

Malkara Consulting

**Australia's Submarine Program:
A Failure in Anti-Corruption Due Diligence?**

5 March 2018

About Malkara Consulting

Malkara Consulting is a consultancy firm that specialises in the provision of training and advice in relation to money laundering, terrorist financing, bribery and corruption, sanctions, fraud, financial investigations and risk management¹. The training and advice is designed to increase the effectiveness of current AML systems and to target harden organisations from the threat of organised crime and terrorism by explaining and demonstrating how money laundering and other financial crimes work.

Advice and training provided by Malkara Consulting is based on extensive experience across a range of industries including the Australian Federal Police, National Australia and the mining and logistics sector. Malkara's financial crime expertise was obtained from service with the Australian Federal Police involving investigations into money laundering, drug trafficking, people smuggling, human trafficking, organised crime and significant fraud upon the Australian Government.

Training experience with the AFP involved the design and delivery of investigation training programs (financial investigations, money laundering, bribery and corruption) in Australia to Australian law enforcement and intelligence agencies and to state police forces and overseas to representatives of law enforcement agencies, prosecutors, customs officers, judges and financial intelligence units from Indonesia, Malaysia, New Zealand, Sri Lanka, China, Pakistan, Singapore, Fiji and the United Arab Emirates.

Malkara Consulting conducts business primarily in Australia, South East Asia and West Africa.

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¹ Malkara is an Australian Aboriginal word meaning "shield".

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Executive Summary

Australia is embarking on a naval building program, the largest undertaken since the Second World War. A significant aspect of that building program is the replacement of the current Collins class submarines, known as the Future Submarine Program (or Project SEA1000). The estimated cost of building 12 new diesel electric submarines is \$50 billion, not including the combat system.

On 20 February 2015, the Australian Government announced that a competitive evaluation process (CEP) would be undertaken involving design concepts submitted by 3 submarine manufacturers namely; Direction de Constructions Navales Services (DCNS) of France; ThyssenKrupp Marine Systems GmbH (TKMS) of Germany and Mitsubishi of Japan. On 26 April 2016, the Australian Government announced that DCNS had been selected as the preferred partner to build the submarines.

DCNS is now known as the Naval Group. It was previously DCN. Since 1997, DCNS has been involved in 5 major corruption scandals. Three of these events were known before the company was selected to design Australia's submarines and two have come to notice since it was selected. Four of the incidents involve the supply of submarines or frigates to Taiwan, Pakistan, Malaysia and Brazil and the loss of information pertaining to the submarines the company is building in India. DCNS has denied any wrongdoing, but there are too many incidents have occurred to be ignored, and further information should be sought by the Australian Government about them and appropriate anti-corruption measures applied.

After DCNS was selected, the Australian National Audit Office conducted an audit into the selection process, which included the probity process that was overseen and delivered by the Australian Government Solicitor. There were no issues discovered by the ANAO and the selection process was found to be fair and free of conflicts of interest. However, the ANAO audit report makes no reference to any anti-corruption due diligence being undertaken by the Department of Defence on any of the submarine manufacturers before the CEP or on DCNS following its successful selection as the preferred partner.


Conducting anti-corruption due diligence on a major equipment supplier, particularly a company located outside of Australia, is sound risk management and business practice. It is important that the Department of Defence, DCNS and every company in the submarine building supply chain, has an effective anti-bribery and corruption system that equals international standards. The international standard is ISO 37001 Anti-Bribery Management Systems.

If the Department of Defence has not undertaken anti-corruption due diligence processes on DCNS, then it should do so immediately. And the department should demand information from DCNS on how it responded to previous allegations of corruption and the changes the company made to prevent further occurrences.

Australia is facing increasing scrutiny from foreign intelligence services and Australia's submarines are an attractive intelligence target. The Australian Senate should conduct an inquiry to establish if any anti-corruption due diligence processes were applied during the CEP; and what if any due diligence will be undertaken by the department and any anti-corruption framework it will put in place for each of the service and component suppliers involved with the project. Senate oversight of the submarine project should continue until the last submarine has been launched.

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Failure to target harden Australian defence industry from bribery and corruption, increases the risk of information being stolen by foreign intelligence agencies and organised crime. Either outcome could have a disastrous result for the safety of Australia's submarines and crew during a conflict and seriously damage Australia's national security.



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5 March 2018

Australian Submarine Program: A Failure in Anti-Corruption Due Diligence?

Introduction

1. A professionally managed business planning a major project involving the purchase of high valued assets or services from a vendor, would undertake appropriate anti-corruption due diligence on the supplier. The level of vetting of the supplier would be determined by the results of a risk assessment and the value of the potential purchase. Due diligence could involve a simple internet search to discover any adverse information about the supplier and a credit check. Or a search of commercial databases for links to criminal activity, terrorism; or to a sanctioned entity. Where the value of the contract is large, organisations engage independent firms to undertake a thorough investigation into the supplier, including its owners, managers, customers, associates, and their supply chain².
2. Governments, do not usually operate in a commercial environment and are not always aware of or have experience in anti-corruption due diligence processes. A case in question, is the current Australian submarine program to replace the aging Collins Class submarines.
3. This paper will discuss what anti-bribery and corruption due diligence processes, if any, were undertaken on any of the submarine manufacturers who tendered designs before and after the successful partner was announced. The paper will not re-canvas other risk issues relating to the submarine selection process, unless relevant. Those issues have been addressed by other authors. For example, in 2017 Insight Economics Pty Ltd undertook an analysis of strategic risk, economic risk, technical risk and industrial risk. Nor will the paper discuss the capability of any submarine. That is beyond the technical skills of Malkara Consulting. This paper briefly examines the anti-bribery and corruption risk relating to the program. And concludes that from an ABC risk perspective, DCNS should never have been a candidate for the submarine program or selected as a partner with Australia to build the submarines.

Background

4. Australia is embarking on a naval building program, the largest undertaken since the Second World War. A significant aspect of that building program is the replacement of the current Collins class submarines, known as the Future Submarine Program (or Project SEA1000). The estimated cost of building 12 new diesel electric submarines is \$50 billion, not including the combat system.
5. Commentary and debate about building the submarines has focused on capability, cost and where the vessels will be built. But surprisingly no discussion has been held on the corruption risks associated with the program. Big money attracts greedy people and firms. And new defence programs, particularly the acquisition of major assets with new and advanced regional

² The latter is a requirement under the laws of some countries to ensure an organisation does not have any aspect of human slavery in its supply chain.

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capabilities that the new submarines are expected to possess, also attract foreign intelligence interest.

Foreign Intelligence & The Corruption Threat

6. There is a symbiotic relationship between successful intelligence gathering operations and corruption. Foreign intelligence agencies employ corruption techniques to penetrate governments, primary builders, contractors, sub-contractors and suppliers. A common corruption technique is grooming, a method being practiced to great effect by a major foreign power around the world, as recent events involving an Australian senator have confirmed.
7. Corruption is an act of extremely poor governance. And there are some red flags of poor governance in the Australian defence industry. Recent lapses in security by firms operating in the defence industry have shed the spotlight on some aspects of their governance and operations. For example, the loss of commercial non-military data by a defence contractor to hacking and the loss of security plans to parliament house. In intelligence operations, all the pieces matter, and even the loss of unclassified information, adds to the pool of potentially valuable information that could be exploited by a future enemy. And while the incidents have caused a refocus on the security of defence information, there has been no public discussion on whether other areas of governance, for example anti-bribery and corruption risk management plans, are in place and are effective.
8. Anti-bribery and corruption plans are usually part of an overall risk management plan. Implemented correctly, an ABC programme raises the standard of risk awareness in an organisation and target hardens it against all major risks, not just against corruption. And if a foreign intelligence agency or criminal group was to employ corruption techniques to obtain sensitive information, then their attempts are least likely to succeed when an organisation has an effective ABC program.
9. Even if Australian firms engaged in the naval building program have an effective ABC plan, corruption risks to the ship building program would exist offshore. Particularly where a ship manufacturer has been involved in corruption incidents as an alleged perpetrator. A foreign intelligence agency seeking to obtain classified information about Australia's new submarines would probe any foreign company associated with the program for weak links. A foreign intelligence agency would understand, that if a company is prepared to pay bribes, then unless there has been a change in culture, then there is a high probability it will employ staff who are prepared to accept bribes in return for releasing information. The intelligence agency would search for any weakness in the foreign company. And that is a major risk to the security of Australia's naval forces.
10. It is not possible to prevent all acts of bribery. To attempt to do so, would place a huge financial and administrative burden on any organisation. And any plan to mitigate corruption should be proportional to the risks and reasonable. But that doesn't mean Australia should be a soft target either. When it comes to

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Australia's naval building program, the risk of bribery and corruption occurring in the tendering process and building phase is large, as there could be over 4,000 subcontractors involved.

Australian Future Submarines: A Major Intelligence Target

11. Australia has claimed that the new submarines to be built by DCNS will be the largest and most advanced diesel electric submarines in the world. Automatically that claim, will attract the interest of submarine builders around the world and from foreign intelligence agencies. In the naval ship building industry, having and maintaining a competitive advantage is vital to survival. Very few governments will want to buy equipment from a naval builder that is not supplying vessels at the cutting edge of naval technology. And the building of submarines has become a competitive industry in recent years with new manufacturers entering the international market. Consequently, all other submarine builders would be interested to learn as much as they can about the capability and technical details of the submarine to be built by DCNS for Australia.
12. Intelligence agencies from countries with an interest in Australia's defence would have now designed an intelligence collection plan in relation to the submarines and would have commenced gathering information. Those countries would include friends and potential adversaries. A starting point would be examining weaknesses in the manufacturer and in the supply chain that can be exploited using a multitude of methods including bribery and corruption techniques. Submarines are more complex than surface ships and have more parts and software to develop and test. With long and complex supply chains, often with suppliers operating in countries that have a high rating for corruption, the potential for penetration of any one of the suppliers by an intelligence agency using corruption techniques is significant.

Competitive Evaluation Process – Selection of DCNS

13. On 20 February 2015, the Australian Government announced that a competitive evaluation process (CEP) would be undertaken to select the replacement for the Collins submarines. CEP involved evaluating the design concepts submitted by 3 experienced diesel electric submarine manufacturers namely; Direction de Constructions Navales Services (DCNS) of France; ThyssenKrupp Marine Systems GmbH (TKMS) of Germany and Mitsubishi of Japan.
14. CEP was never intended to evaluate a completed operating submarine or establish a firm price for each submarine or the total project cost. The objective of CEP was to select a partner, not a submarine. Even though a model name has been attributed to the submarine, it only exists on paper and even then, not in complete form. DCNS was selected on the basis of the design concept it marketed and promoted to Defence.
15. The CEP evaluation team was scheduled to submit its recommendation to an expert advisory panel by early June 2016. However, the timing was brought

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forward as the Australian Government wanted the successful bidder announced before any expected federal election. On 26 April 2016, only 14 months after the evaluation process commenced, the Australian Government announced that DCNS had been chosen as the successful international partner to build Australia's submarines.

Assessment by National Security Committee of Cabinet

16. In April 2016, the National Security Committee of Cabinet and the Prime Minister met to consider the proposal from the Defence Department recommending DCNS as the preferred partner to build Australia's submarines. The NSC had only 4 working days to consider the proposal between the time it was received by the committee and the time of the announcement of the successful bidder.
17. It is apparent that the NSC had inadequate time to consider all the risks associated with the submarine project. In particular, the potential corruption risks. And due to the secrecy surrounding defence decisions, it is not known, if the Department of Defence raised any bribery and corruption concerns about DCNS in its submission to the NSC. And if they did, it is not known what weight was made by the committee of them and what if anything was discussed or decided upon on how to mitigate the risk of corruption. And if corruption risk was not contained in the recommendation by Defence to select DCNS, it is not known if any concerns about corruption were raised, or any concerns about DCNS were raised, by any member of the NSC and the response to those concerns if they were raised.

ANAO Audit

18. After the selection of DCNS, the Australian National Audit Office, undertook an audit of the competitive evaluation program. Risk was one of the criteria used in evaluating each competitor, which was defined to mean: *"Ability to work with Australia to identify and understand key program risks, their impact, and sustainability of proposed mitigation strategies"*. The ANAO report was tabled before both houses of the Australian Parliament on 27 April 2017. Just twelve months and a day, after the announcement of the successful partner.
19. The ANAO, reporting on the probity aspect of the CEP, found that the Australian Department of Defence had effectively designed and implemented a competitive evaluation process to select an international partner for the Future Submarine program. Meaning the process was free from any conflict of interest, information was handled appropriately, and each competitor was evaluated fairly.
20. Advice and assistance in relation to probity was provided by the Australian Government Solicitor.
21. The ANAO report on the audit it conducted, makes no reference to auditing any anti-corruption due diligence program relating to the submarine project.

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Anti-Corruption Due Diligence Program

22. While the selection process was subject to a probity assessment, the issue, in relation to CEP, is the extent, if any, of anti-corruption due diligence (ACDD) being undertaken on each or any of the submarine manufacturers by the Australian Government prior to the selection of the successful partner. The ANAO report makes no mention of it being done by the Department of Defence or by any other agency. Given the need to complete the evaluation process quickly, it is understandable that defence might not have had time to conduct due diligence on every contender itself. And the Department of Defence might not have had the resources either. During the audit, the Department of Defence explained to the ANAO that an assessment of a submarine is a highly complex task and skills in Australia to do it were in short supply. It therefore wanted to choose a sole partner and proceed to assessing the design, as it did not have the resources to evaluate three designs. It is assumed therefore that perhaps the department did not have the resources to undertake a thorough due diligence of the submarine builders.
23. The objective of the CEP was to select a partner not a submarine design. Therefore, it would be reasonable to expect that significant due diligence, including from an anti-bribery and corruption perspective would have been undertaken on each of the submarines manufacturers. But that does not appear to have happened. Despite the objective, the focus appears to have been on selecting a partner who could build a submarine that closely met Australia's requirements.
24. Given that CEP was focused on selecting a partner, then prudent business and national security grounds would have necessitated that the Department of Defence undertake an anti-corruption due diligence program on each of the manufacturers before being allowed to participate in the CEP. And if that was not done, then it should have been done on DCNS before it was selected as the preferred partner.
25. If the Department of Defence did not have the capacity to undertake any anti-corruption due diligence program, then they should have outsourced that function to a firm that specialises in that process. And, if it couldn't undertake due diligence on all three contenders; then it should have at least undertaken it on DCNS prior to the announcement that it had been selected as the preferred partner.
26. It appears from examining the ANAO report, that the CEP did not include any due diligence being undertaken on any of the submarine builders. As risk was identified as being the: *Ability to work with Australia to identify and understand key program risks, their impact, and sustainability of proposed mitigation strategies*". How can Australia work with any submarine builder to identify risks, when Australia does not know all or any of the risks involved with the builder itself? If due diligence was undertaken on DCNS, why was it chosen given its links to past allegations of corruption? And if due diligence was not undertaken, why wasn't it? Has the omission not to undertake due diligence, increase the

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risk to the project, with Australia selecting a building partner who perhaps has a high corruption risk?

DCNS Corporate History

27. On 28 June 2017, DCNS changed its name to Naval Group. It is what is known in France as a private law company. The French Government owns 62.49% of its capital, 35% is held by Thales, 1.64% by current and former members of staff and 0.87% by the company.
28. The company has a long history in naval affairs. Prior to 1991, the organisation was known as *Direction des Constructions et Armes Navales* (DCAN), which became DCN (*Direction des Constructions Navales*) in 1991. DCNS, which itself was formed when *Direction des Constructions Navales Services* (DCN) acquired Armaris, from Thales in 2007.
29. Despite the name changes, Naval Group still operates the same business from the same locations as DCN and DCNS.

Allegations of Corruption

30. While various levels of anti-corruption due diligence could have been applied to the CEP; a detailed search might not have been necessary. A simple internet search would have identified serious corruption red flags in relation to DCNS.

Prior to the Selection Announcement

31. Prior to the announcement in April 2016, the Defence Department would have discovered that:
 - a. In 1997, an investigation was launched into the sale of three submarines by *Direction des Constructions Navales* (DCN, later known as DCNS, now Naval Group) to Pakistan. A car bomb explosion in Karachi, Pakistan, on 8 May 2002, killing 14 people, including 11 French employees of DCN exposed the corruption scandal. The Pakistani chief of Naval Staff admitted the payment of bribes by DCN to secure the deal.
 - b. In 2002, DCNS was embroiled in a corruption scandal involving the supply of six Lafayette-class frigates to Taiwan in 1991. Former French Foreign Minister Roland Dumas later admitted that the French government had, through the partially state-owned oil company Elf Aquitaine, paid US\$500 million in bribes to secure the frigate deal. And a Taiwanese naval officer who collected evidence on the ships deficiencies was later murdered.
 - c. In 2010, French authorities launched an investigation into the 2002 sale by DCNS of three submarines, including two Scorpene class, to Malaysia. Allegations of corruption relating to the sale arose following the murder of 28-year old Mongolian interpreter in 2006 by two officers of the Malaysian Special Branch. Four people are being prosecuted in France

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for their part in using bribery over the sale of the submarines. Two of those charged are former chairmen of DCNI.

Post Selection Process

32. And since the selection of DCNS to build the submarines for the Australian Navy, the following issues have come to notice:
 - a. In August 2016, the Australian newspaper reported the leakage of a complete set of plans and information on the combat and stealth capability of India's six Scorpene submarines which are being built by DCNS. The plans were allegedly unlawfully removed by an ex-French naval officer working on contract for DCNS.
 - b. In May 2017, French authorities announced that they are conducting an inquiry into alleged corruption relating to the sale in 2008 of four Scorpene attack submarines and related technology to Brazil.

Transparency International Corruption Ratings

33. Corruption Ratings published by Transparency International are commonly used by businesses undertaking corruption risk assessments when there is a potential new business partner or target business in an acquisition or merger. In 2008 Brazil ranked 80th out of 180 countries on Transparency International Corruption Perceptions Index (CPI). While in 2002, Malaysia ranked 33 out of 102 countries. A low corruption index rating identifies to any organisation considering doing business with a country, that it needs to be more careful and apply additional anti-corruption due diligence measures to reduce the risk of being caught in corruption. It would be unwise and irresponsible not to undertake any, including a simple open source search.
34. In 2016, the year Australia chose DCNS to be the preferred supplier of the submarines, France ranked 23rd from 176 countries on the CPI. The low ranking, particularly for an OECD member, even without the allegations of prior corrupt behaviour, would warrant a prudent investor to undertake a thorough due diligence program on a supplier operating in France. A ranking of only 23rd, for an advanced industrialised country is a major red flag and any organisation considering do business in France or with a French organisation would apply a thorough due diligence process before engaging in any business in that country or with that organisation.

Commonwealth Procurement Rules

35. The Commonwealth Procurement rules that Commonwealth department and agencies are required to follow that when making purchases of goods and services, they make no mention of any requirement to undertake an anti-corruption risk assessment of any supplier.

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36. A publication “Defence and the Private Sector. An Ethical Relationship” published by the Department of Defence, makes no reference to anti-bribery and corruption standards or policies.

Australia’s Anti-Bribery & Corruption Framework

37. Unlike the United Kingdom and USA, the Australian Government, via the Commonwealth Attorney-General’s Department provides very little information on what organisations in the public and private sector can do to reduce their risk of being involved in corruption either in Australia and offshore. There is also no guidance provided on what anti-corruption due diligence procedures they should follow when vetting a supplier of goods and services.

Allegations Cannot Be Ignored

38. DCNS has denied any wrong doing in all reported instances of corruption. It is not implied that the Naval Group and DCNS had any involvement in the murder of the Taiwanese naval officer, the Mongolian interpreter in Malaysia or the bombing in Pakistan, referred to earlier. However, either DCNS has been one of the unluckiest defence suppliers in recent history, or the incidents are a strong indication of the company’s corporate culture, past and present; the quality and effectiveness of its anti-bribery and corruption compliance program, or the level of due diligence it undertakes on the people it transacts business with, especially in high risk corrupt jurisdictions.
39. The allegations of corruption made against DCNS cannot be ignored by the Australian Government. The Government should demand full details from DCNS about each matter, including ascertaining, what investigations were undertaken, the results of those investigations and what has changed with the company following the allegations to prevent re-occurrence. However, as allegations of corruption keep resurfacing, there appears to be prima-facie evidence that little or nothing has changed to prevent bribery and corruption.
40. Corruption is a serious breach of trust. Once it occurs, it brings into question, all aspects of a relationship. Not just integrity. Trust, quality, capability, transparency, and reliability are also questioned. The Australian Government therefore should satisfy itself that:
- a. It can trust DCNS to manufacture a submarine to the standard and capability that was promoted?
 - b. DCNS has anti-bribery and corruption and risk management plans that are at international standard.
 - c. The supply chain involved in the design, planning and construction of the submarines has effective anti-bribery and corruption plans and are secure.

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Conflicting Standards

41. In Australia, people with serious criminal convictions are banned from working in many industries including defence. And even where people do not have a criminal conviction, they can and are prevented from acquiring a high-level security clearance, if they have engaged in activities that threaten or could threaten the security of Australia and its interest. And where, a person is required to have a very high security clearance level and possible access to highly classified material, the due diligence undertaken on them is intense. For some positions, applicants are subject to a 360-degree assessment involving past and present colleagues and friends; drug testing; and psychological tests.
42. The standards set by Australia to protect its national interests are very high. And they should be and must be. As Australia is facing increasing interest from foreign intelligence agencies, both onshore and overseas. Information is the new wealth. It has a value. And if foreign intelligence agencies cannot steal sensitive information then organised crime will attempt to, either on its own initiative or on instructions from foreign intelligence agencies. Australia's very high personal security vetting standards prevent people with a disposition to commit crime or to undertake subversion, gaining access to highly classified information.
43. Given the rigorous vetting processes people are put through to obtain a job and/or security clearance, why shouldn't the same standards or higher be applied to a company seeking work from the Department of Defence? And why is a company, that has a history of being caught in allegations of corruption, whether they are proven or not, allowed to participate in Australia's largest defence acquisition? It needs to demonstrate what has changed within the organisation to earn our trust.

ISO 37001 Anti-Bribery Management Systems

44. The international standard for the prevention of bribery is ISO 37001, Anti-Bribery Management Systems. ISO 37001 was released by the International Organization for Standardization on 15 October 2016. Australia was a party to the working group involved in drafting the new standard.
45. ISO 37001 specifies mandatory requirements for an organization to implement when it is establishing or updating its anti-bribery & corruption risk management systems. Measures that need to be implemented will depend on the corruption risk an organization might reasonably anticipate.
46. Implementation of ISO 37001 by all companies involved in Australian defence acquisitions, will:
 - a. Target harden them against corruption and indirectly against foreign intelligence and organized crime activity
 - b. Promote trust and confidence in defence supply chains

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- c. Assist an organization to obtain finance to expand either in Australia or offshore
 - d. Reduce compliance costs when dealing with customers particularly those located in the UK and US where there exist more stringent anti-bribery and corruption laws and policies.
47. The Australian Government recently announced a new Defence Export Strategy to assist and encourage Australian companies to seek opportunities in the international defence market. Adoption of ISO 37001, will make it easier for Australian defence exporters to secure joint venture partners; adjust to local anti-bribery and corruption standards; and reduce the risk of being caught in an offshore corruption scandal.
48. Australian companies engaged in the defence industry should insist, that all companies, including foreign owned parent companies and subsidiaries they control, tendering for local defence work or who have won a defence contract and all organisations working under sub-contract, demonstrate that they have in place an anti-bribery management system in accordance with the standard.

Questions for The Department of Defence

49. From an anti-bribery and corruption perspective, the Australian Department of Defence has many questions to answer in relation to the choice of DCNS as the preferred partner to build Australia's submarines. These include:
- a. Prior to the announcement of DCNS as the preferred partner in constructing the submarines, what due diligence did the Department of Defence conduct on the company?
 - b. Did the Defence Department send a team to India or to Malaysia to examine the performance of DCNS in building the submarines in India or supplying the submarines to Malaysia? Prudence would have dictated that Australia would establish all aspects of the company's performance from its past and current customers, not just in relation to any ethical issues, but also construction standards and associated building problems if any.
 - c. If anti-corruption due diligence was not undertaken on any of the submarine manufacturers before the CEP was announced, then why wasn't it?
 - d. If the Department of Defence was aware of the corruption allegations involving DCNS, why was it selected to be part of the CEP and eventually chosen as the preferred partner?
 - e. During the evaluation process, did the department ask for and examine the anti-bribery and corruption compliance program from the contenders and from DCNS, including interviewing the CEOs and senior executives about the effectiveness of their compliance programs generally?

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- f. Has the department ascertained if any of the people involved in the corruption allegations, are also involved or will be involved in any way with the design and manufacturing of Australia's submarines?
 - g. Is the Defence Department going to examine Naval Group's anti-bribery and corruption program given the past and current allegations and incidents?
 - h. Is the Department of Defence monitoring the prosecution in France of the people connected with the sale of the submarines to Malaysia? And what action is the department going to take if any of them are found guilty of corruption or any other serious offence?
 - i. Upon completion of the CEP and the announcement of DCNS as the successful partner, did Australia sign an agreement with DCNS allowing Australia to undertake an anti-bribery compliance assessment of Naval Group, including specifying what information Australia can obtain to assess the corruption risk relating to the submarine project. And does the agreement include a penalty clause, including termination of any agreement should the Naval Group fail to comply?
50. In relation to sub-paragraph 46 (e) above, of interest, would be the operation of any whistle blower program and how past issues of fraud and corruption involving employees, managers and contractors had been dealt with, and how the program extends to third parties, including customers and sub-contractors. A poor handling of whistle blower matters and reports of corruption and fraud; is a good indicator of how serious a company takes in preventing corruption both as a victim and as a perpetrator.

Australian Government Response to DCNS Data Leak

51. When the story of the lost Indian submarine data and alleged bribery involving the Brazilian submarine deal came to public notice, what action did the Department of Defence take? Regarding the theft of DCNS data, Christopher Pyne, the Defence Industry Minister, is reported to have advised Dennis Richardson, the then Defence Department Secretary, to convey a "reminder" to DCNS that Australia expects the handling of classified information to be as tight as Australia's³. That response fell short of anti-bribery and corruption and risk management standards. It did not recognise the seriousness of the issues involved. Government Ministers and Departmental heads, set the tone at the top which influences those below and those organisations doing business with it. The response by the minister gave an indication that he saw the matter as merely a minor error and not a serious act of corruption and a threat to national security.

³ The recent loss of classified material from the Prime Minister and Cabinet, which was found in a secured cabinet awaiting disposal, hardly inspires any confidence in Australian protective security measures.

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52. The theft of data by a DCNS contractor is corrupt behaviour. And five major bribery and corruption incidents linked to one company are too many to ignore. Arguing that the stolen data has no relationship to the Australian submarines, as the submarines will be entirely different to the Scorpene submarines and therefore not a potential threat to national security, is not the main issue. Any smart customer would have demanded answers and access to the anti-bribery and corruption compliance program and overall risk management programs in operation by DCNS, to ascertain if they were effective. And clearly, there are red flags that they are not.
53. If the anti-bribery and corruption compliance programs are deficient; either in DCNS or any company that provides it with components and services, then there is a high risk that data could be stolen again by corrupt employees or contractors along any part of the supply chain. But on the next occasion, should it occur, the information could end up being supplied to a foreign intelligence service. As advised earlier, managers or staff of a company that are prepared to pay bribes, would be prepared to accept bribes in exchange for supplying classified information.

Relationship to Other Defence Programs

54. Anti-bribery and corruption compliance programs have application beyond the submarine project. ABC compliance programs, including anti-corruption due diligence processes have relevance to all defence acquisition programs, particularly high value projects such as the future frigate program and the armoured vehicle replacement programs for the Army.

Conclusions

55. Australia will invest significantly in building what is claimed will be the world's best conventional submarine. But the capabilities will be eroded and amount to little, putting our Australia's security at risk, if the submarine plans fall into the hands of a future enemy.
56. Undertaking due diligence on a supplier is not only an important anti-bribery and corruption requirement, it is a sound approach to doing business. International standard anti-corruption due diligence appears not to have been undertaken on any submarine manufacturer before, during or after the CEP. Failure to undertake due diligence on the successful partner, has probably increased the security risk to Australia's submarine project.
57. Australia has selected a company to build its next generation of submarines, with a history of alleged involvement in bribery and corruption scandals. A company that is also based in a country with a poor CPI rating. Five corruption scandals involving the same company, is a clear indication that its corporate governance in relation to the prevention of bribery and corruption occurring is poor and as a result, poses a high risk to the integrity of Australia's submarine program.

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58. From an anti-corruption risk management perspective, DCNS should not have been allowed to partake in the CEP and it should not have been selected by the Australian Government as the preferred partner to build Australia's submarines; until it had demonstrated that it had a robust anti-corruption program in place which was enforced and the outcome of any investigations into past allegations of corruption had been disclosed.

Recommendations

60. In relation to the Australian submarine project and to current and future defence acquisition programs, the following is recommended:
- a. In the interests of national security, Australia should not allow a defence company to tender for a project that has a history of poor corporate performance, involving unlawful behaviour, without establishing what changes have been made to prevent a re-occurrence.
 - b. The Australian Government should stipulate that all companies supplying equipment or services to the Department of Defence have in place anti-bribery and corruption plans that meet international standards and best practice. The Australian Government should terminate any relationship with a company that cannot meet international anti-bribery standards.
 - c. The Australian Government should mandate that anti-bribery and corruption standards be applied and enforced in all components of a component or services supply chain. This should extend down to the lowest component.
 - d. All successful tenderers and contractors for defence work, including the submarine project be made responsible and liable for all security breaches and any sub-contractors utilised by them.
 - e. A senate inquiry should be undertaken into the Competitive Evaluation Process from the perspective of anti-bribery and corruption with an emphasis on:
 - i. Establish whether anti-corruption due diligence processes were applied during the process and if applied, how thorough were they conducted.
 - ii. If no anti-corruption due diligence was undertaken on any of the submarine manufacturers either before, during or after the CEP, then ascertain why they were not pursued.
 - iii. Whether DCNS should have been allowed to participate in the CEP.
 - iv. Assess the anti-bribery and corruption risk to the submarine project and defence acquisition projects generally.

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- v. Should the anti-bribery and corruption risk be too high, then whether DCNS (now Naval Group) should be allowed to continue as a partner with Australia in building the submarines. Noting that it is not uncommon for companies seeking to acquire, merge or do business with another company to pull out of a deal, when the bribery and corruption risk is unacceptable. The Australian Government should be prepared to do the same.
- vi. What action if any the Department of Defence has done to target harden the submarine project (and other defence acquisition projects and service agreements) from bribery and corruption via the implementation of international standard anti-bribery management plans.
- vii. What action has the Department of Defence taken to establish how DCNS handled previous corruption allegations, the results of any investigation undertaken, and changes made to its anti-bribery and corruption policies.
- viii. Whether people who have been involved in any of the previous corruption allegations are involved or will be involved in the design and manufacture of Australia's submarines.
- f. Given the value and complexity of the submarine project, senate oversight should occur throughout the life of the program until the last vessel is delivered to the Royal Australian Navy.
- g. Future audits by the ANAO should incorporate an examination of the effectiveness of the anti-bribery and corruption risk management plans in operation pertaining to the submarine project.
- h. Australian Department of Defence mandate that all contractors and suppliers have in place and enforce, anti-bribery & corruption policy and procedures.
- i. Government procurement guidelines be amended to include reference to anti-bribery and corruption controls.
- j. DCNS should be subject to enhanced anti-bribery and corruption due diligence monitoring throughout the life of the submarine project.

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Appendix 1

Chronology: Due Diligence Submarine Program	
1997	Investigation launched into sale of 3 submarines to Pakistan by DCN (changed to DCNS)
2002	DCNS named in a corruption scandal involving the sale of Lafayette Class frigates to Taiwan in 1991
2010	French authorities launch an investigation into the sale of submarines by DCNS to Malaysia in 2002
20 February 2015	Australian Government announces competitive evaluation process for the submarine project
26 April 2016	DCNS chosen as the preferred partner to build the submarines
August 2016	Complete plans to India's Scorpene submarines acquired from DCNS leaked
15 October 2016	Introduction of ISO 37001 Anti-Bribery Management Systems
27 April 2017	ANAO Report tables in both houses of the Australian Parliament
May 2017	French authorities announce investigation into sale of Scorpene submarines by DCNS to Brazil