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HOUSE OF COMMONS  
LONDON SW1A 0AA

Speech

## Defence Reform: A New Relationship with Industry

*On 27<sup>th</sup> February 2015, Sir Michael spoke about the need for reform and efficiencies in defence as the then-Defence Secretary.*

“I’m delighted to be here in the north east.

A part of a world where I began my career as an MP; as well as an area with a fantastic heritage of engineering and manufacturing.

Over the past 5 years, we’ve been determined to help the north east grow.

We’ve invested over £300 million in the Regional Growth fund, millions more in the Tees Valley Growth Deal, and the Sunderland City Deal.

Creating tens of thousands of jobs and expanding the region’s advanced manufacturing base.

We’ve invested in road and rail as well as broadband to boost economic growth.

And we've seen those efforts pay off.

Today employment is up by more than 45,000 and there are 10,000 fewer households where no one has a job. That's thousands of people with the security of a pay packet.

More than 30,480 young people started apprenticeships last year, and there are 27,000 new businesses.

But what impresses me most is the way industry has adapted to meet the demands of the 21st century.

Nowhere is this better illustrated than in the defence sector.

Where once tanks were hammered into shape on the banks of the Tyne, the factories of the Tees churned out gun boats and torpedo boats sped into the waters of the Wear.

Today, we find a high tech industry specialising in everything from carbon and stainless steel fabrications to composite tubes for military applications.

No wonder that when our armed forces seek sophisticated solutions they often turn to the innovation and imagination of companies here in the north east, from the Primes to niche SMEs.

Whether it's Darchem engineering who've supplied the intake, exhaust systems and folding fire barrier doors for the HMS Queen Elizabeth and HMS Prince of Wales aircraft carriers.

Or CAV Aerospace in Consett, specialists in ice protection systems technologies, who were a key supplier in our C-17 programme.

Or Petards in Gateshead currently fitting out our Merlin Mk 2 helicopters are fitted with the latest Electronic countermeasure equipment by SMEs like.

Or Third Eye Technologies here in Durham, who installed their immersive reality Blue Room technology to enhance RAF Leeming's Forward Air Control applications, impressing NATO and a host of leading overseas companies in the process.

And this brings me to my next point. Expertise from the north east is increasingly winning world wide recognition.

Electronic control panels engineering by north Shields company Parmley Technologies were used in both UK and US armoured vehicles and became essential to clearing mines in Afghanistan.

While companies like Durham based Kromek Ltd which, a few years back, won the Global Security Challenge for its security systems to screen liquids at airports and is now marketing gamma-ray detectors to identify nuclear isotopes, which has won it big contracts in the US and in Japan.

### Need to transform

The transformation we see here is also one we want to see replicated across the defence industry.

Because with Russian aggression, with the horror of ISIL spreading, with pressures on public spending, adaptability, agility and flexibility must become our watchwords.

### Progress

MOD is fitter than it's been for years.

The £38 billion black hole we inherited is long gone.

Our procurement arm Defence Equipment & Support has been reformed.

And we've reduced costs by almost £400 million in our major projects.

UK defence is the biggest defence spender in Europe, £14 billion a year and I've signed off investment in new strike fighters, more surveillance aircraft, hunter killer submarines, two aircraft carriers and the most advanced armoured vehicles around.

But the job's not done.

We've only completed stage one of our reforms.

We've turned MOD into an intelligent customer.

The next challenge is about helping the defence industry to become leaner, concentrating on innovation and exportability, encouraging primes to opening up supply chains, so that our SMEs can bring their innovation to the table.

### Importance of partnership

We're not expecting something for nothing.

We've published a 10 year £163 billion equipment plan so industry has greater certainty about what's coming down the track and greater confidence the money is there to pay for it.

We're investing in innovation, protecting our annual investment in S&T, and using our Centre for Defence Enterprise to develop novel innovations.

We've established the Defence Growth Partnership, harnessing the talents of industry, academia and government to provide leading edge capability for our armed forces around the world.

We've got the Defence Solutions Centre, making the most of its understanding of the UK's value chain, to help respond to future international opportunities.

Everyone in the government, from the Prime Minister down, is going out of their way to bang the drum for British exports.

### The problems of single source procurement

But one area where we need to do more is procurement where for national security or other reasons we can only use one supplier.

I back competition and free enterprise. Everyone in this room knows that competitive pressure delivers the best outcome.

Our default approach is robust competition between suppliers. But the truth is when you're dealing with hugely complex or very sensitive pieces of kit sometimes only one manufacturer can provide what you're looking for. We spend more than £6 billion a year on this single source procurement.

It is vital that we get a fair deal for the taxpayer when we have no choice but to procure from a single company to give our armed forces the kit they need.

In the past some defence suppliers exploited a lack of competitive pressure and transparency. Companies even tried to claim back overhead costs that included croquet, horse racing trips, motoring fines, even 2 close up magicians.

Since 2010 we have cracked down on claims like these that were the result of an unacceptable culture.

### Fixing the problem

This is a long standing issue that we need to put right.

Our answer is to change the relationship between government and industry.

First, by making it more transparent. It will now be up to suppliers to justify, rather than for us to disqualify, every pound of their contracts.

There will be guarantees in place to protect suppliers' market sensitive information. But companies cannot complain about having 100% transparency.

Taxpayers have a right to know what their money is being spent on.

Second, to ensure that contract prices are fair and reasonable to both parties. As for costs, they must be appropriate, attributable and reasonable before being allowable.

Third, it brings in proper enforcement. Our new costs watchdog will be scrutinising a company's financials and if they find costs coming in are in stark contrast to the estimates going out, they will clamp down hard on companies to reduce their prices. SSRO will be able to issue penalties of up to £1 million, and name and shame report if companies don't play fair.

### Firm but Fair

But it's not a case of all stick, no carrot.

The partnership principle is as important here as elsewhere.

Our costs watchdog will be scrupulously fair to both MOD and the contractor.

Our suppliers who support this approach can expect us to offer the capital investment and the export support to enhance their reputations.

We want a strong defence industry to help deliver the equipment our armed forces need.

This is not about attacking profits. We support firms getting a reasonable profit for delivery, performance and efficiency.

This is about striking a new relationship so that industry considers itself not so much suppliers, but deliverers for defence.

And we're doing so because the prize for achieving our goals is more than just a better equipped armed forces.

More than just more jobs and more businesses.

It is about making sure we keep the skills and talent the enterprise and entrepreneurship, that has always powered this great part of the world, coming through.

## Conclusion

5 years ago our economy was on the brink, with a deficit second in size only to Greece in the EU.

Now we are the fastest growing major economy in the world, you and other businesses have created 1000 new jobs everyday in this parliament, we have the joint lowest corporation tax level in the G7.

There is a fundamental difference of view on the economy and the importance of enterprise, some want to intervene, control companies and prices, and penalise success by making sure firms don't become 'too big'.

I am unashamedly pro-enterprise. That means promoting competition, opening up markets, and championing new firms. It's something I've done whether in the business department scrapping red tape, or in energy backing new suppliers. It's what I want to do in defence by opening up more spending to SMEs.

What the north east needs, what your businesses need, is to stick to the plan that has delivered the jobs and the taxes on which our public services, and our defence, depend.

As a country we should never take the success of business for granted.

So I want to end by saluting your enterprise, for taking risks to create jobs for other people.

My commitment is to keep backing you so the north east can keep on growing.

Only then can we be certain of securing a better future for the country.

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