

Minister
of National Defence



Ministre
de la Défense nationale

Ottawa, Canada K1A 0K2

GOVERNMENT RESPONSE

OCT 06 2017

The Honourable Kevin Sorenson
Chair
Standing Committee on Public Accounts
House of Commons
Ottawa Ontario K1A 0A6

Dear Mr. Sorenson,

Pursuant to Standing Order 109 of the House of Commons, I am pleased to present the official Government Response to the 29th report of the Standing Committee on Public Accounts entitled: *Report 7 – Operating and Maintenance Support for Military Equipment – National Defence Fall 2016 Reports of the Auditor General of Canada*, which was tabled in the House of Commons on June 8th, 2017.

Ensuring the proper stewardship of public resources is of utmost importance, and the Government remains committed to continuing to improve the management of military equipment, as evidenced in Canada's new defence policy, *Strong, Secure, Engaged*. National Defence appreciates the insight provided by the Standing Committee on Public Accounts, continues to work diligently to address the concerns identified in your report, and agrees with its recommendations. National Defence will provide reports by the timelines requested in the Standing Committee on Public Accounts report.

I would like to thank you and the other members of the Committee for undertaking the study to produce this report, and for your continued commitment and service to Canadians.

Sincerely,

A handwritten signature in black ink, appearing to read "Harjit Sajjan".

The Honourable Harjit Sajjan, PC, OMM, MSM, CD, MP

CC:
Michel Marcotte
Clerk, Standing Committee on Public Accounts

Canada

GOVERNMENT RESPONSE

GOVERNMENT RESPONSE TO THE REPORT OF THE STANDING COMMITTEE ON PUBLIC ACCOUNTS ENTITLED: *REPORT 7, OPERATING AND MAINTENANCE SUPPORT FOR MILITARY EQUIPMENT – NATIONAL DEFENCE, OF THE FALL 2016 REPORTS OF THE AUDITOR GENERAL OF CANADA*

Introduction

The Government of Canada has considered the report of the Standing Committee on Public Accounts (PACP) entitled: *Report 7, Operating and Maintenance Support for Military Equipment – National Defence, of the Fall 2016 Reports of the Auditor General of Canada*.

The Government would like to thank the members of the Committee for undertaking such a thorough study. National Defence will provide all eight reports requested by the committee by the recommended deadline. The report for recommendation five is included in this response. In addition, National Defence would offer further information on each of the recommendations below.

Recommendation 1: That, by January 31st 2018, National Defence provide the Committee with a report assessing the effectiveness of the new challenge function and the Sustainment Initiative in ensuring that equipment support contracts are based on achievable planning assumptions and allow for adjustments in the contracts based on changing circumstances.

The Government agrees with this recommendation. The Sustainment Initiative, which brings together procurement experts from National Defence, Public Services and Procurement Canada, and Innovation, Science and Economic Development, to identify best approaches for in-service support, began rolling out in June 2016, and is expected to be fully implemented in January 2018. As such, while National Defence will provide an interim report on the progress of the Sustainment Initiative by January 31st 2018, it will take two to three years of data collection in order to determine the overall effectiveness of the initiative through the performance measurement of equipment support contracts.

The Office of the Auditor General (AG) noted that National Defence overestimated equipment use, underestimated support costs, and under-resourced personnel requirements in its planning assumptions, which led to higher than expected support costs, did not optimize value for money, and in some cases, reduced the availability of equipment.

The Sustainment Initiative is one way in which these challenges can be mitigated, as it significantly improves National Defence's approach to in-service support contracting. It allows

contracting experts to collaborate earlier and more closely with each other and with the Canadian defence industry to develop tailored support solutions that balance the principles of performance, value for money, flexibility and economic benefit to Canada, rather than relying on prescriptive contracting frameworks that discourage innovation.

Under this program, new and existing equipment support contracts over \$20 million in total value will be subject to a Sustainment Business Case Analysis process, which will be triggered at points that include the requirement for a new support contract, contract renewals and the exercise of significant option periods within existing contracts. The relevant departments will ensure there is the appropriate level of flexibility to adjust contracts based on changing circumstances, keeping in mind the principles identified above - equipment performance, economic benefit and value for money.

The tri-departmental approach of the Sustainment Initiative also ensures a challenge function is inherent in the system, as each of the three departments must collaboratively review, negotiate and approve the approach being proposed. These results are documented and retained to inform future contracting decisions.

Recommendation 2: That, by January 31st 2018, National Defence provide the Committee with a report detailing how proper life-cycle costing is now being used, and how its Investment Plan has been updated to reflect more complete life-cycle costs.

The Government agrees with this recommendation, and commits to providing a report to demonstrate its improvement in how proper life-cycle costing is being used in National Defence by January 31st 2018.

The AG observed that the 2014 National Defence Investment Plan did not include full life-cycle costs for the equipment considered in the audit, and recommended that life-cycle cost estimates should be prepared for key decision points for each type of equipment. Furthermore, the AG recommended that National Defence monitor actual costs against estimates, and update the Investment Plan to include more complete life-cycle costs.

Since the audited contracts were signed, Treasury Board policies have evolved to require departments to consider all relevant costs (acquisition, support, infrastructure, personnel and operating costs) over the useful life of the equipment, and not the initial acquisition costs (as was the case when those contract were signed). National Defence's costing process has been standardized to comply with Treasury Board guidelines and is in line with international costings standards, and can now deliver high quality cost estimates that are credible, well documented, repeatable and promote accountability.

Much of the improvement is attributable to a realignment of key personnel involved in costing. The Chief Financial Officer (CFO) has assumed full responsibility for the costing function within National Defence, expanding the costing function from a small directorate to a much larger organization, the Centre for Costing in Defence (CCD), and internally realigning it to report directly to the CFO. In addition, the CCD is advancing the skills and knowledge of its analysts, adopting the International *Cost Estimating Analysts Association* curriculum, with nearly 50 employees currently progressing through the Association's *Cost Estimating Body of Knowledge* program.

The CCD, working closely with Defence Research and Development (DRDC), has used leading and best practices to create tools and methods to further improve the costing process. Some tools and methods that have been developed to date include a standardized Cost Breakdown Structure that can map to American and NATO standards, Best Practice Spreadsheet Modelling Standards, Cost Risk Framework, including Monte Carlo statistical analysis and risk and uncertainty methods, and Quality Review Procedures. The CCD has also worked with DRDC to develop a data collection model to enable better data collection for cost estimating.

In addition, to ensure consistent data collection, the CCD publishes the Cost Factors Manual, which provides standard costs for the main categories of resources used by National Defence, such as personnel, equipment and facilities. The Economic Model is another tool created by the CCD to measure and forecast defence specific inflation to allow for more precise costing, in addition to the publication of other guides such as foreign exchange and energy forecasts.

Some of these efforts are outlined in *Strong, Secure, Engaged*, which commits that, in support of the 2017 Investment Plan, cost estimates for all planned and ongoing projects be updated to reflect a more complete life-cycle cost estimate, to include sustainment and inflationary costs. The 2017 Investment Plan also will include a plan to identify individual acquired goods and services investments over \$20M and life-cycle costs on a program basis. In addition, National Defence will monitor life-cycle costs at key decision points. This will result in significant progress towards addressing the AG observations and recommendations in this regard.

Recommendation 3: That, by January 31st 2018, National Defence provide the Committee with a report explaining how its use of incremental funds has been clarified.

The government agrees, and National Defence commits to providing a report to explain how use of incremental funds has been clarified by January 31st 2018.

The AG noted that National Defence did not monitor whether it used funds from the fiscal framework for the purpose for which they were intended, and recommended that this funding should be tracked separately and used only for the equipment for which it was allocated.

Strong, Secure, Engaged identified a new Defence Funding Model, which is based on acquiring capital assets using Vote 5 capital funding sources from the accrual envelope. Sustainment and operating costs related to those assets will be funded from the Vote 1 operating budget sourced from the fiscal framework.

Previously, the incremental Vote 1 sustainment and operating funding received by Defence for new assets were sourced from the accrual envelope. This practice created confusion, as this incremental funding, downloaded for a specific purpose, may not always have been expended on that specific asset. As sustainment funding is generally managed on a portfolio basis, surpluses in incremental funding for a new asset in a specific year would be used to offset other sustainment pressures. Conversely, shortfalls in sustainment funding for a new asset would be offset from other surpluses in the portfolio.

Moving forward, National Defence is committed to providing greater transparency in the management of incremental sustainment and operating costs. Similar to acquisition funding received for a specific project, National Defence will allocate and track the use of incremental operating costs on an asset basis to demonstrate its ability to utilize new funding in the manner approved by Treasury Board. Over time, National Defence will explore the possibility of attributing existing baseline sustainment funding against each equipment type to provide a full representation of sustaining funding by weapon system for enhanced performance measurement.

Recommendation 4: That, by April 30th 2018, National Defence provide the Committee with a report detailing its Defence Team Human Resource Strategy, as well as the plan and schedule for its implementation.

The Government agrees with this recommendation. As requested, National Defence will provide a report detailing the strategy and its planned implementation schedule, by April 30th, 2018.

The AG identified National Defence's personnel shortage in operating and servicing existing equipment, as well as in negotiating, monitoring and challenging contractor performance. The AG recommended that National Defence monitor and manage support risks to ensure sufficient personnel and funds are aligned with operations and training requirements.

To help meet this challenge, National Defence is developing an integrated human resource strategy to balance skills and personnel across the department. Working in alignment with *Strong, Secure, Engaged*, the *Defence Team Human Resources Strategy* will harmonize independent human resources strategies across National Defence. This will help foster an integrated approach to personnel management and will synchronize departmental efforts.

One of the goals of the *Defence Team Human Resources Strategy* is to align the defence team in

order to better achieve departmental goals. While not explicitly stated in the strategy itself, this includes allocating sufficient personnel to support new equipment in terms of maintenance, operation and training, as noted in the Committee's report.

While the AG noted that recruitment targets in the *Canada First Defence Strategy* were not met, *Strong, Secure, Engaged* commits to nine concrete new initiatives to ensure the effective recruitment, training and retention of the future work force, as summarized on page 22 of *Strong, Secure, Engaged*. The *Defence Team Human Resource Strategy* will further work to ensure the principles, goals and initiatives enshrined in the new defence policy are applied across the department.

The *Defence Team Human Resource Strategy* is currently in development, with implementation expected to begin in 2018-19.

Recommendation 5: That, by October 31st 2017, National Defence provide the Committee with a report detailing the concrete measures the Department has implemented to ensure that its data is used effectively to make evidence-based decisions.

The Government agrees, and provides the following report.

Going forward, the department will increase its focus on performance measurement as a means towards continuous improvement. Specifically, the Department of National Defence is establishing, governing and operationalizing a Business Analytics capability that will support decision makers at all levels. This capability will collect data, interpret it, turn it into information, and then turn information into business intelligence. In 2018, these efforts will be concentrated on three areas: the Departmental Results Framework (DRF), business planning, and the supply chain, which includes materiel management.

The end-state of this initiative is to have a capability that will support both the strategic and the day-to-day management of the defence program across National Defence. The initiative will deliver department-wide reporting and analytics capability in order to support decision makers who execute priority operational processes at all levels of National Defence. This analytics capability will build upon existing investments made in Enterprise Resource Planning, which was introduced to facilitate better management of all business/operational functions and decision-making, as well as to improve the integrity of financial data and reporting.

The strategic objectives for this analytics capability are as follows:

- a) Establish a supported governed analytics capability with personnel, processes and tools that enable the use of analytics at all levels of National Defence;

- b) Drive Digital Transformation with an enterprise approach, unlocking the potential to innovate at scale and enabling coordination/benefit across the department;
- c) Support the rollout of the DRF by leading efforts to digitize DRF processes and reduce the cost of data creation, reporting and analytics;
- d) Establish Data Management as a core capability in order to manage data as a strategic asset and to govern investments and manage data readiness across National Defence;
- e) Drive the integration of analytics with performance management at an enterprise level and enable the integration of analytics in priority operational processes throughout National Defence;
- f) Improve the management of information and reduce security vulnerabilities;
- g) Strengthen the culture to support enterprise performance management and generate leaders of Digital Transformation;
- h) Build an ecosystem of Business Analytics stakeholders and partners who are enabled to innovate and accelerate Digital Transformation in National Defence.

The Business Analytics capability project will commence this summer, and its implementation is expected to begin by summer 2018.

Recommendation 6: That, by January 31st 2021, National Defence provide the Committee with a report assessing the overall effectiveness of all the Department's initiatives that seek to improve data quality in the Defence Resource Management Information System, including the Inventory Management Modernization and Rationalization Project, the National Stocktaking Project, and the implementation of materiel accountability action plans.

The Government agrees with this recommendation, and commits to providing a report assessing all the initiatives to improve data quality in the Defence Resource Management Information System (DRMIS) by January 31st 2021.

The department remains committed to improving the data quality of its information in DRMIS. Its management action efforts include integrating its related business requirements into DRMIS, executing national stocktaking and stock verification visits to augment mandated physical counts of materiel to ensure data accuracy in DRMIS and to rationalize the inventory held in National Defence, while modernizing the business process within an integrated DRMIS enterprise environment.

These efforts are part of a larger, more comprehensive effort to improve materiel data quality. These efforts are articulated in the National Defence 2016 Inventory Management Action Plan and represent a multi-year deliberate effort that also includes robust department level governance, Automatic Identification Technology, Enhanced Materiel Accountability, Pricing Project and Pricing Legacy Data Clean-up. These collective efforts will have a significant and positive impact on data quality within DRMIS.

Recommendation 7: That, by April 30th 2018, National Defence provide the Committee with a report detailing the progress regarding the streamlining of internal governance processes to align with the Treasury Board Policy Suite Reset.

The Government agrees with this recommendation, and the department will provide a more detailed report concerning the streamlining of internal governance processes to align with Treasury Board Policy Suite Reset by April 30th 2018.

While the AG did acknowledge more departmental oversight into contracting, including the improved decision-making this could enable, they recommended that National Defence streamline governance processes. In addition, the AG recommended better integration of resource planning in equipment support matters.

National Defence amends its processes in response to changes in policy and governance changes from central agencies. This will continue once the Treasury Board Policy Suite Reset, which will update and streamline all Treasury Board policies, is implemented.

In order to better streamline governance processes, in February 2017 National Defence launched the National Defence Project Approval Process Renewal (PAPR) initiative, which helps create a more timely, effective and responsive procurement process. For instance, it seeks to streamline the approval process for projects that fall within the Minister of National Defence's authority. Subject to certain conditions, Ministerial approval for expenditure authority for procurement projects may only be needed once, as opposed to twice under the previous system. Other ways in which the PAPR initiative has improved the timeliness of defence procurements is through creating and staffing positions identified as chokepoints in the procurement process.

PAPR has also led to other improvements in defence procurement. The establishment of the Capital Investment Programme Plan Review provides defence leadership with the opportunity to review and adjust capital investment decisions on a regular basis, helping to ensure procurement is driven by departmental priorities. PAPR is also aligned with and supportive of other key initiatives such as the Defence Procurement Strategy, Treasury Board Secretariat Policy Suite Reset, and the Independent Review Panel for Defence Acquisition, an independent,

third party panel that provides a challenge function to validate stated requirements related to major procurement projects.

Recommendation 8: That, by April 30th 2018, National Defence provide the Committee with a report detailing the progress of the Departmental Results Framework—including the rationale for selecting key performance indicators regarding equipment support and availability—as well as how internal results are being reported to Parliament and to Canadians.

The Government agrees with this recommendation, and commits to an update report on the progress of the Departmental Results Framework by April 30th 2018.

The AG noted that while National Defence has performance measures in support contracts with the private sector, similar measures do not exist for maintenance that National Defence itself performs. The office recommended that National Defence rectify the situation.

A new National Defence Departmental Results Framework (DRF) is currently under development. Once approved, the DRF is scheduled to be in place on April 1st, 2018. The DRF will contain performance measures across all of the Department's core responsibilities, but more applicable to the AG's audit, the DRF is expected to capture indicators relating to serviceability and availability of military equipment. The performance measures will encompass calculation methodologies and clear definitions to better ensure consistency in reporting. Once the DRF is implemented, the Department will be in a better position to improve the monitoring of and reporting on maintenance performance indicators in a more consistent manner.

The DRF will contain performance indicators demonstrating whether National Defence obtained the required equipment to meet requirements, and whether or not that equipment is ready for operations. Within the DRF, the calculation methodology and definitions for availability have been both clarified and simplified to better ensure consistent and meaningful performance measures.