have put in their notice, the impact of Service life on family and personal life remains the top reason for leaving the Armed Forces. In 2016, more personnel cite current job satisfaction as a reason for leaving than in previous years, making it the second most common reason.

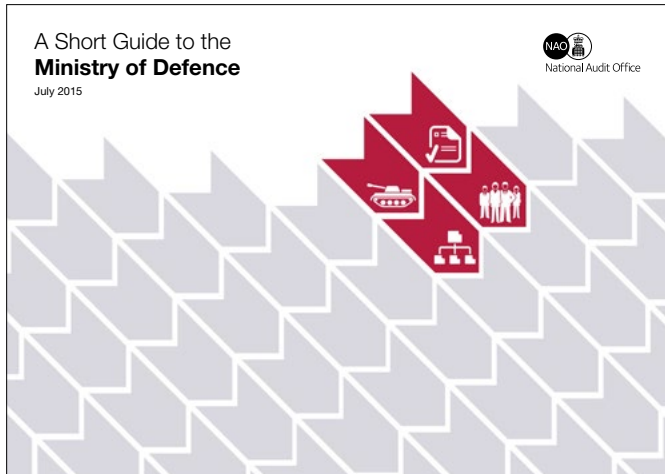
Satisfaction with Service accommodation

2016 has seen a decrease in satisfaction with the overall standard of Service accommodation, with just over half (53%) reporting that they are satisfied. Satisfaction has fallen noticeably among those living in Service Families Accommodation, with a decrease of seven percentage points to 50% in 2016.

In 2016 personnel are also less satisfied with the value for money, response to requests for repairs or maintenance to their accommodation, and the quality of repairs carried out. One-third (33%) of personnel report satisfaction with the quality of repairs, with 45% dissatisfied.



Relevant National Audit Office publications



[A Short Guide to the Ministry of Defence](#)
National Audit Office, July 2015

NAO reports relevant to the Department

[Strategic Financial Management in the Ministry of Defence](#) (July 2015)

[Major Projects Report 2015 and the Equipment Plan 2015–2025](#) (October 2015)

[Impact of the Strategic Defence and Security Review on the Equipment Plan](#) (June 2016)

[Service Family Accommodation](#) (June 2016)

Cross-government reports

[Use of Consultants and Temporary Staff](#) (January 2016)

[Investigation into the acceptance of gifts and hospitality](#) (February 2016)

[Government's spending with small and medium-sized enterprises](#) (March 2016)

[Disposal of public land for new homes: a progress report](#) (July 2016)