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Chair: The Honourable John McKay





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• (0850)

[*English*]

**The Chair (Hon. John McKay (Scarborough—Guildwood, Lib.)):** We are commencing a study. We welcome the Parliamentary Budget Officer, Yves Giroux, and his colleague, Christopher Penney, to launch our study. It is pursuant to a motion taken by this committee on April 21 that we will begin studying the impacts of Canada's procurement process on the Canadian Armed Forces. I'm looking forward to the PBO's analysis.

We appreciate your appearance here today. With that, you have five minutes, sir.

[*Translation*]

**Mr. Yves Giroux (Parliamentary Budget Officer, Office of the Parliamentary Budget Officer):** Thank you, Mr. Chair.

Good morning, members of the committee. Thank you for having invited us to testify before you today.

We are looking forward to telling you about our analysis in connection with your review of the impact of Canada's procurement process on Canadian Armed Forces preparedness. With me today is Christopher Penney, our eminent defence advisor-analyst.

[*English*]

In accordance with the PBO's legislative mandate to provide impartial, independent analysis to help parliamentarians fulfill their constitutional role, which consists of holding the government accountable, my office has published the following recent reports related to your study: "The Life Cycle Cost of the Canadian Surface Combatants: A Fiscal Analysis", "Canada's Military Expenditure and the NATO 2% Spending Target", "The Industrial and Technological Benefits Policy: An Analysis of Contractor Obligations and Fulfillment", and "Planned Capital Spending Under Strong, Secure, Engaged—Canada's Defence Policy".

In the coming weeks, we are also planning to release an independent cost estimate of the F-35 fleet as well as an analysis of the defence force structure model.

Christopher and I would now be pleased to respond to any questions you may have regarding our defence analysis or other PBO work.

Thank you.

**The Chair:** Thank you.

Witnesses should always be this economical with their opening remarks.

Ms. Kramp-Neuman, you have six minutes, please.

**Mrs. Shelby Kramp-Neuman (Hastings—Lennox and Addington, CPC):** That's excellent.

Thank you for your brief testimony. I'm sure we'll get into some questions from all of the respective parties.

With regard to my first question, in the PBO's 2022 report entitled "Planned Capital Spending Under Secure, Secure, Engaged—Canada's Defence Policy: 2022 Update", it states that the capital spending from 2023-24 through to 2027-28 "potentially raises questions regarding the ability of the Government to manage increased procurement activity."

Could you speak of any recent progress that the government has made towards ensuring that procurement problems do not arise from the dialled-up defence spending over this period?

**Mr. Yves Giroux:** When we released that report, we indicated that the government was underspending compared to its planned capital expenditure under strong, secure and engaged, to the tune of about \$8 billion over a four-year period, which led to a shortfall of about \$2 billion per year. The government, at the point when we released our report, had revised its capital expenditures to make up for that shortfall.

With respect to whether we have more information, I'll let Christopher answer that part of the question.

**Mr. Christopher Penney (Advisor-Analyst, Office of the Parliamentary Budget Officer):** The only thing I would add is that we know that in 2022-23, there was a shortfall, as compared to planned SSE spending, of about \$1.5 billion in capital. In 2023-24, the present fiscal year, the main estimates suggest that the shortfall will be about \$4 billion.

There was over \$10 billion planned spending under SSE for 2023-24, and only \$6 billion was asked for in the main estimates.

**Mrs. Shelby Kramp-Neuman:** Thank you.

For my next question, I understand there are excessive project specifications and that they're a major factor with regard to the timeline we see for many defence procurement projects. Would you be able to explain how we could speed things up by eliminating unnecessary specifications?

**Mr. Yves Giroux:** It's a delicate issue. We're not military experts when it comes to the needs of the Canadian Forces and it's difficult for us to determine whether these specifications are excessive or not. However, we can provide general statements or general observations when it comes to defence procurement.

There's clearly no single point of accountability that may explain the delays. For example, there are at least two ministers in two departments involved in major procurement processes. Major procurements are ultimately resting upon political decisions. There are also contracting approaches that favour industry partners and tend to cede control from the federal government.

When it comes to the specification aspect, there are obviously unique specifications required due to Canadian-specific characteristics, land-mass size and climate. However, there could probably be improvements, when it comes to specifications that would benefit from being clearly delineated from the get-go, as opposed to changing the specifications once the procurement process is launched.

**Mrs. Shelby Kramp-Neuman:** Okay, perfect.

Just to take further your response to that, if the dispersion of responsibility is across several different government departments and agencies, do you agree with the diagnosis that having a single point of ministerial responsibility would contribute to a faster and more efficient procurement process?

**Mr. Yves Giroux:** It would certainly be a contributing factor and something that would favourably enhance the speed of procurement and the efficiency of the procurement process to have one single minister and one single senior official responsible.

**Mrs. Shelby Kramp-Neuman:** Okay. Thank you.

Further, with regard to reassignment of authority, it's often been said that the defence procurement is its own beast and therefore it may not be appropriate to assign a responsibility over to PSPC.

Do you agree with this characterization? If so, what department or agency would be most appropriate for managing it and why do you think that?

**Mr. Yves Giroux:** That's a question that I don't think I am in the best position to answer as to who should be responsible. I think as long as there is one organization or minister or senior official who is ultimately responsible with the right skill set and the right support structure behind them, that would be appropriate. Whether it be PSPC or National Defence or even somebody else, I don't think is material or matters that much, as long as they have the right skill sets and the appropriate structure to support them.

**Mrs. Shelby Kramp-Neuman:** Thank you. I'll go to my next question.

In the PBO's 2022 report entitled "The Industrial and Technological Benefits Policy: An Analysis of Contractor Obligations and Fulfillment", it stated that the "ITB policy affect the outcomes of competitive procurement processes" and "a supplier that proposes

lower value-for-money, or a higher price, could still be awarded a multi-million dollar contract if it promises greater economic benefits to Canada."

In your view, does the eventual ITB benefits generally exceed the extra costs?

• (0855)

**Mr. Yves Giroux:** Again, it's a value judgment that's a bit difficult to make or to decide upon because there are reasons why the ITB has been put in place. One would need to look at the counterfactual to determine in the absence of ITB what would be the price and what would be the economic benefits.

What we have found though, and what was surprising to us, is that even if there are a multipliers that reduce the dollar requirement for ITB investments for corporations in post-secondary education, for example, or research and development, very little of the value of these contracts go toward the higher multiplier effect. This suggests that the ITB may not be working fully as intended when it comes to multiplying the economic impacts in these high-value sectors such as post-secondary education and research and development.

**The Chair:** Thank you, Ms. Kramp-Neuman.

Mr. Fisher, six minutes.

**Mr. Darren Fisher (Dartmouth—Cole Harbour, Lib.):** Thank you, Mr. Chair.

Thank you, gentlemen, for being here and the important work that you do every day ironing out all of the wrinkles in the way government works or sometimes doesn't work.

You may have touched on some of this with Ms. Kramp-Neuman, but I'm thinking of the layers of policies. I'm thinking about the layers of process, especially with defence procurement. I'm looking for specific recommendations. How do we streamline? How do we get more agile?

I know we can do procurement of a baseball hat pretty well, but when it gets to really big things and we have multiple departments within government all looking at defence procurement specifically, how do we streamline? How do we get more agile and responsive to our incredible military requirements?

**Mr. Yves Giroux:** It's an interesting question because we start from a base where there's a small defence industrial base in Canada compared to other countries. Right there, we are at a disadvantage especially if we insist on having Canadian-made major equipment. The government obviously for various reasons often insists on domestic production. That severely limits the competitive base on which the government can tap. A small industrial defence base, that's one disadvantage.

There are ways, I think, of overcoming at least in part this disadvantage, notably by having one single point of contact when it comes to defence procurement and not just a point of contact but a point of accountability. Right now there are at least two departments involved, Defence and PSPC. That would be one way to simplify things, having one person and one organization ultimately accountable for military procurement.

There are obviously ways to simplify the procurement process. I think specialists in procurement could be better placed to explain in detail how to streamline the procurement process.

**Mr. Darren Fisher:** How do we balance competition while still seeking speed and also acknowledge that we have to be fiscally responsible?

**Mr. Yves Giroux:** That requires a delicate balancing act between cost and value for money versus.... It's that and also ensuring that there are significant or measurable economic benefits for the country while also ensuring, as has been the government's policy for some time now, the development of a domestic defence capability. As has been pointed out to me, it's one thing to procure major equipment from abroad, but in case of war, it doesn't guarantee us that we'd be first to be served. We'd probably be at the back of the queue.

There are intangible costs to procuring abroad in case of unforeseen needs. There is obviously value in having a domestic production capacity.

• (0900)

**Mr. Darren Fisher:** Speaking strictly about democracies, not just in procurement but specifically in defence procurement, which democracies are doing it right? What are they doing differently?

**Mr. Yves Giroux:** It's difficult to provide a definite and clear answer to that. If you look at some countries, there are anecdotes that some military departments can buy pens and screws at prohibitively expensive prices, but on the other hand they're very efficient at producing and putting frigates in the water and so on.

We have some numbers here as to costs. They may not be comparable. The Arleigh Burke destroyers in the U.S. cost about \$2.2 billion U.S. apiece, the South Korean destroyers cost about \$1 billion apiece and so on. In comparison, the Canadian surface combatants are at over \$5 billion Canadian apiece. However, it's not entirely sure that these numbers are fully comparable. The U.S. and South Korean numbers may not include all the costs that we include in our own estimates.

There are other countries that do well in some specific areas of procurement. In this case, it's warships.

**Mr. Darren Fisher:** Do all democracies in defence procurement demand or expect a level of domestic production?

**Mr. Yves Giroux:** I don't know about that.

**Mr. Christopher Penney:** In my experience, it seems that almost every country levies some type of program that is similar to the industrial and technological benefits program. We generally refer to these as defence offsets. This is more the norm rather than the exception. It is something that we see. There is a favouritism toward domestic production, yes.

**The Chair:** Thank you, Mr. Fisher.

Madam Normandin, you have six minutes, please.

[*Translation*]

**Ms. Christine Normandin (Saint-Jean, BQ):** Thank you, Mr. Chair.

I'd like to thank you as well, Mr. Giroux.

I'd like to discuss something that had been announced in 2019, but which, I gather, never came to pass. I'm referring to the creation of an entity that would have been called Defence Procurement Canada. It would have prevented duplication in various departments, including National Defence and Public Services and Procurement Canada. People seemed to be in favour of it, but I gather that the idea, even though announced in 2019, was never mentioned in the mandate letters to the ministers, to the great disappointment of some of them.

Are you aware of what this entity might have been, and can you tell us whether you were consulted at the time about its introduction?

**Mr. Yves Giroux:** To answer the second part of your question, no, we were never consulted. Like you, we did not see any progress in this area. Nor did we see this entity mentioned in any of the mandate letters.

What I can say, however, without being aware of all the details and without having been consulted, is that the establishment of a specific agency could solve a number of problems, on condition that defence procurement rested exclusively with that agency. For example, introducing a new player while continuing to assign a major role to the two departments you just mentioned would only cause further confusion and even increase the number of steps involved in the procurement process. I believe that creating another agency is not necessarily required to improve the process. We could very well reshuffle the existing cards without adding another entity.

**Ms. Christine Normandin:** So the main problem is duplication between departments. However the problem is dealt with, eliminating this duplication would be a step in the right direction.

**Mr. Yves Giroux:** That's what I believe too. There is no need for another entity, but if it were established, it would have to be the only organization responsible for procurement. And yet it would likely be difficult to have a only one entity responsible, because for obvious reasons, the armed forces will clearly want to have their say in contracts and specifications. So I don't think it would be the magic bullet that would fix all the procurement problems.

**Ms. Christine Normandin:** Thank you very much.

I've heard that other countries have policies established by public servants rather than politicians or agencies. These policies are systematically reviewed every two years to remove politics from the process and to ensure that requirements and requests are monitored on a regular basis. Is that something we should consider?

• (0905)

**Mr. Yves Giroux:** That's definitely a model we should consider. If politics were removed from the decision-making process, the approach to procurement would become a much more neutral.

We all know that politicians are elected to represent what the people want. It's important, particularly in matters pertaining to defence, to reflect people's preferences. So it could lead to delays without basically improving the procurement process. We have only to think of decisions with respect to the F-35s, and how it's going to cost us a lot more today than it would have only a few years ago.

The establishment of a new agency would therefore be a desirable approach in some instances, but it would still have to be closely monitored by politicians, who are ultimately responsible for government decisions.

**Ms. Christine Normandin:** Thank you very much.

A little earlier, Mr. Fisher said that it seemed to be much easier to buy baseball caps than major military equipment. Based on a number of articles that have appeared this week, I would tend to disagree.

The military are complaining that the equipment for personnel that they are receiving is often obsolete when it arrives. Are the feedback loops for end users fast enough to ensure that equipment is not obsolete by the time it is delivered?

**Mr. Yves Giroux:** That's a question for the department to answer, particularly by service personnel who have to cope with the shortcomings of this procurement system. I don't have a detailed enough knowledge of the procurement processes and feedback loops, and Mr. Penney has indicated to me that he is no better informed than I am.

**Ms. Christine Normandin:** We know that there are procurement delays. Do you systematically carry out studies on the additional costs resulting from these delays? The pandemic reminded us that costs can rise very quickly, particularly in construction. Are these delays and cost increases attributable to the slow procurement process being tracked?

**Mr. Yves Giroux:** We don't do these checks systematically. We have done so for major programs, combat ships for example, but not for the entire procurement process or other specific processes, apart from the reports we've published. It's probably something that relates more closely to the Auditor General's mandate.

**The Chair:** Thank you, Ms. Normandin.

[English]

Ms. Mathysen, you have six minutes.

**Ms. Lindsay Mathysen (London—Fanshawe, NDP):** Thank you, Mr. Chair.

I appreciate your being here, Mr. Giroux and Mr. Penney. Thank you.

I know your report on the new acquisition of the F-35s isn't out yet. I think we should consider, as we continue on this study, inviting the PBO back once it's out. That's just a suggestion.

You sent a letter to the Minister of National Defence on January 16, asking to do that examination of true costs. Your predecessor, Kevin Page, did the same thing on the sole-source contract that the Conservatives did on the F-35s. At the time, it was discovered that DND actually kept two books on the costs of the F-35s, and they were tricky in terms of how they estimated the lifespan. That reduced overall the costs of what was estimated on each of the aircraft that was acquired, or was supposed to be acquired.

Obviously, we don't want that to happen again. We don't want those same tricks. From what you've received thus far, can you comment at all on whether you've seen anything like that, or if we should be concerned?

**Mr. Yves Giroux:** What we have seen so far does not lead to concerns of that nature—or what we've seen several years ago. We have received very good collaboration from the Department of National Defence. There have been some hiccups: information that we had asked for earlier this year that did not exist and that now exists, but I think that was just an oversight—nothing major. We are confident that what we have in terms of information fully represents the numbers and what DND is really using.

The other advantage we have compared with several years ago is that we have gained several years of experience, as has the Department of National Defence, in costing that fighter jet. They've had lots of time to refine the cost estimate, as we say, for various reasons.

• (0910)

**Ms. Lindsay Mathysen:** One of the recommendations you put forward in the ITB report was that National Defence “should review its materiel forecasting and positioning to ensure that sufficient stocks are maintained at the right locations.” That was a big issue. The union involved in a lot of that categorizing and maintenance of stocks.... That's been privatized over the years. The union is quite upset about a lot of the privatization and outsourcing of those contracts. Did you find that this was part of some of the problems in terms of keeping those stocks?

**Mr. Yves Giroux:** We didn't look at that. You may be referring to a report by the Auditor General. We did not make recommendations—

**Ms. Lindsay Mathysen:** Yes. I'm sorry.

**Mr. Yves Giroux:** Maybe it's something that I completely forgot, but I don't think so. We didn't look at the intricacies of the process and the privatization of some processes at National Defence.

**Ms. Lindsay Mathysen:** I think that was an AG report. I apologize.

**Mr. Yves Giroux:** That's fine. Maybe Madam Hogan will be a bit insulted that you confused her with me.

**Ms. Lindsay Mathysen:** I'm sorry.

**Mr. Yves Giroux:** That's fine.

**Ms. Lindsay Mathysen:** Yes, I wouldn't want to ever do that.

Ultimately, you did find, though, that in terms of the procurement process, there's quite a huge gap in terms of specialists who have been hired within National Defence or who can do that job. There's a chronic issue that hasn't seen any resolution in terms of I think 30% of positions, or 4,200, being unfilled as of May 2022, and a lack of trained resources, of people who are able to help with those procurement issues.

What do you suggest or what are you looking at in terms of how the department needs to deal with that or ultimately what the consequences in the long term will continue to be, as we've seen thus far?

**Mr. Yves Giroux:** We have not looked at specifically the lack of procurement personnel at DND, but in the course of our multiple reports—and we've released a lot over the years—it's something that has come up regularly, that there is a lack of procurement personnel at DND.

In order to improve the procurement process, it's clear that it is an essential part that DND—or whoever is ultimately responsible for the procurement process, if there were to be changes made—has the appropriate number of persons in place with the right skill set. A lack of personnel is obviously an impediment to an efficient procurement process.

**Ms. Lindsay Mathysen:** That's right. Those ballooning costs that we keep talking about are a huge part of the fact that we just don't have enough people to be able to do the work that's being required of them.

**Mr. Yves Giroux:** That's a contributing factor.

**Ms. Lindsay Mathysen:** I want to ask about this as well: When you're analyzing these major procurement projects, how do you integrate social costs? You've talked about the cost of climate change and the impact of that. When we're analyzing these major procurement and equipment purchases, how do we keep up with that social cost of climate change, environmental policy and different lenses, such as an indigenous lens of procurement?

**Mr. Yves Giroux:** That's a question that is very.... It's something that comes up every now and then.

We're a budget office, so we tend to go with dollars and cents, with numbers and the cost of specific proposals. Even though there are social impacts and environmental impacts to many of the government's policy proposals, we don't tend to look at these systematically. In the case of defence procurement, we don't look at these other aspects, generally speaking. Similarly, we don't look at the benefits for Canada to having warships or fighter jets, because these would be difficult to quantify.

**The Chair:** Thank you, Ms. Mathysen.

We have Ms. Gallant for five minutes.

**Mrs. Cheryl Gallant (Renfrew—Nipissing—Pembroke, CPC):** Thank you, Mr. Chairman.

With respect to the NATO 2% of GDP spending, the Wales commitment, apart from the obvious—the equipment, the fuel, the training, deployment, base infrastructure—what other things are included in this calculation that would be different from what had been done previously?

• (0915)

**Mr. Yves Giroux:** That's an interesting question, because I myself looked at that when the issue resurfaced several months ago. I was a bit surprised to hear that. I should not have been surprised, but there are elements other than pure DND spending.

For example, there are veterans pensions and benefits—some benefits are included. There are some expenditures by the RCMP—not all, but a small fraction. There is spending by the Canadian Coast Guard, because in many countries the coast guard is considered a paramilitary force, so Canada is allowed, under NATO rules, to include expenditures by the Coast Guard, as well as some transfer payments to NATO and other international organizations.

**Mrs. Cheryl Gallant:** Were those changes made over the last 10 years, or had those always been there?

**Mr. Yves Giroux:** No, they have not always been there. They were made in 2014-15.

**Mrs. Cheryl Gallant:** The word is that 2% will become the minimum, as opposed to the aspirational 2%, which Canada has taken it to be. Given the modifications, it made it look like our percentage of GDP has been increased.

**Mr. Yves Giroux:** Yes. As a result of including these additional expenditures, which is consistent across NATO countries—it's not unique to Canada, so it's a NATO definition—the proportion of GDP going to defence expenditures has gone up, and is expected to go up, but mostly as a result of increased capital expenditures at DND. It will still fall short of the 2% target, or minimum, depending on the wording, depending on whom you talk to, and that results in a shortfall of between \$13 billion and \$18 billion.

**Mrs. Cheryl Gallant:** There's often the concern that the increase in defence spending goes towards salaries, as opposed to capital projects. What percentage of the budget currently goes towards the capital projects specifically?

**Mr. Christopher Penney:** It should be about 30% at this point.

**Mrs. Cheryl Gallant:** Given Canada's slow ability to increase military capabilities, are there currently any ways to require that they maintain a minimum 20% investment in capital projects?

**Mr. Yves Giroux:** It's a target also under NATO, but it's difficult to reach that level with the current constraints, especially when it comes to delivering on military projects. Over time, with the expected increase in capital spending, that goal could be attained over the next couple of years, assuming there are no further delays or issues with military procurement.

**Mrs. Cheryl Gallant:** Earlier you mentioned that a single-point responsibility, both at the ministerial and the senior management level, is required to be more efficient in our procurement.

What other countries seem to get procurement right and efficiently? Apart from the difference in leadership, what are they doing that perhaps we could be emulating?

**Mr. Yves Giroux:** I'm a budget guy, so I've done reports on Canada's military, and I've looked at numbers for other countries, but I am not a military procurement specialist per se, especially not on the international scene.

Maybe the eminent Chris has more knowledge and information than I do.

**Mr. Christopher Penney:** Certainly.

The only two I would point out were the two you pointed out earlier. That would be Japan and South Korea. They seem to be doing quite well. I believe it was recently announced in Poland that they've acquired, or entered into an agreement to acquire, new tanks and other materiel from South Korea, and they're to be delivered within six months. These are top-of-the-line, next-generation, quality platforms.

**Mrs. Cheryl Gallant:** Are there different budgetary procedures that we could follow, better planning procedures, in order to get the equipment into the hands of the military more quickly?

• (0920)

**Mr. Yves Giroux:** I'm not sure that the budget process or the funding process is itself at fault, because there's already a predictable budget track for capital expenditures under "Strong, Secure, Engaged". Even before that, there was a capital spending envelope at the Department of National Defence that was highly predictable, and the government provided flexibility at DND to re-profile it according to its needs.

In my opinion, having worked on budgets for decades now, the budget process and the funding process itself is not the main element. There's already significant or sufficient, I think, predictability in the DND capital spending, and I don't think that is the main issue.

**Mrs. Cheryl Gallant:** With respect to the length of time it takes to get from approval, for example, to the actual cutting of the steel, be it for ships, I understand there's quite a lengthy delay, and a portion of that is with Treasury Board.

Is there anything that can be done to speed that up? Are all those procedures, checks and balances necessary to get it out of the door and into hands more quickly?

**Mr. Yves Giroux:** As I said, I think having a single point of contact or a single point of accountability would be the ideal scenario where you have fewer and ideally one agency, department or organization responsible for procurement, including decisions.

It doesn't mean that we have to forget about the oversight of Treasury Board, but the Treasury Board Secretariat is not populated with military procurement specialists, so their role is essentially to ensure that due process has been followed.

If we can streamline the process and reduce the number of agencies and organizations involved in the military procurement process, it will, indeed, I think, facilitate the work of the Treasury Board Secretariat and Treasury Board ministers in ensuring that due process has been followed.

**The Chair:** Thank you, Ms. Gallant.

Ms. O'Connell, you have five minutes.

**Ms. Jennifer O'Connell (Pickering—Uxbridge, Lib.):** Thank you, Mr. Chair.

Thank you both for being here today.

I want to follow up on the 2% spending piece, because I wasn't quite sure. I want clarity.

In your testimony, you mentioned that in 2014-15, the change came in terms of including parts of the Coast Guard and veterans' salaries.

Is that what I understood? Is that when Canada started to include those things in the 2% spending?

**Mr. Christopher Penney:** That's correct.

**Ms. Jennifer O'Connell:** That was obviously a previous government changing the ability...or bringing in other departments to increase to the 2%.

There has been lots of testimony and debate around reaching the 2%, but we also saw that, previous to our government, we were not even at 1%.

Do you have the dates when they started to increase, let's say, going back to 2010?

**Mr. Christopher Penney:** I don't have it in front of me right now going back to 2010, but from 2014, we were at 1%, and that's when the change occurred in the definition.

I should note that this is a NATO definition. Obviously, it comes from them. It had been the case that you could include these other cost categories for many years before that. It's just that Canada started defining it that way in 2015.

**Ms. Jennifer O'Connell:** That's understandable. I just think that the criticisms of reaching 2% spending without clarifying that one of the ways that a previous government increased their percentage was to include new categories, and it wasn't new defence spending.... It was a recategorization of putting that spending that was already being done into the 2% spending.

In terms of those numbers, though, in terms of the increases, would that be something you could table with the committee? I would be curious of that progression going back to 2010.



**Mr. Christopher Penney:** NATO publishes those numbers. They are very easily available.

**Ms. Jennifer O'Connell:** That's perfect, thank you.

In answering another question earlier, you used the example of if there was a war, there might be difficulty at that time procuring.

Well, we're seeing a war right now, the illegal invasion in Ukraine by Russia. Have you determined any analysis that could be part of the reason for, again, criticisms of spending that has gone unspent? Is it an issue of there being only so many companies or agencies that we would work with in terms of procuring this equipment? It is probably in high demand right now in certain parts of this world.

Has that analysis been done? Is that a factor in some of the unspent money?

• (0925)

**Mr. Yves Giroux:** We haven't done an analysis of the specific factors behind the lapses at National Defence, but we have seen lapses for a number of years now and they predate the war in Ukraine.

**Ms. Jennifer O'Connell:** That's fair enough. Thank you.

In terms of U.S. procurement, I know you mentioned that you look at numbers. When I was on the finance committee, we often looked at U.S. military procurement from a finance perspective in the sense that, for example, defence in the U.S. would put out a request for tender saying—this is an example that was used so I don't know the details; this was testimony—to design a gun that can shoot around corners.

I'm serious. This is what the testimony was. That created this industry of people now developing all this technology. Obviously it's not a gun, but probably some sort of camera or microscope-type thing. By doing that, because defence spending was so massive in terms of their procurement, it incentivized companies to come up with all this different technology.

It's really difficult to compare the U.S. to the Canadian example. They may never have even used any technology that came out of it, but so much money was spent in even the development of these ideas that might be wild to us.

Are there policies, which may not be as extreme as some of that, that Canada could implement that would actually see the development of this sort of technology through our procurement process?

**The Chair:** Thank you, Ms. O'Connell.

It's an important policy question as to whether the PBO can answer a question that has to do with whether a gun will shoot around a corner. If in fact the PBO comes up with how to shoot a gun around a corner, we'll all be interested in that. That does strike me as a little bit beyond their mandate.

With that, I'm going to ask Madam Normandin to go ahead for two and a half minutes.

[Translation]

**Ms. Christine Normandin:** Thank you, Mr. Chair.

Mr. Giroux, I'd like to return to the matter of industrial and technological benefits. One of the criticisms I've heard from industry in recent years is that benefits have become politicized to some degree. Very broad criteria are put in place, and these may look positive and focus on a particular clientele, but they are not necessarily suited to requirements. Is that something your office has noted? Is the politicization of benefits that I've heard about giving rise to inefficiencies?

**Mr. Yves Giroux:** When we studied economic benefits or policies on industrial benefits, we found that benefits were often generated in areas not directly related to defence policy.

These expenditures meet the criteria for the number of dollars spent, but relatively few went to small and medium-sized enterprises. Very little is done in priority sectors like research and development, or investment in post-secondary institutions, even though the enterprises that are required to meet these criteria obtain credits of four to nine times the amounts invested. They could multiply the number of dollars spent in these sectors by four or nine times, but they do so very rarely. This suggests that the expenditures or investments that meet the industrial benefit criteria would probably have occurred in any case, or would not add anything to what would have been done without the policy.

• (0930)

**Ms. Christine Normandin:** Thank you.

I'm now going to address the geographical distribution of the benefits. I've heard that it used to be done from a regional perspective and that we actually knew where the money was going. It would appear that it's more difficult to know that now. Is that the case?

**Mr. Yves Giroux:** Our study did not focus on regional distribution. I don't know whether Mr. Penney found references to regional distribution in his studies or when the report was being written.

**Mr. Christopher Penney:** No, as Mr. Giroux mentioned, that was not included in the scope of our report.

[English]

**The Chair:** Thank you, Madam Normandin.

Ms. Mathysen, you have two and a half minutes.

**Ms. Lindsay Mathysen:** Building off what I think Mr. Fisher was asking, in terms of how you balance a speedy delivery with the idea of a more open process, a lot of small-c conservatives talk about the industry needing that competition in order to innovate, but there is that balance of speed and efficiency, and so on. How do you, as the PBO, try to assess where money could be saved from sole source? There's a lot of pressure on government to do that versus the open bid and to drive innovation within open bids, but also there are the costs.

**Mr. Yves Giroux:** It's a question that calls on many constraints. For example, you can have open competition, and you can have value for money or the lowest bid, but it's difficult to meet all of the constraints if you also add domestic production, because Canada has a small industrial defence base. If the government, or if any government, insists on domestic production, it's difficult to have sound competition that would also drive down the costs.

The only way to square that circle would be to say we are willing to go domestic, but if we don't get an accurate or a reasonable price, or if there are cost overruns, we will go abroad and we'll outsource this, or we'll go to foreign suppliers. Then that would be in breach of the domestic production capacity or policy, and that would leave Canada exposed to foreign suppliers in case of a war outbreak, which would require significant ramp-up of production.

**Ms. Lindsay Mathysen:** Within your report, it said that even though there was that policy of going into Canadian companies, the money still went to foreign owners. The majority of the money still went into international hands because of the way foreign-owned companies take on Canadian contracts or Canadian companies themselves.

**Mr. Yves Giroux:** We didn't look at where the money went. We looked at the overall costs of the Canadian surface combatants, for example. We didn't look at whether the money was spent domestically or which share was spent abroad.

**The Chair:** Thank you, Ms. Mathysen.

We will go to the very respectable-looking Mr. Kelly for five minutes, please.

**Mr. Pat Kelly (Calgary Rocky Ridge, CPC):** Thank you.

Our excessive project specifications, are they a factor in these excessive times we see and in the delays in getting projects funded and built?

**Mr. Yves Giroux:** That certainly is a factor. I'm not sure if I can call them excessive, not being a specialist myself on the needs of the Canadian Forces, so maybe they're totally justified. It's clear that we see it in procurement projects—not only defence but also IT projects—where, if you ask the ultimate users what they would like to have or what do they need to have, they'll have lots of specifications. It's not clear whether each and every one of them is necessary, but if they become part of the requirements in the contract, they drive up costs even though not every single one of them may be necessary.

**Mr. Pat Kelly:** Do you think that TBS thresholds are too low for military procurement?

**Mr. Yves Giroux:** To be honest, and I'm taking a risk by saying this, I'm not sure that the Treasury Board process adds that much value in terms of military procurement.

● (0935)

**Mr. Pat Kelly:** You're concerned that maybe there should be no threshold and that TBS should be cut—

**Mr. Yves Giroux:** I'm not sure what you mean by “threshold” at TBS.

**Mr. Pat Kelly:** I mean for the \$50 million or for the amount that would engage the TBS process.

**Mr. Yves Giroux:** Well, I think the Treasury Board Secretariat is not equipped with military specialists. If there are specialists, there are not that many, so I'm not sure they have the best skill set to be able to push back or to challenge appropriately the requirements of the Department of National Defence or of PSPC.

**Mr. Pat Kelly:** Okay. Is there sufficient competition for military contracts?

**Mr. Yves Giroux:** For the big ones, like the ones for which we did reports—surface combatants, notably—there is not a lot of competition domestically. That is one of the issues when the government wants to procure these major acquisitions and major pieces of equipment and insists on procuring them domestically.

It has to help financially with the building of the capacity, which is not the case, for example, in the U.S., where there is already a much bigger base for building these warships.

**Mr. Pat Kelly:** It's up to the government to explain having only \$6 billion out of the \$10 billion in the estimates, but do you have any way to attribute that shortfall? Is it delays in the process?

Does it appear to be a conscious decision to not fund “Strong, Secure, Engaged”, or is it a matter of delays?

What do you make of that?

**Mr. Yves Giroux:** I wouldn't attribute that to a conscious decision. What we've been told is it's a combination of delays in procuring major projects and the pandemic, which has slowed down many things. These are the main elements that we've been told.

**Mr. Pat Kelly:** Specifically, what are the central procedural issues in the system that are causing the delays? What can you pinpoint?

**Mr. Yves Giroux:** It's the fact that there are multiple players and multiple organizations—so multiple departments—and the policy decision-making process, or in other words, the political decisions that have to be made. These can be very delicate decisions that involve multiple factors.

The combination of all these elements tends to slow down military procurement, in addition to a relatively small industrial base in Canada, which reduces the number of bidders and competitors. These are all factors contributing to delays.

**Mr. Pat Kelly:** There are bureaucratic factors and there are also political factors.

**Mr. Yves Giroux:** Yes.

**Mr. Pat Kelly:** We have maybe 20 seconds left.

How do we ensure that these lapsed funds and the non-inclusion in the estimates of what's necessary to implement “Strong, Secure, Engaged”...? What's one thing you could say in those 10 seconds you have here to get it done?

**Mr. Yves Giroux:** I'd say focus the minds and reduce the number of players involved.

It's less than 10 seconds.

**The Chair:** Thank you, Mr. Kelly.

That's good advice. Focus the minds and reduce the number of players.

Madam Lambropoulos, you have five minutes, please.

**Ms. Emmanuella Lambropoulos (Saint-Laurent, Lib.):** Thank you, Mr. Chair.

I'd like to thank our witnesses for being here to answer some more questions today.

I've met with Canadian industry in my riding. I have a pretty big aerospace industry. There's CAE, Bombardier, several companies that have worked with the government and received contracts in the past. A major complaint they have is that we often go toward the outside and toward other countries instead of domestically procuring some of the equipment that we use in our Canadian Armed Forces.

They actually met with the minister recently. One of the reasons the minister gave was the fact that different countries that are all part of NATO have to have similar equipment when they're training and when they're working together.

First of all, can you confirm that this is a factor that's taken into account when looking at where to procure from and which equipment will be required for our Canadian Armed Forces?

• (0940)

**Mr. Yves Giroux:** It's clear that interoperability with our major allies is an important factor in design specifications. We obviously want our military equipment to be able to operate alongside our allies, so it may or may not be a factor in some or all of our military procurement projects.

Beyond that, I think the minister and her officials would be best placed to answer in more detail the extent to which this is a limiting factor.

**Ms. Emmanuella Lambropoulos:** Thank you.

How does Canada compare to other countries in terms of domestic procurement versus external procurement? Do you know how other NATO countries or, for example, G7 countries, compare to Canada in terms of reinvesting in their own industry?

**Mr. Yves Giroux:** Based on my knowledge, it seems to be broadly similar. Of course, there are exceptions for big countries like the U.S., which has a strong, wide military industrial base, but for other smaller countries, it is broadly similar to Canada.

**Ms. Emmanuella Lambropoulos:** Okay

Industry does feel that if we don't at least prioritize them in terms of contracts, then other countries are also going to have difficulty going towards them because they won't feel they have credibility because their own country isn't preferring them. By doing this, then, we are only making it worse because the small base that exists in Canada is only going to be getting smaller and smaller. Is there

no way that you could see a potential way to help change that? Is there no way there could be better communication, perhaps, between the government and industry in order to really show, "This is what we need. These are what our needs are going to be. This is the vision we have going forward, and we would like to prioritize you"?

Also, they feel that because there's this interoperability that you're mentioning, if we were to choose and see that Canada produced something great, then we could also promote it abroad. Then we could have some of our Canadian technology, which is pretty good technology, helped in that way. We're pretty good at this especially in the aerospace area. What are your thoughts on this?

**Mr. Yves Giroux:** I think you raise a very good point. If Canada does not rely on its domestic producers, it becomes difficult for them to be credible when they try to sell their products abroad if their own national government is not even depending or relying on them to equip its armed forces. That leads to difficult decisions at the political level as to when and what to procure and who to ask to supply the Canadian Forces. Do we go with the lowest bidder or do we go with the lowest bidder or a Canadian producer to ensure this becomes a national champion or a nationally recognized supplier, which can then become also recognized by other armed forces abroad and export its product? It's a delicate balancing act.

**The Chair:** Thank you, Madam Lambropoulos.

**Ms. Emmanuella Lambropoulos:** Thank you.

**The Chair:** Colleagues, we've been very efficient. Thank you to our witnesses. For the first time I can remember, I actually got in two full rounds in the time allotted.

As you know, we are intending to go in camera after this, so I just want to canvass the room as to whether you want to go for a third round. If we shrank the round to, say, three minutes and one minute, would that be of interest? These are valuable witnesses here. Would that work? Are we ready for that?

Okay.

If that's all right with you and you're not going to charge us overtime.... One coffee, that's the price. Okay.

Mr. Clerk, could you attend to the coffee needs.

With that, we'll start the third round.

Mr. Bezan, you have three minutes.

• (0945)

**Mr. James Bezan (Selkirk—Interlake—Eastman, CPC):** Thank you, Mr. Chair.

I want to thank the PBO for being with us today.

You mentioned a couple of times now reducing the number of players and having one point of ministerial accountability, one senior civil servant to also be in that accountability chain.

Who would you eliminate from the team to streamline it and what role can PCO play in helping oversee and coordinate defence procurement and speed up that process?

**Mr. Yves Giroux:** Personally, I am agnostic as to who should be in the driver's seat, so to speak, as long as it's somebody with the right expertise and the right knowledge and who is well supported by a sufficient number of officials and the right skill set.

When it comes to a coordination role, in my experience whenever there is a group or a task force, or whatever you want to name it, that's housed at PCO, the Prime Minister's department, it tends to focus the minds in the public service and it tends to signal the issue is very important to the Prime Minister and to the clerk. Having a coordination group or a responsible secretariat within the Privy Council Office, which is the Prime Minister's department, usually tends to signal to the entire bureaucracy that the issue is very important. It tends to make things happen, and make them happen as quickly and efficiently as possible.

**Mr. James Bezan:** Thank you very much.

The other issue we've been talking about is ITBs. Industry Canada is responsible for ensuring that ITBs are actually taking place. Are they policing it to ensure that there is dollar-for-dollar value? Are they making sure that it's actually creating high-skilled jobs and expanding our industrial base, or has it become more of just a shell game, moving money between different companies that could end up buying a potato farm in Manitoba, for example?

**Mr. Christopher Penney:** I can certainly say that ISED has personnel who verify every transaction under defence contracts to make sure there is no double counting and that these funds are actually spent.

With regard to the creation of employment and the economic activity aspects, they use a modelling approach to estimate that. It's not a situation where they're counting  $x$  number of jobs created in such-and-such a locality. It's estimated via models.

**Mr. James Bezan:** Do I still have any time left, Madam Chair?

[Translation]

**Ms. Christine Normandin:** You have 20 seconds left, Mr. Bezan.

[English]

**Mr. James Bezan:** I'll go to my final question.

If we are talking about creating a sovereign capability within our defence industrial base, the policy should be, then, to buy Canadian whenever possible, and only off the shelf when we don't have an affordable Canadian option. Would that be it, in your estimation, based on all the work you guys have done over the years on defence procurement?

**Mr. Yves Giroux:** That seems to already be the case, to a certain extent. That's a policy decision that's outside my realm, but that is one possible approach.

**The Chair:** Thank you, Mr. Bezan.

Mr. May, you have three minutes.

**Mr. Bryan May (Cambridge, Lib.):** Thank you, Chair.

A PBO report on progress under Canada's defence policy "Strong, Secure, Engaged" noted delays in capital spending and a shift in expenditure to later years. This shift is expected to mean that project costs will be higher than initially projected. At the same time, a recent DND internal audit noted a large portion of unfilled positions for procurement professionals and noted competition with the private sector as a main driver.

In your opinion, sir, could spending more on ensuring that National Defence has the capacity it needs actually save us money in the long term by helping to avoid project delays that lead to these cost increases?

• (0950)

**Mr. Yves Giroux:** Well, the number of military procurement personnel at DND and PSPC is certainly one factor explaining the delay in procuring some major equipment, but it's not the only one. Increasing the number of procurement personnel is probably necessary, I think, but it may not be sufficient in ensuring that the pieces of equipment that DND needs for its forces would be procured on time and within budget.

It's necessary but probably not sufficient. There are other issues at play, such as the capacity in Canada for domestic production, for example.

**Mr. Bryan May:** Thank you.

The PBO conducted an analysis on the industrial and technological benefits policy last year. Could you go through a little bit more of what the main findings of that analysis were?

**Mr. Yves Giroux:** We found there were some issues with the ITB. We looked at a limited period of time. The ITB was in place since 1986, so we looked at the period that started, if my memory serves me well, in 2015. We found there was about \$18 billion in ITB. The majority of these ITBs were to larger corporations. Only less than 20% of ITBs went to small and medium-sized businesses.

We also found that despite the fact there is a multiplier that gives credits between four to nine times the amounts actually spent to the businesses themselves if they spend in categories that are high value, such as post-secondary education and R and D, only 5% or so was effectively spent in these categories. That's despite the fact that they get between four and nine times the value in credit towards meeting their targets in ITB.

That's a very short, high-level summary of the findings on our ITB report.

**The Chair:** Thank you, Mr. May.

You have one minute, Madam Normandin.

[Translation]

**Ms. Christine Normandin:** As we are now completing a study on this, I'd like to hear a general comment on cybersecurity, including life cycle analysis. At the Office of the Parliamentary Budget Officer, what challenges result from the fact that this field is evolving at lightning speed and that we are always trailing behind the latest technological breakthroughs?

**Mr. Yves Giroux:** That's not something we've studied in any detail. Unfortunately, I have no significant or relevant comments to make. Sorry.

**Ms. Christine Normandin:** Okay, thank you.

[English]

**The Chair:** Thank you for that efficient and excellent question.

Madam Mathysen, you have one minute.

**Ms. Lindsay Mathysen:** To conclude, I put forward private member's Bill C-300 to try to get at what we were discussing in terms of the money that is supposed to go into Canadian hands at source and which is finding its way into more of the foreign larger corporate hands.

We talk about the spin-off jobs in my city. In my constituency, there's a very large contractor, but it's the smaller spin-offs....

Is that considered in a lot of these projects within your analysis, and is it just more of the hardware, or were you looking as well at training and education in some of the companies that were doing that work?

**Mr. Yves Giroux:** Our reports so far have focused on the expected costs of procuring these major pieces of equipment. We have not looked at the spin-offs or the economic benefits or the industrial benefits.

In and of themselves, the major procurement projects we have looked at are massive and they require quite a bit of analysis. Essentially, our capacity to do that analysis sits here to my left. There's some help that we get in the office, but by and large, he's the bulk of our capacity.

**The Chair:** Thank you, Ms. Mathysen.

Mr. Bezan, you have three minutes, please.

**Mr. James Bezan:** Let's go back to the issue of looking at where the government has allowed money to lapse. You were saying it's \$2 billion just on capital spending this year and there's a \$4-bil-

lion difference between the departmental plans and the main estimates.

As these numbers continue to reduce overall defence spending, how much is that impacting the numbers you forecasted on Canada meeting the 2%? You already said that over the next five or six years, there's a \$75-billion shortfall between 2% GDP and what was planned. Are we now adding in another \$10 billion plus on top of that \$75 billion?

• (0955)

**Mr. Yves Giroux:** It's clear that when we have a shortfall in capital spending, it likely reduces the ratio and it further takes us away from reaching the 2% NATO target, but it also has another impact. If you don't spend money now and you spend the same amount in the upcoming years, with inflation that is specific to the defence sector, it reduces the absolute value of that money. If you spend \$4 billion now versus spending \$4 billion in five years, you can buy less gear with the same billions of dollars five years from now due to inflation. It also impacts the capacity of DND to acquire military bases, equipment, barracks and so on.

In the absence of an increase in the overall amount, delaying also has a detrimental impact on the value of what you can buy.

**Mr. James Bezan:** Is defence inflation similar to the Canadian average or is it much higher? How much does that erode the buying power of the Canadian taxpayer? How much more is it going to cost the Canadian taxpayer to get the same kit?

**Mr. Christopher Penney:** It's actually quite dependent on which type of materiel is being considered. In the case of naval shipbuilding, for instance, you'll see defence inflation rates between 1.2% and 4%. If it's for land vehicles, it's right in line with the economy.

It does vary, but as a general rule, it's a few percentage points higher.

**Mr. James Bezan:** If we're running at 4.2%, or where the inflation is right now, we could expect somewhere between 4% and 6%. Is that what you're saying?

**Mr. Christopher Penney:** That's correct.

**Mr. James Bezan:** In the F-35 study that you guys are doing right now, are you taking a hard look at what that inflationary cost was from making the decision to purchase 10 years ago versus a purchase now and when the fighter jets are actually procured?

**Mr. Christopher Penney:** Unfortunately, we won't be considering the difference—or the money lost, I suppose—had we procured sooner. You're right. There is some amount there.

**The Chair:** Thank you, Mr. Bezan.

The final question goes to Mr. Sousa.

**Mr. Charles Sousa (Mississauga—Lakeshore, Lib.):** Thank you very much, gentlemen.

Can you tell us what the balance of trade in the military industry is between Canada and the other NATO countries?

**Mr. Yves Giroux:** That's an interesting question. I say that because I don't have the answer, unfortunately.

**Mr. Charles Sousa:** The reason I'm asking is that we're often chastised for the percentage of spending by NATO, and yet in some respect we're being told by the very producers that we buy from... There obviously is an interest in our procuring from some of these major markets.

My suspicion, and I think you've alluded to this now a number of times, is that Canada has a small critical mass. We're unable to compete effectively on some of the big projects. Consequently, we are reliant on foreign support. At the same time, we're trying to procure locally to provide some sovereignty issues on our part, but then, how many of our local producers are selling abroad? Do you have a sense?

**Mr. Yves Giroux:** No, I don't have a sense, but I know there are areas of excellence that export. It's been widely reported in the media for some of these years, but I don't have an overall number when it comes to the balance of trade in the military area.

**Mr. Charles Sousa:** It would be nice to know.

In regard to the actual procurement process, you talk about it being more focused and having fewer individuals. The complexity of these projects is substantive. Treasury Board is going to be required in order to allot the required funding.

How is that going to actually make procurement that much more simple, when in fact you're going to end up going through the same process anyway?

• (1000)

**Mr. Yves Giroux:** If you have one ultimate decision-maker responsible as opposed to having two or even more than two, it reduces the number of steps. If they can sing from the same songbook at the beginning as opposed to having interdepartmental meetings, meeting after meeting, and having different processes in two different institutions, it can streamline things.

You're right. If you have the right persons, despite having the wrong governance structure, sometimes it can work, but it has to have the right governance structure in place to streamline things to the extent possible.

**Mr. Charles Sousa:** I appreciate that.

If there's more time, I want to understand the political undertones here. The sovereignty issues, the notions of trying to support other issues beyond the diplomatic stuff—I guess I could put it that way—that has to... You can't determine that on occasion. That's where the complexity comes into play.

I appreciate your testimony.

**The Chair:** Thank you, Mr. Sousa.

Surprise, surprise, a former finance minister defends the Treasury Board. That's the first time in history that anyone has defended Treasury Board.

With that, I want to thank our witnesses. You have launched this study brilliantly. We really do appreciate it. You've directed us to the critical questions that need to be asked.

Thank you for not only your hour, but your hour and 15 minutes.

With that, colleagues, I'm going to adjourn, but for those who are online—

**The Clerk of the Committee (Mr. Andrew Wilson):** You're going to suspend.

**The Chair:** I thought it was adjourning.

**The Clerk:** No, you just need to suspend.

**The Chair:** Okay, apparently I'm suspending.

**The Clerk:** You can adjourn if you want.

**The Chair:** That would not be a good idea.

For the benefit of the colleagues online, which is why I thought we had to adjourn, you have to leave the meeting. In your memo, there is a second set of instructions as to how to sign in. The sooner you do that, the sooner we can get on with the in camera portion of our meeting.

With that, the meeting is suspended.

*[Proceedings continue in camera]*









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