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## **Standing Committee on Public Accounts**

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**EVIDENCE**

**Thursday, May 3, 2012**

**Chair**

**Mr. David Christopherson**



## Standing Committee on Public Accounts

Thursday, May 3, 2012

●(0845)

[English]

**The Chair (Mr. David Christopherson (Hamilton Centre, NDP)):** I now call this 42nd meeting of the Standing Committee on Public Accounts to order.

We have with us today Mr. Alexander, Parliamentary Secretary to the Minister of National Defence, who returns. Welcome.

Mr. Hawn, welcome back again.

We're also joined by Mr. John McKay, my former colleague on the national defence committee, who is the national defence critic for the Liberal Party. Welcome, sir.

And the Honourable Bob Rae, interim leader of the Liberal Party, is here with us also. Welcome, Mr. Rae.

With that, folks, today will be a regular two-hour meeting. The first hour will be with the Parliamentary Budget Officer. The second hour will be a resumption of our discussions and questions with the deputy ministers.

Are there any questions, comments, or concerns about the agenda as I've outlined it?

Very well, we'll move forward.

Mr. Page, welcome, sir. I would ask you to introduce your delegation and present your opening remarks. Then we'll begin our questions and comments, in rotation.

Colleagues, I want to remind you that with one hour we won't quite make the regular rotation. I'll leave it with you whether we will just exhaust it as far as we can or if some members have some creative idea they'd like to approach. Notwithstanding that, we'll begin the regular procedure. When we run out of time, we run out of time. Then we'll start the second hour of our meeting.

Agreed? Very good.

Mr. Page, you now have the floor, sir.

**Mr. Kevin Page (Parliamentary Budget Officer, Library of Parliament):** Thank you, Mr. Chair.

By way of introduction, I have Peter Weltman, one of the principal authors of our F-35 work. Tolga Yalkin, senior analyst, is another principal author of our F-35 work. Mr. Sahir Khan is the assistant parliamentary budget officer for expenditure and revenue analysis. And Dr. Mostafa Askari is our assistant parliamentary budget officer for economic and fiscal analysis.

Good morning, Mr. Chair, vice-chairs, and members of the committee.

[Translation]

Thank you for inviting me and my colleagues to speak to you today.

I have provided you with a deck which tracks my opening remarks. I would be happy to discuss the slides in greater detail.

Broadly speaking, I have three points to make. I will attempt to be as brief as possible. All points concern the PBO and the information provided to it or the information it has provided in relation to the proposed acquisition of the F-35 fighter jets.

●(0850)

[English]

First, over the last few weeks it seems that some confusion has surfaced as to whether or not the PBO included operating costs within its estimate provided to Parliament in March 2011. I'm here to reconfirm that it did; the PBO estimate includes operating costs.

When the PBO provides operating and support costs in its report, it tracks the language of the Department of National Defence costing guide, second edition, 2006. In chapter 2, page 2, that guide provides the following:

Operating costs include: personnel costs such as the activation of reserves, overtime cost of civilian employees, and the cost of any other personnel hired to provide service; rations, quarters, temporary duty, travel and transportation; variable and step variable operations and maintenance costs of equipment; total operating costs for facilities and materials consumed. The cost of capital assets purchased by the Department for the purpose of providing the service may also be included.

This definition of "operating costs" is consistent with the U.S. Department of Defense *Cost Analysis Guidance and Procedures*, published in December 1992. Furthermore, inclusion of operating costs within a life-cycle cost estimate is consistent with Treasury Board policy. Given this, it seems difficult to understand how there could have been any confusion as to whether or not the PBO included operating costs within its estimate.

[Translation]

Second, over the past few weeks, it has become clear that the Department of National Defence provided the PBO with figures that did not include all operating costs. The PBO understood that it had been provided with full life cycle costs from DND as required by the House of Commons Standing Committee on Finance in its November 1, 2010 motion. That motion required the provision of:

...All documents that outline acquisition costs, life cycle costs, and operational requirements associated with the F-35 program and prior programs (CF-18)...

[English]

In March 2011 the PBO provided Parliament with an independent life-cycle cost estimate for the F-35A. As part of that report, it compared figures provided by DND, obtained as a result of the motion, to its own estimates.

After publication of the PBO report, DND compared on its website, side by side, its figure of \$5.7 billion and the PBO's figure of \$14 billion, labelling both as operating and support costs. While the PBO's cost estimate was complete in this regard, it has since become evident that the government's public figures did not include all components of full life-cycle costs, as required by the House finance committee motion of March 2010.

Third, it might now be observed that the figures found in the Auditor General's report, confirmed as accurate by the Minister and Deputy Minister of the Department of National Defence, bring that department's life-cycle cost figures into the same order of magnitude as the PBO estimate. Furthermore, DND's figures and the PBO's estimates are in line with those found in the United States Department of Defense December 2011 Selected Acquisition Report, released last month.

Thank you again, for inviting us here today. We would be happy to take your questions.

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

Colleagues, we'll now turn to questions and comments in rotation in the prescribed manner.

Mr. Saxton, you now have the floor.

**Mr. Andrew Saxton (North Vancouver, CPC):** Thank you, Mr. Chair.

Thank you, Mr. Page and colleagues, for coming here this morning.

My first question is to ask you to please describe the pricing model that you used in the first report on the aircraft, and also, please explain the limitations of this model.

**Mr. Kevin Page:** Thank you, sir, for the question.

The model that we used in the report, which is actually described in some detail—certainly the model and the assumptions—is what we would call a cost-estimating relationship model. We're historically extrapolating costs on fighter planes.

We used this extrapolation of 30 years of history of previous fighter planes, indexed, based on a per-kilogram kind of basis, to project forward an estimate of acquisition costs. Then we derived sustainment costs based off that estimate of acquisition costs, based on historical estimates for different cost categories.

There are benefits and certainly limitations for this model. First of all, when we look at these top-down models, sir, we see them as tests of reasonableness of where costs may be. So we were actually pleased to see today—or actually earlier than today, when we saw the release of the full life-cycle cost estimates from the Department

of National Defence—that our numbers are roughly in line on a total life-cycle cost basis.

But again, you're using high-level data and you're extrapolating forward using broad-based assumptions. You're assuming that history will repeat itself. So there are always limitations in that sense.

Yes, I think these sorts of models should be complemented by much more detailed, bottom-up models to provide real confidence. We hope, going forward in that context, to work with the new secretariat, or they could conduct some of this work themselves. I think it would add a lot to this debate in Parliament.

• (0855)

**Mr. Andrew Saxton:** Thank you.

Now, is another name for this costing model that you used parametric?

**Mr. Kevin Page:** Certainly we're using parameters. Again, we're creating an index based on history for these costs. There are parameters we're looking at that deal with performance, deal with design, and deal with weight. But yes, sir, I'm sorry, we're using parameters.

**Mr. Andrew Saxton:** Is that a yes, or—

**Mr. Kevin Page:** It's a yes. I apologize, sir.

**Mr. Andrew Saxton:** That's a yes. Okay, thank you.

Now, it's generally understood and generally agreed that this type of a costing model is used very early on in the development stage. So my question to you, Mr. Page, is why would you choose to use this type of costing model when the jet had in fact already been built and was already flying?

**Mr. Kevin Page:** That's a very good question, sir.

When we started this project in 2010, we went to different people to look at what our choices were with models. We were also looking at the history of this particular fighter plane from the early 1990s to present day. We looked at more bottom-up, more detailed parameter models where you literally cost component by component—the engine, the airframe, stealth components, etc.—and then we looked at these cost-estimating relationship models.

We actually invested in proprietary models in both cases. We chose this one, sir, primarily because it looked like history was repeating itself in this case. The costs were providing significant overruns. Even when we were doing our work, already just in the research and development phase, there was already 60% cost overruns. It looked, in that sense, like history was repeating itself, and we became comfortable with this high-level estimate.

I repeat, to your very good first question, these are high-level models, and they should be complemented by the work of DND and other officials, more bottom-up detailed models.

**Mr. Andrew Saxton:** So the fact is that this is a high-level model; it's based on assumptions and the information that comes out is only as good as the information that goes in. Is that correct?

**Mr. Kevin Page:** I think that's well said. I would add to that, sir, that these types of models.... Everybody is using these models. It wasn't hard to find them in the U.K. and the United States. They're well used. In the SAR reports that we're using now, we provide an estimate actually of O&S. It's based on a CER parametric kind of model. So these models are well used. They have limitations.

**Mr. Andrew Saxton:** Okay. From a technical perspective, can you explain how your costing model differs from that used by the Department of National Defence?

**Mr. Kevin Page:** Actually, Mr. Sahir Khan will take that question. Thank you, sir.

**Mr. Sahir Khan (Assistant Parliamentary Budget Officer, Expenditure and Revenue Analysis, Office of the Parliamentary Budget Officer, Library of Parliament):** Sir, we actually made a number of requests after the finance committee motion to get additional details. We have these actually published on our website.

**Mr. Andrew Saxton:** Can you explain the difference between your model and DND's?

**Mr. Sahir Khan:** Actually, sir, we have not been provided with the details of the modelling exercise. The response we had was that they were using information provided by the project office.

**Mr. Andrew Saxton:** You don't know the difference between your model and their model?

**Mr. Sahir Khan:** We were not asked to.... Our request from Parliament was not to review their model, sir.

**Mr. Andrew Saxton:** My request from me, today, is to explain the difference between your costing model and DND's costing model.

**Mr. Sahir Khan:** We don't know what their model is.

**Mr. Andrew Saxton:** You don't know what their model is. Okay. Very good.

In your report, Mr. Page, did you mention fuel, salaries, and other operating costs?

**Mr. Kevin Page:** Sir, when we provided.... When we are working with proprietors in this sort of case, we work with standard definitions of operating and support. We are working from U.S. definitions, which map very closely, as we highlighted in our opening remarks in our text.

**Mr. Andrew Saxton:** Did you include fuel?

**Mr. Kevin Page:** Yes.

**The Chair:** No, Mr. Saxton—

**Mr. Andrew Saxton:** Can you please provide the background information to our committee?

**The Chair:** Order, please.

Mr. Saxton, you're not starting out in the greatest way. You're pushing. I had asked you to come to order. At that moment, if somebody wants to say something, I'll listen to them, but you went in after the wire.

The question will stand. Your colleagues can pick up on it later, but your time has expired.

**Ms. Joyce Bateman (Winnipeg South Centre, CPC):** Point of order, Mr. Chair.

**The Chair:** Yes, Madam Bateman.

**Ms. Joyce Bateman:** I think the information that Mr. Page is referring to would be of benefit to all members of this committee and all visitors to this committee from Parliament, so would it be appropriate for us to receive that?

**The Chair:** It would also be appropriate for everyone to follow the rules so that we could have a fair hearing for all involved.

I allowed Mr. Saxton, as I do.... If it's after the time, I allow what's happening to be concluded. It had concluded a few moments after the time limit, and Mr. Saxton then put his question, which was over the time. If you noticed, I actually sat back a bit and let it go on, and then we started getting something over here. That's what happens when I get too flexible.

I think the request for the information is valid, but I would ask if one of the government members would reiterate that very quickly; it will only take a moment. Mr. Page can respond in the way he will, and then I can still go about trying to make sure that every member is treated equally.

● (0900)

**Ms. Joyce Bateman:** Mr. Chair, I will happily use some of my time to do that. Thank you for the clarification.

**The Chair:** You're very welcome. Thank you.

If there are no further interventions, we will move to Monsieur Ravnat and Madame Blanchette-Lamothe. Is there a split of time there? No?

Okay, Mr. Ravnat, you have the floor.

**Mr. Mathieu Ravnat (Pontiac, NDP):** Mr. Page, I think that Canadians are rightfully worried. We have the PBO saying one thing, we have the Auditor General saying another. We have the government grudgingly accepting that something may have gone awry in this, and then we have the deputy ministers essentially saying no, we did everything we had to do, there's no problem. There's a series of mixed messages here, and it's in that spirit that I'm asking you these questions.

My first question to you is simply, when you were looking at the history of fighter jets, how long was the shelf life for the CF-18s?

**Mr. Kevin Page:** Sir, with the CF-18s, the shelf life started in the early 1980s and continues to the present.

**Mr. Mathieu Ravnat:** So we're talking about 40 years. Okay.

So your 30-year assumption for sustainment costs, on the basis of the life of the CF-18s, is accurate.

**Mr. Kevin Page:** The information we got from the SAR, the selected acquisition report, work from DND, and just other airplanes in general was that 30 years is a reasonable estimate.

**Mr. Mathieu Ravnat:** So why would the Department of National Defence use a 20-year estimate?

**Mr. Kevin Page:** Sir, that's a better question put to the Department of National Defence. We're very comfortable with 30 years.

**Mr. Mathieu Ravignat:** In your opinion, obviously you've had some issues with getting information from the Department of National Defence, so my question to you is could they have lowballed the 20 years in order to appear as if the program was less costly than expected?

**Mr. Kevin Page:** Yes, I think we could.... The Auditor General provided some disclosure to us on what the numbers could look like on a 20-year basis—what's fully in. It's not hard for people like us to move numbers from 20 to 30 years, or to 36 years. We could easily do the work. But yes, you get a lower life-cycle number at 20 years.

**Mr. Mathieu Ravignat:** If you have a lower life-cycle number, obviously you have lower costs.

**Mr. Kevin Page:** You create the impression there are lower costs over a 20-year period, but again, it's not hard for us to extrapolate that to what that would look like on a 30-year basis.

**Mr. Mathieu Ravignat:** Were you able to get information from the Department of National Defence on the difference between their initial estimate of \$15 billion and what appears to be their hidden estimation of \$25 billion?

**Mr. Kevin Page:** Since the AG report we've had some, but very limited, follow-up with the Department of National Defence officials, and more on just providing confirmation on our side of what we had included in terms of operation and support. We were not poking at their numbers. All these numbers are on the DND website. All the correspondence is on our website as well.

**Mr. Mathieu Ravignat:** Did you ask for anything from the Department of National Defence that you did not receive?

**Mr. Kevin Page:** Again, the original request goes back to the House finance committee in the late fall of 2010, when they asked for full life-cycle cost. From the Auditor General's report, we have leaned that we received only partial information with respect to what we call sustainment, or on the operating and support costs.

**Mr. Mathieu Ravignat:** Why would you receive only partial information on your request for additional information?

**Mr. Kevin Page:** We don't know the reason for that, sir, other than what you have heard in previous testimony from deputy ministers.

**Mr. Mathieu Ravignat:** Would it be fair to say there was generally a lack of collaboration from the Department of National Defence with your office?

• (0905)

**Mr. Kevin Page:** I would say, with respect to the original request for information, that we in the committee received some but not all information.

**Mr. Mathieu Ravignat:** Could you be more specific about what other additional information you requested?

**Mr. Kevin Page:** Well, certainly partial information with respect to operating and support costs. Again, we received this information roughly less than a week before we released our document.

**Mr. Sahir Khan:** I would add that two weeks prior to the publication of the report, we had asked for clarification from the department on the partial information we received. Specifically, item number one on the list of a number of items was operating and support. We wanted further clarification on that figure.

**The Chair:** You have time for a quick one.

**Mr. Kevin Page:** May I add one point, sir? We also asked for information on their methodology and did not receive it.

**The Chair:** Thank you. I appreciate your cooperation.

Mr. Hawn, you have the floor, sir.

**Hon. Laurie Hawn (Edmonton Centre, CPC):** Thank you, Mr. Chair. I didn't think it was my turn yet, but thank you so much.

Thank you, Mr. Page and your associates, for being here.

I want to go back to the previous question. In your report on the costs of fuel, salaries, and other operating costs, as was attempted to be asked a few moments ago, can you provide the committee with all that methodology and all the information you used in your report, including any correspondence with consultants and so on?

**Mr. Kevin Page:** There's significant disclosure. I don't know what the page number is. Perhaps we can find it in our report on how we estimated operating costs. Again, it's a top-down model. We're using a standard definition of operating and support. We're looking at a 30-year history. Then we're projecting forward for this cost.

**Hon. Laurie Hawn:** You can provide all of that information to the committee?

**Mr. Kevin Page:** Absolutely. I'm saying we've provided a report. If you want additional information in terms of our estimates—they are technical in nature, how we extrapolated—we're happy to do that.

**Hon. Laurie Hawn:** As well as any correspondence you had with consultants you would have derived that information from—you could provide that?

**Mr. Kevin Page:** Yes, sir.

**Hon. Laurie Hawn:** Okay, thank you.

You had the DND costing handbook here. Just to be clear, when you talk about operating costs, is that talking about personnel costs, activation of reserves, overtime costs for civilian employees, and so on? And there are other things listed. Is that total costs, or is that delta for the new piece of equipment, over and above what is already being spent—i.e., for people who are already on salary, and so on?

**Mr. Kevin Page:** Yes, sir. We looked at total costs because we don't really know what's in the fiscal planning framework per se. We had no choice but to do a total-cost basis.

**Hon. Laurie Hawn:** Aside from all this, if you were running a business, and you had a key piece of equipment that needed to be replaced, and you are going to look at projecting what it would cost to replace it and so on, and what it would cost to run it, would you be interested in the delta—over operating your current piece of equipment versus the replacement piece of equipment? Because you already have the people there who are operating that old equipment. They can operate the new one, and so on. Would it not make sense to be more interested in the delta? What's already there for the old one is going to be there for the new one. Nothing changes.

**Mr. Kevin Page:** Sir, we were responding to a request that we received to provide an estimate of life-cycle costs, but I would be interested in both. I would be interested in both. As a former fiscal policy officer, I'd be interested in both as well.

**Hon. Laurie Hawn:** Now, in terms of the 20 years, you're saying that DND used 20 years. DND has always used 20 years, in my experience with DND. We certainly used that for the CF-18 when that came out. We've used it I think for every capital air program I'm aware of.

The reason for that is, I suggest, in asking you the question, do we know what it's going to cost to operate the CF-18 for 40 years? I think the answer is no, because we're not there yet. The closer we get, the smarter we get.

So as for projecting ahead to operate the F-35 for 20, 30, or 40 years, do we know what the cost of fuel is going to be in 20 years, 30 years, or 40 years?

**Mr. Kevin Page:** Well, sir, it's a very good question. When you go beyond 20 years, are there additional uncertainties, perhaps? I mean, we don't know what the cost of fuel will be in 20 years, but again, this is sort of standard practice to look at life cycle and to use what we deem to be a reasonable life cycle.

**Hon. Laurie Hawn:** Yes, I understand that, but what I'm getting at is that the reason DND has used 20 years, in my experience, is because.... I mean, even that is an estimate. Someone called it the wag—to a certain extent, the closer you get, the smarter you get.

But I would suggest that it's not hiding anything or anything else. It's just a matter of there's no confidence at all beyond 20 years, and there's a limited amount of confidence even up to 20 years, because of all the unknowables—the cost of fuel, the missions the airplane will do. When we bought the F-18, we didn't know we'd be in Kosovo, Kuwait, or Libya, for example. There are so many unknowables. So I'm suggesting.... I'm not arguing with you on the technical number and so on, but is it a very useful number?

• (0910)

**Mr. Sahir Khan:** Sir, if I just may say, we're principally trying to respond to our report and our methodology. So your point is well taken. There may be other approaches. But we used 30 years for very specific reasons: because it's the estimated service life based on the U.S. Department of Defense and it also happens to correspond to the useful service life of the F-18.

The other issue is that if you take the service life estimated by Lockheed Martin for the aircraft—8,000 hours divided by the average flying hours—it also gives you a number over 30. A lot of the methodology.... To go to Mr. Saxton's very good question, we consulted with a wide range of experts, including the peer reviewers, the Congressional Budget Office, Queen's University, and the Australian Strategic Policy Institute. This was the advice we got about what's conventional.

When we can appeal to an authority like the U.S. Department of Defense Selected Acquisition Report, we use things that are most conventional, so definitions that come out of the cost analysis guidance procedures, which is the basis of our engagement with our consultants. So we tried to stay as close as we could to those

standard practices, in particular since it was U.S. procurement with the U.S. defense department's practices.

**Hon. Laurie Hawn:** Okay.

**The Chair:** Your time has expired, Mr. Hawn. Sorry. Thank you very much.

Madame Blanchette-Lamothe, you have the floor, ma'am.

[*Translation*]

**Ms. Lysane Blanchette-Lamothe (Pierrefonds—Dollard, NDP):** Thank you.

I would like to go back to what Mr. Khan has just said.

If I am not mistaken, you consider that an estimate of costs over 30 years is the closest to the usual practice in this area.

**Mr. Sahir Khan:** Can you repeat the question, please?

**Ms. Lysane Blanchette-Lamothe:** You were just finishing a sentence and we did not have a lot of time left.

Could you tell me if an estimate of costs over 30 years is the closest to the usual practice in this area?

**Mr. Sahir Khan:** For our methodology, we applied the practices for the procurement of military products that are normally used in the United States. Their Department of Defense uses 30 years as its base period. This corresponds to the lifespan of an F-18, according to the manufacturer's estimated lifespan of 8,000 flying hours. This number is then divided by the average number of hours of use per year. So the aircraft's normal and expected lifespan is set at 30 years in the industry, using a number of measures.

**Ms. Lysane Blanchette-Lamothe:** I would like to go back to the partial information you obtained and the information you asked for but did not obtain.

How would having all the information that you asked for have been useful to you? Would it have enabled you to do more meaningful calculations?

**Mr. Sahir Khan:** The request of the Standing Committee on Finance was quite specific. It asked for life cycle costs. It is important because, in the Department of National Defense guide, life cycle costs are defined. Receiving partial information makes things more difficult.

In the course of our analysis, we believed that the information that we and the committee had been given represented all the costs. Later, we discovered, after the auditor general's report appeared, that the costs submitted to Cabinet were not the same. We can now see how those two amounts were arrived at and we can see that they are quite similar, in general terms.

**Ms. Lysane Blanchette-Lamothe:** A little earlier, Mr. Page said that he had asked for information on methodology, but that he had not received it. What would that information have allowed you to do?

**Mr. Sahir Khan:** It would have allowed us to do a better comparison between the two and between the other estimates provided by other international bodies. This study of estimates lacks precision. So complete costs are very important in determining if the costs are really reasonable. In this case, it is essential to know those figures.

By knowing all the costs, we can determine how close our estimate is to the government one provided to Cabinet. In addition, the costs are closer to the estimates from the United States Department of Defense.

**Ms. Lysane Blanchette-Lamothe:** Is there a difference between the operating costs of the CF-18s and those projected for the F-35s?

• (0915)

**Mr. Sahir Khan:** Yes. The Selected Acquisition Report of the United States Department of Defense states that it is quite significant. This is on slide 7 in the deck we provided to committee members. The Department of Defense says that the operating and required personnel costs associated with the F-35s is higher than the costs associated with the aircraft they are replacing. This information is on page 84 of the report that was published four or five weeks ago. The figures provided indicate a cost for an F-35 of \$31,000 per hour compared to \$22,000 per hour for an F-16.

**Ms. Lysane Blanchette-Lamothe:** For people like me who are not terribly familiar with this area, would you say that that cost is considerably different?

**Mr. Sahir Khan:** The difference is significant. The original hypothesis was that this aircraft would cost more or less the same as the aircraft it replaced. The United States Department of Defense has concluded that this aircraft is quite costly in comparison to the aircraft it is replacing. This aircraft has more capabilities, but, in financial terms, it costs \$10,000 more per hour to operate.

**Ms. Lysane Blanchette-Lamothe:** In your opinion, is...  
[English]

**The Chair:** I'm sorry, the time has expired.

Moving on, Mr. Kramp, you now have the floor, sir.

**Mr. Daryl Kramp (Prince Edward—Hastings, CPC):** Thank you, Chair.

I welcome our guests here today. It's really important that you're here to try to provide some clarity, so that we as Parliament and we in government can all live and learn from doing things right. Occasionally, if there's an error in an assessment in a particular region, this gives us the opportunity to correct it.

We're really pleased, of course, as you are so well aware, that this is timely and that we have not gone to the expenditure or the acquisition stage yet, so decisions still will be reached as to whether we should spend money or should not. We're very comfortable with that, and I think this is a beneficial investigation that we're doing here.

It is very well known that we've had significant success in acquiring industrial benefits out of this. I want to put forward a little bit of a balance sheet for it—a balance of estimates versus cost versus income.

Do you agree that we've had some significant industrial benefits?

**Mr. Kevin Page:** Sir, we have certainly read reports that there are benefits with respect to the industrial benefits program. We really saw this as beyond our report, so we haven't commented on it in our report.

**Mr. Daryl Kramp:** Okay, but I think it is important, because it was noted in the Auditor General's report, which of course you'd be oh so familiar with, in which he lauded, of course, the success of the program in acquiring industrial benefits.

Would you agree with the Auditor General's assessment, or do you find some difficulty with it?

**Mr. Kevin Page:** Sir, we don't really have a comment on that. I'm sure that Industry Canada officials are much better placed to comment on that program.

**Mr. Daryl Kramp:** Okay, but my suggestion would be that it's very important to investigate cost—there's no doubt about that—but it's also imperative that we base cost-benefit analysis on this, and that's why I think it would be reasonable to expect your department at some point....

Given the fact that we have the fifth-largest aerospace industry in the world, the third-largest aerospace industry among all of our allies, do you not think it would be reasonable to expect that there might be significant potential long-term benefits to Canada?

**Mr. Kevin Page:** Sir, I think it's reasonable that there could be significant long-term benefits for Canada, but again, it was outside the scope of our report.

**Mr. Daryl Kramp:** Okay. So then you've never had an opportunity to talk to any of our industry partners across the country?

**Mr. Kevin Page:** Actually, sir, we have read reports on what these benefits could be, and at some point—there is some context in the paper we provided—we thought this would eventually be compared with the total life cycle cost estimate. Our job, we thought, was to look at one side of that equation, to look at the life cycle cost-benefits and get good estimates of what these benefits are, then provide an overall comparison to Parliament. But we focused on only one side. If I need to apologize for that, I apologize.

**Mr. Daryl Kramp:** No, there's no apology necessary; we're just trying to get some clarification. In any business, and of course in the business of running the country, there are expenses and there is income. I'm certainly not going to suggest that we extrapolate the success we've had today in the industrial benefits across the entire acquisition and suggest that we're going to make money on it; far from it. But it is my understanding that Parliament has budgeted approximately \$700 million during the developmental stage, they have spent something in the neighbourhood of \$300 million in the developmental stage, and in industrial benefits already we have in excess of \$435 million.

So there have been some tremendous successes, particularly due to the fact that we have a vibrant aerospace industry that quite frankly performs a very significant role in our economy. We're very proud of that, and obviously we don't believe it should be minimized to any particular extent, particularly when we look at an acquisition cost and at our being a participating partner in this entire program, not only as one of the originating partners.

I think you can see where I'm going on this. When the U.S. Air Force alone is going to build 2,400 of these just for their use alone, there can be some significant benefits down the road to Canada.



So I understand that cost is very important, but I would suggest very strongly, sir, that I think.... I'm not going to suggest that you do another study now, but what I am suggesting is that we could certainly be mindful of this story. I think this is a story that Canadians should hear. At that point.... I'm hopeful that at some point, you or your department or officials will start to ascertain the regional benefits from this from across the country.

I know we can ask industry for that, and they'll give us that information, but for security purposes, right now a lot of these companies cannot even be identified; I think we can all understand that. But you have the privilege, sir, and the means with which to do some preliminary investigation, because of your security clearance. Have you done that?

• (0920)

**Mr. Kevin Page:** Sir, no, and it was never our intention to minimize this. I thought we were quite clear in the report we released in 2010 that we saw this as beyond the scope of our paper, but we did highlight it as being very important.

**Mr. Daryl Kramp:** Okay. Thank you very much.

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

Next is Mr. McKay. You now have the floor, sir.

**Hon. John McKay (Scarborough—Guildwood, Lib.):** Thank you, Chair.

Thank you, Mr. Page and your colleagues, for trying to bring some reconciliation to the numbers.

I think at this point DND, AG, and PBO essentially agree on the core numbers. The real issue has been whether the \$10 billion gap has been communicated to Canadians, and for whatever reason the government chose not to do so.

Moving beyond that point to trying to stay all on the same page, I think you make a very valid point when you say that the handbook is the Canadian handbook, the U.S. handbook, the Queen's handbook, the Pentagon's handbook, and the intellectual framework for cost analysis is what is agreed by all parties: there can't be much variation going forward.

The question then becomes, as we are price takers and not price makers for this particular asset, how you reconcile Mr. Fonberg's numbers earlier this week, in which he said that he thought the plane was going to be about \$75 million to \$85 million—and I think he's using the \$85 million number—when in fact the selected acquisition report of December 31, 2011, says it's going to be \$137 million. That's \$85 million versus \$137 million. Even given that we're getting the cheaper version, if you will, how do we reconcile those two numbers?

The second issue was raised earlier. It has to do with the costs of flying this asset, which seem to be significantly higher than for the F-18s. The F-18s, I understand, cost somewhere in the range of \$18,000 to \$20,000 an hour, whereas this one costs \$32,000 an hour. Are we in a situation wherein you can buy it but you can't fly it? The government seems stuck on this notion that the only amount they're going to spend is \$9 billion.

I'd appreciate some reconciliation of how we get from \$85 million to \$120 million to \$137 million, and how we reconcile using legacy costs for projected future costs.

**Mr. Kevin Page:** Thank you, sir.

I think with respect to the cost of acquisition, this is a complicated area where there are many different definitions. I think that in some cases this is just a question of comparing apples and oranges, unfortunately.

Again, the numbers we've seen from DND represent what we see as something called unit fly-away cost, which is usually the lowest number generally provided with this plane. I think those are the numbers in the range of \$70 million to low-\$80 million coming out of the selected acquisition reports.

The number you also referred to, in the range of \$138 million a plane, is something called the average procurement unit cost. It includes different elements of costs. It's a more fulsome kind of cost. I was thinking about this. If I say to my wife that I want to buy a brand-new BMW motorcycle, and the price at the top of the sheet is \$15,000, but when I walk away it's going to cost \$20,000, but I only tell her it's \$15,000, it's a bit of a problem.

So it is important, I think, going forward, which I think is the spirit of your questions, that we come to a common definition. If the average procurement unit cost seems to be the common definition used for a procurement basis in the United States, and we can get comfortable with that, I think, for the secretary going forward, we would all benefit. But to start, it's an apples and oranges question.

On your other point, about the cost of flying and the different costs, certainly coming out of the latest SAR, with respect to the F-35 having a higher operating and support cost per hour, I think this highlights the importance, in a full life-cycle model, of including the full operating and support costs. But certainly the models, which are parametric models, used by the project office to provide these estimates suggest higher costs for the F-35 on an operating and support basis.

Perhaps Mr. Khan could just add quickly to that.

• (0925)

**Mr. Sahir Khan:** Let me just add, and Mr. Hawn has said this in the past, that if you actually take the total acquisition pie and divide it by 65, you are actually looking at \$138 million allocated per aircraft. If you keep quoting the \$75 million, which is a fly-away cost, it risks understating. There's actually a really good paper from the Pentagon's acquisition unit covering why it's important to use the more fulsome cost number.

When you compare that to the latest selected acquisition report, you get a figure of \$137 for all variants. So you want to do a little bit of discounting—some experts suggest 10% or 12%—to get to the A variant.

Again, as you note, on page 84 of the selected acquisition report, over the long term, there is a delta, based on current estimates, between the F-35 and the legacy aircraft it replaces. This is the issue that will have to be considered from a fiscal point of view.

**Hon. John McKay:** So when Mr. Fonberg—

**The Chair:** I'm sorry, Mr. McKay, your time has expired.

**Hon. John McKay:** Time goes so quickly.

**The Chair:** It just races by when you're having that much fun.

Mr. Aspin, you have the floor.

**Mr. Jay Aspin (Nipissing—Timiskaming, CPC):** Thank you, Chair.

I'm going to share my time with Ms. Bateman, but before I do, I have a couple of quick questions.

Welcome, gentlemen.

Mr. Page, you indicated that your model was based on \$148 million per plane, and you used one model. Is that correct?

**Mr. Kevin Page:** That's correct. We provided an estimate of what we think would be kind of an average estimate over the delivery period. We also provided a total program cost estimate. We had \$148 million as the average sustainment cost, and we had a total program cost of \$128 million per plane.

**Mr. Jay Aspin:** Thank you.

Why would you arbitrarily use conventional cost models, given that this project isn't unique in terms of its international appeal and in terms of there being eight to ten partners involved?

**Mr. Sahir Khan:** We spent a lot of time with people who worked with the F-22 Raptor—retired Pentagon officials, the GAO, the Rand Corporation—a lot of people who have a great deal of expertise over generations of fighter aircraft. In particular, one of the reasons we collaborated with the firm in the U.K. is that they actually provide similar advice to the U.K. National Audit Office and the U.K. Ministry of Defence, and they do this on a lot of fighter jet programs. What is interesting, actually, is that there is quite a bit of commonality associated with the program.

**Mr. Jay Aspin:** You do agree that it was conventional modelling you used, even though this project is unique.

**Mr. Sahir Khan:** Actually, sir, a lot of the advice we got was in terms of the patterns, as Mr. Page said earlier, that were emerging in terms of development. There was a lot of expert advice that said that in fact it's not as unique as one might think. We've talked about different generations of aircraft, but in terms of a capabilities increase, there is a long history of aircraft, every generation having new... They're larger, they're heavier, they have more capabilities. But in fact if you look at the time series in our report that was logarithmic, you'll see that the dispersion around the trend lines is actually very tight. It suggests that actually, as you go from generation to generation, these aircraft exhibit commonalities.

**Mr. Jay Aspin:** That's fine. My time is limited and I apologize for interrupting.

The second thing that is curious to me is why you would use U.S. life cycle estimate of 30 years, Mr. Page, when you are a Canadian budget officer. Why would you do that?

• (0930)

**Mr. Kevin Page:** We were purchasing the plane from our American colleagues. I think the Auditor General suggested that perhaps even a better estimate would be 36 years. We thought 30 was appropriate. It's what other people were using.

**Mr. Jay Aspin:** Why would you use one model and not a number of models? Why would you stick to just one model?

**Mr. Kevin Page:** As I said earlier, we'd prefer it. We would like to use multiple models. We started out looking at two different models.

Almost half of my team is sitting at the front of this table. We think it's important that DND also use multiple models. We use high-level models that test reasonableness and we come up with very similar numbers.

**Mr. Jay Aspin:** Okay, that's fine, Mr. Page; I appreciate—

**Mr. Sahir Khan:** The result's quite important here. At the end of the day, while you have multiple approaches from the SAR, from DND, and from us, the interesting thing is they all end up in a similar result for the life cycle costs pro-rated for a 30-year period. We think this is pretty important.

When you do modelling, you test for reasonableness. We had a peer review panel, including the Congressional Budget Office, look at that—

**Mr. Jay Aspin:** Okay, that's fine. I'd like to transfer my remaining time to Ms. Bateman.

Thank you.

**The Chair:** Ms. Bateman, you now have the floor.

[*Translation*]

**Ms. Joyce Bateman:** Thank you.

I have four quick questions.

[*English*]

**The Chair:** You have one minute.

[*Translation*]

**Ms. Joyce Bateman:** Fine, thank you.

First, thank you for providing this clarification and bringing us these figures. It is really necessary for all committee members.

My question is for Mr. Page.

[*English*]

I heard you in response to Monsieur Ravignat say that with a shorter life cycle you have lower costs. I'm not asking you to respond right now, but I am asking that we as a committee review the context of your comments. Perhaps you would like to clarify or if necessary correct your comments. My understanding is that the longer the life of an asset, the lower the cost.

In preparing your report, you reviewed the MOU that Canada signed as a member country. Can you tell us if Canada is on the hook for increases in development costs?

**Mr. Kevin Page:** No, we excluded all development costs.

**Ms. Joyce Bateman:** No? Okay, we're not on the hook. Under that MOU, do member countries get a lower price for the plane than non-member countries?

**Mr. Kevin Page:** Yes, I think we—

**The Chair:** Mr. Page, please answer briefly. We have run out of time.

**Mr. Kevin Page:** Yes.

**The Chair:** That's as brief as it gets.

Thank you, Madam Bateman.

In rotation now, we'll move over to Mr. Allen.

**Mr. Malcolm Allen (Welland, NDP):** Thank you, Chair.

My thanks to our guests for being here.

Mr. Kahn, you were telling us why we looked at U.S. numbers and why we didn't look at Canadian numbers. Walk us down that path a bit more. Give us a decent overview of how that unfolds, why it's important, and why we end up basically at the same stop at the end of the day.

**Mr. Sahir Khan:** The program has had well-publicized cost overruns and delays. But one of the advantages is that we now have some useful reference points. We've recommended that parliamentarians at least consider that figures coming out of the selected acquisition report, plus reports from the U.S. Government Accountability Office, begin to illuminate the subject—providing estimates on both acquisition costs and O and S, long-term sustainment—in effect, life cycle costs.

There are now good reference points. A year ago when we did our report, there was not an independent estimate that you could pull out for the F-35A or for sustainment, of which operating support is the largest component. A year later now, you're seeing these numbers on a selected acquisition report and through the U.S. Department of Defense's CAPE unit. You're seeing average procurement unit cost numbers that are also important, because this is the basis of budgeting in the United States and appropriations, not recurring fly-away.

You'll see in the selective acquisition report that the same figures used here will be part of the defence department's submission for the budget process.

**Mr. Malcolm Allen:** Since we will buy this plane, if we buy it, from the U.S. government, not actually from Lockheed Martin—that's the way it will be eventually, if we decide to buy this plane—we get the same price they get for that particular model, according to the MOU.

Is it safe to assume that the cost to operate here would be plus or minus 5%, say, of what the costs are to operate in the U.S.?

• (0935)

**Mr. Sahir Khan:** Sir, at this point that would be speculative. I think we can refer you to the fact that they've now done an estimate of the cost difference—their belief in the cost difference—using parametric models to look at the O-and-S cost, operating and support, per flying hour for the F-35. You'll see on page 84 that they actually give you the flying hours for the F-35A versus the other variant. We've provided a kind of illustrative calculation of that, and you can now start to see those indications.

To your first question, it is useful now to start using these reference points to look at what's reasonable. I think it's the same point about parametric modelling and the use of it: what's reasonable.

If points start to converge, then at least, from a parliamentary point of view, there's a richer planning environment. You can have a little more confidence going forward.

We caution that they're all estimates at this point. But to your first question, it becomes interesting when they start to converge. That's why we think the latest report published just five weeks ago from the U.S. Department of Defense is very handy in that regard.

**Mr. Kevin Page:** Sir, if I may add very quickly, just to put in a plug for the Department of National Defence officials, we would say the numbers they presented to cabinet on a full life cycle basis looking at operation and support were quite close to what was provided very recently by the selected acquisition report.

I think that gives the budget office certainly a lot of comfort.

**Mr. Malcolm Allen:** I don't disagree, by the way, that the \$25.1 billion reported to cabinet is what a reasonable—to use your term, Mr. Khan—person doing this would probably come up with. Unfortunately, that's not the number they told the Canadian public. They said it was less than \$15 billion. The reality is that albeit we can give them credit for telling cabinet, we can't give them credit for not telling us and the general public that it was \$10 billion less. That's what they communicated. They didn't really give us what information they knew; they gave us other information.

Mr. Page, I recognize you've done this as a career, I would assume as a cost analyst. In your experience, have you seen these programs ever go down in price?

**Mr. Kevin Page:** No. Actually, sir, that's one of the reasons that when we looked at different models and we looked at the experience of the F-35 when we took on this project, we thought a cost-estimating relation of the kind of project that picks up these escalating costs....

There's a chart we have—I know you can't see it, but it's in our report—that looks at 30 or 40 years' worth of history. When you look at the cost of this type of technology, these sorts of systems, on a per-kilogram basis it's been growing exponentially, certainly 3.5%, or actually in the 4% range when you add in the weight itself. The costs have been going up.

**The Chair:** The time has expired, Mr. Allen. Thank you, sir.

Over to Mr. Dreeshen, who now has the floor.

**Mr. Earl Dreeshen (Red Deer, CPC):** Thank you very much, Mr. Chair.

I'd like to give my time to Mr. Alexander.

**The Chair:** Mr. Alexander, you have the floor, sir.

**Mr. Chris Alexander (Ajax—Pickering, CPC):** Thank you, Chair.

Mr. Page, do you know the low-rate, initial production period, per-aircraft price of the variant of the F-35 that Canada may be acquiring?

**Mr. Sahir Khan:** Which LRIP batch are you referring to, sir?

**Mr. Chris Alexander:** Do you know which model Canada intends to buy?

**Mr. Sahir Khan:** The F-35A, sir. But which LRIP batch are you referring to?

**Mr. Chris Alexander:** It's conventionally known in the trade as the LRIP, the low rate of initial production period per-aircraft cost. Do you know what it is?

**Mr. Kevin Page:** Sir, we would need to be told working assumptions and when we expect the delivery to be.

**Mr. Chris Alexander:** So you don't know what it is.

**Mr. Kevin Page:** Sir, we have used assumptions, which we highlighted in our report. If we were asked to do an additional report, we would need an update on what the expectations—

**Mr. Chris Alexander:** But am I clear in understanding that you don't know what it is?

**Mr. Sahir Khan:** Actually, sir, from LRIP one to five.... First of all, there are two issues here. There are actually published figures and they're contracted. The issue is those are actually a price, not a cost—

**Mr. Chris Alexander:** Excuse me. There is one figure that has been agreed by the joint program office. Do you know what it is?

**Mr. Sahir Khan:** The LRIP 5.... Which LRIP batch?

**Mr. Chris Alexander:** For the low-rate, initial production period, per-aircraft cost.

**Mr. Sahir Khan:** Forgive me. It's just that we're unsure which batch you're referring to, sir.

**Mr. Chris Alexander:** The initial production period batch.

**Mr. Sahir Khan:** Sir, there are multiple batches within the LRIPs. Currently we're at—

• (0940)

**Mr. Chris Alexander:** You give me all the ones you know and we'll see whether you actually know what the LRIP is.

**The Chair:** Order.

**Mr. Sahir Khan:** We have a chart, sir. I just want to know which batch.

**Mr. Chris Alexander:** I have—

**Mr. Peter Weltman (Senior Director, Expenditure and Revenue Analysis, Office of the Parliamentary Budget Officer, Library of Parliament):** May I respond quickly?

**Mr. Chris Alexander:** Please.

**Mr. Peter Weltman:** There are six LRIP batches in the process right now. Two of them have been negotiated, and the other four are under negotiation and they're cost plus. They're in the SAR. We'd probably have to get back to you on the cost. They are available.

**Mr. Chris Alexander:** You'd have to get back to me, all right.

The cost is \$100 million, the LRIP cost. Why was the figure that you've used as a fundamental parameter for your estimate over \$40 million more than this?

**Mr. Sahir Khan:** Sir, actually the LRIPs, for each batch, have a specific price attached to them. There have been cost overruns. In some cases those have been borne by the defence department, and in some cases they've been shared.

**Mr. Chris Alexander:** Could you give me a clear justification for a discrepancy of over \$40 million per unit cost between your assumption and the LRIP, which is well known to all of the partners in this project?

**Mr. Sahir Khan:** Sir, in some cases some of the LRIP batches actually exceed \$200 million per aircraft, so we thought it would be unfair simply to compare the early rate production.

**Mr. Chris Alexander:** Excuse me, Mr. Khan, but I think you will have to agree with me, when you consult your figures, that none of the LRIP batches reach a number anything close to that high. That is for—

**The Chair:** On a point of order, Mr. McKay.

**Hon. John McKay:** If Mr. Alexander is working from some figures, it would probably be helpful if he tabled the figures with the committee so that the PBO can actually respond in a fulsome fashion.

**The Chair:** Thank you. That's not a point of order, Mr. McKay.

I would appreciate it if colleagues would use points of order only when there is really something out of order, as opposed to trying to find an opportunity to make a statement you otherwise couldn't, not that you have done exactly that, but that has happened and I want to stop it right now.

I am also reinstating the time that Mr. Alexander lost due to a point of order that wasn't a point of order.

Mr. Alexander, you have the floor. Please continue.

**Mr. Chris Alexander:** Thank you, Chair. I'm very grateful for that.

My next question is for Mr. Page.

You are the Parliamentary Budget Officer of the Parliament of Canada. You know full well that the Department of National Defence, under Liberal governments and Conservative governments, has, as a standard for aircraft acquisitions, used a 20-year life cycle framework. You chose to use a 30-year timeframe, which has been used by the Department of Defense of the United States. Why?

**Mr. Kevin Page:** Sir, I see actually no logic, as a budget officer, to use 20 years when we know that the real life cycle is going to be probably 30 years, potentially more.

**Mr. Chris Alexander:** Which country is buying the aircraft?

**Mr. Kevin Page:** Sir, Canada is. Even if we look at the CF-18s—and we have a fighter pilot at this table right now—we know that they've been in service for over 40 years, so why would we use a 20-year number?

**Mr. Chris Alexander:** Which department is going to buy this aircraft for Canada?

**Mr. Kevin Page:** Taxpayers are going to buy the—

**Mr. Chris Alexander:** Which department, under our procurement laws, will acquire the aircraft?

**Mr. Kevin Page:** The Department of National Defence, sir.

**Mr. Chris Alexander:** And what is the standard life cycle assumption that National Defence has used for years for aircraft acquisitions?

**Mr. Kevin Page:** Sir, the one that DND uses should be the one that's consistent with Treasury Board policy. It would vary for different types of equipment.

**Mr. Chris Alexander:** So is it a 20-year assumption that they have used in the past? Yes or no?

**Mr. Sahir Khan:** Sir, the idea is, for fiscal—

**Mr. Kevin Page:** They've used it in the past. If they use it, does that make it right?

**Mr. Chris Alexander:** Would it not be reasonable to expect the Parliamentary Budget Officer of the Parliament of Canada to do a budget estimation that reflects life cycles used by departments of the Government of Canada?

**Mr. Kevin Page:** If you want a Parliamentary Budget Officer to provide independent estimates, and we would work with Treasury Board policies that we would hold accountability officers accountable to, the Parliamentary Budget Officer will start with Treasury Board policies.

**Mr. Chris Alexander:** Does independence—

**The Chair:** I'm sorry, Mr. Alexander, your time has expired, sir. Thank you very much.

We have only a couple of minutes, but those minutes belong to Mr. McKay. You have the floor, sir.

**Hon. John McKay:** Thank you, Chair.

Just pursuing this argument a little further, it seems to me that DND is the only outlier here. The U.S. accepts this formula; Canada, through Treasury Board, accepts this formula; the U.K.; Queen's University; pretty well any entity.

Am I correct to assume that the only entity that seems to go for only 20 years is DND, and they seem to be offside with Treasury Board guidelines?

• (0945)

**Mr. Kevin Page:** Sir, we're very comfortable in providing our estimates to you, to all parliamentarians, on a 30-year basis, and we think that's quite consistent with Treasury Board policies and international practices.

**Hon. John McKay:** I'm inclined to agree with you. I think it is. The issue then becomes trying to get DND to be consistent with Treasury Board guidelines and consistent with every other entity's costing process. It seems that even with moving to the acquisition cost, they still don't want to come forward with consistent methodology so that Canadians can compare apples to apples, as opposed to apples to oranges to lemons.

**Mr. Kevin Page:** Sorry, as I alluded to earlier, I think as we move forward, if we could agree on the way parliamentarians will be presented cost of acquisition—here's the way they will be presented operation and support cost, on a total life cycle cost basis; here's our reasonable estimate for life cycle based on other international practices other people are using—I think the go-forward process will be much enhanced.

**Hon. John McKay:** A final point—

**The Chair:** Mr. McKay, your time still remains, but the meeting doesn't. It is now one hour after we started, so I must bring this to a conclusion.

Mr. Page and your colleagues, thank you all very much for your participation today.

We will suspend for three minutes while we exchange witnesses. Please, everyone, be ready to go in three minutes. We now stand adjourned for those three minutes.

• (0945)

\_\_\_\_\_ (Pause) \_\_\_\_\_

• (0950)

**The Chair:** I now declare the 42nd meeting of the Standing Committee on Public Accounts back in order for the second hour of our meeting.

I will welcome our deputies and staff here from our previous meeting. I know they've just been waiting and waiting to come back and continue the exciting discussions we've been having. Thank you all very much. We do appreciate it.

I believe every single person returned. I'm not sure whether that says a lot about how good you're doing or how ineffective some people here are, in leaving you still being able to walk. However, you're all here and we do appreciate it.

Colleagues, if you are ready, we will begin. As I mentioned at the beginning, we will do a fresh rotation and start from the beginning and again we will continue until such time as our committee time expires.

With that, unless there are any interventions from colleagues—I see none—we will then proceed with Mr. Saxton.

Mr. Saxton, you will kick off the rotation. You now have the floor, sir.

**Mr. Andrew Saxton:** Thank you, Mr. Chair.

My first question is for the Treasury Board secretary.

In his remarks to our committee just before you arrived, the Parliamentary Budget Officer stated that he followed Treasury Board guidelines when he decided to choose a 30-year life cycle, and he implied that DND may not have followed Treasury Board guidelines when they chose a 20-year life cycle.

Could you please clarify what the Treasury Board guidelines are for the life cycle?

**Ms. Michelle d'Auray (Secretary of the Treasury Board of Canada, Treasury Board Secretariat):** Thank you, Mr. Chair.

The Treasury Board guidelines are applied in different circumstances. When you are providing information for approval for a project, the life cycle refers to the life cycle cost of the materiel or the asset to be acquired. In the context of an aircraft or air weapons system or the air materiel that the Department of National Defence has procured even in the very recent years, the Treasury Board submission has always looked at a 20-year life cycle costing, especially with regard to maintenance, because beyond a 20-year timeframe, as I indicated in my previous testimony, it becomes very difficult. We consider it high risk to go beyond that timeframe for the purposes of costing for an acquisition.

● (0955)

**Mr. Andrew Saxton:** Thank you very much, Madam Secretary.

My next question is for the Department of National Defence. Can you describe what the 2006 memorandum of understanding has meant for Canada's involvement in this program?

**Mr. Robert Fonberg (Deputy Minister, Department of National Defence):** Thank you.

Mr. Chairman, I would ask Dan Ross, ADM Materiel, to speak to that question, as he has been intimately involved in the MOU.

**Mr. Dan Ross (Assistant Deputy Minister, Materiel, Department of National Defence):** Thank you.

The MOU was key to provide the opportunity for Canada to continue to have access to critical and detailed and highly classified information on the joint strike fighter program. We had verified prior to renewing that MOU that the F-35 remained a valid option going forward, even though there was no SOR and the air force had not stated any detailed requirement at that time. So that's one aspect.

The other aspect was that it kept the door open for Canadian industry to have opportunities in both design and early production industrial opportunities, contract opportunities.

Thank you, sir.

**Mr. Andrew Saxton:** Thank you.

My next question is for the Department of Public Works. Can you explain how the new secretariat will increase the communication between the Department of Public Works and the Department of National Defence?

**Mr. François Guimont (Deputy Minister, Deputy Receiver General for Canada, Department of Public Works and Government Services):** Thank you for the question.

Mr. Chairman, the OAG noted that the file up to this point had characteristics of a department working in a silo. So the first point I would make is that the secretariat would adhere to the structure that I described earlier and will bring people together. That's the first observation I would make.

Second, we will focus on the seven-point action plan. That is the mandate given to us by the government, quite clearly.

Third, we will draw from the experience we have gained through the national shipbuilding strategy. Interestingly enough, pretty much all the people around this table were involved in the national shipbuilding strategy, so I think we have a very good footing to

cooperatively work together in coordinating, providing oversight, and working on a consensus basis.

**Mr. Andrew Saxton:** Thank you.

My next question is for the Department of National Defence. The Parliamentary Budget Officer debated whether this process was unique. Would you clarify how this is different from previous processes in the past?

**Mr. Robert Fonberg:** Just to clarify, is that in terms of actually acquiring, being in part of the development process, and then leading ultimately to the acquisition?

**Mr. Andrew Saxton:** Yes.

**Mr. Robert Fonberg:** Perhaps Dan Ross could answer that question.

**Mr. Dan Ross:** Thanks for the question.

The vast majority of our acquisitions, because of cost, have been military, off-the-shelf, proven solutions that are already in existence and normally in service with another nation. That reduces our risks enormously. Costs are very specific, and there's proven in-service support performance there.

So this approach is very much different from that. In 1997 this was a blank sheet of paper. There was nothing. Four years later, Lockheed Martin, in competition with Boeing, demonstrated a prototype that took off in 500 feet, flew supersonic, and landed vertically. That was in 2011. We had joined that, for a \$10 million contribution, in 1997, and then continued to monitor that over the past 15 years. That was obviously very early in any process of considering replacements for a CF-18, but the other alternatives out there, Eurofighters or Super Hornets, were also, even at that time, ten-year-old technology.

So the program is truly unique. Today there are 1,700 people in a joint project office supported by thousands in industry, supported by the nine partner countries. The aircraft is in production. There are large numbers flying, or about to be added to the fleet. Most of the technology issues are behind us. Costs for acquisition are stabilizing. We're gaining more and more specific insight into what it will cost to run the aircraft.

Thank you, sir.

● (1000)

**The Chair:** Time has well expired. Thank you.

Moving on, Mr. Allen, you now have the floor, sir.

**Mr. Malcolm Allen:** Thank you, Chair.

It's nice to see you back, gentlemen and madam.

Mr. Fonberg, a document—actually, it was a Treasury Board Secretariat report—went to Parliament last year that talked about the F-35 and the \$25 billion as being in “definitions” phase. So looking at the chart, on pages 12 and 13 of the AG's report in chapter 2, I noticed that just this year, that actual wording got changed to “options analysis”.

When I look at the chart, sir, under 2006, it says that “National Defence completed a preliminary options analysis of five...aircraft”. It goes through a series of steps, and then, when it comes to 2010, “National Defence provided letter to PWGSC to justify procuring F-35 without competition”.

Can you explain to me, sir, how “definitions” phase became “options analysis” phase eight months after it was reported to Parliament, when indeed you had decided to buy an F-35, or at least that was the letter you sent to Public Works?

**Mr. Robert Fonberg:** Thank you for the question.

If I may, on the specific question, which I believe is related to the report on plans and priorities from last year, on April 13 of this year my office was informed that there was an error in the supplementary tables on major capital projects in the 2011-12 report on plans and priorities.

Specifically, the RPP indicated that the next-generation fighter capability project status was in the definition phase. That was incorrect, and we apologize for that. In 2011-12 the project was in the options and analysis phase.

I could ask the CFO to speak to what that means. I would—

**Mr. Malcolm Allen:** Fair enough; that works for me, that explanation, in the sense of.... You believed you were at the options analysis phase last year, and yet I believe that just on Tuesday the report back here was that we had gone back to that phase. I believe my friend Mr. Alexander, as the parliamentary secretary, is on the public record as saying we're going back to the options analysis phase, which implies that we were further along. But I'll take your explanation at face value.

At this point, I'd like to turn to Lieutenant-General Deschamps. Sir, do you have a sense of...? The \$19,000 per flying hour for the CF-18—is that close? Is that a close number?

**Lieutenant-General André Deschamps (Commander, Royal Canadian Air Force, Department of National Defence):** Thank you for that question.

I don't manage those costs with regard to operating per hour. My colleague to the left actually manages those issues, so I will defer to him.

**Mr. Malcolm Allen:** Thank you.

**Mr. Dan Ross:** Thank you.

I manage the contracted support for the CF-18 fleet, so all the spare parts and repair and overhaul annually.

**Mr. Malcolm Allen:** I'm looking for numbers here.

**Mr. Dan Ross:** Annually, we have spent, over the last ten years, \$200 million per year. Now, that is not the total operating cost of the CF-18. That is the portion that I manage.

**Mr. Malcolm Allen:** When I use the number \$19,000, you're not able to tell me. Could you provide that to the committee, please, flying hour costs? Could you table that with the committee?

**Mr. Dan Ross:** Sir, yes, we could calculate that for you and get back to the committee.

**Mr. Malcolm Allen:** So when the U.S. says that the hourly cost to fly the F-35A is \$31,000 and change—we can round that up or down—does that number ring to you at all as close to the CF-18 cost? Or is that more than the CF-18 cost at present?

**Mr. Dan Ross:** We've always expected that the F-35, due to its complexity, would cost more. And as I testified here last year, knowing that we'd spent about \$200 million annually for the F-18, I'd estimated \$250 million to \$300 million in my last testimony. So we expect that it will cost more.

**Mr. Malcolm Allen:** Thank you. What I'm hearing from you is that it's going to cost more to fly the F-35 versus the CF-18. Yet we made an operating cost estimate. Mr. Fonberg has repeatedly said here, including the minister, that the sunk costs are the same as the CF-18 for the F-35. You, sir, have just told me they're more.

Mr. Fonberg, square the circle for me. How did it get to be more by Mr. Ross and the same by you?

**Mr. Robert Fonberg:** I think Mr. Ross will answer that question, Mr. Chair.

**Mr. Dan Ross:** Thanks, sir.

**Mr. Malcolm Allen:** Mr. Fonberg, I'm looking for a response from you, sir. You're the deputy minister.

**Mr. Robert Fonberg:** Mr. Chairman, ADM Materiel Dan Ross actually has the technical details on that—

**Mr. Malcolm Allen:** I'm not looking for technical details.

**The Chair:** That's a fair deferral.

● (1005)

**Mr. Malcolm Allen:** I understand, Chair. I'm not going to pursue it any longer. I simply asked to explain how we got more or less. Mr. Fonberg actually said it was the same. Mr. Ross says that the F-35 is actually going to cost more to fly than the CF-18. I accept them at that, so we'll move along.

Mr. Fonberg, you said in testimony on Tuesday that the PBO didn't use operating costs when they came up with these numbers. The PBO was here today, Kevin Page. He said he absolutely did use operating costs. We may not agree on this number, and that's okay, but do you now agree that the PBO did actually use operating costs to come up with the number?

**Mr. Robert Fonberg:** Thank you for the question.

Mr. Chairman, I may actually ask Dan Ross to speak again to some of the correspondence recently and over time with the PBO. What we asked for clarification on, about two weeks ago, was for the schedule of operating costs that we used to build our operating cost numbers. Mr. Ross can walk through that: personnel salaries and allowances, fuel and lubricants, base support services, and on and on.

We are unable to identify any of that in his report. We have asked him for clarification and we have received no firm clarification whatsoever that any of those items are included, other than a statement by him that they are included.

Dan, would you like to...?

**The Chair:** I'm sorry, Mr. Fonberg; we're a minute over now. I just do not have the time. Mr. Allen's colleagues are quite welcome to pick up from that if they wish, but we do have to call the time now.

I will now move over in rotation to Mr. Kramp. You have the floor, sir.

**Mr. Daryl Kramp:** Thank you, Mr. Chair.

Welcome to our guests again.

I have a quick question to Mr. Fonberg and then I'll be going to Mr. Kennedy.

Mr. Fonberg, there was a statement made today by the PBO that quite frankly is a little bit alarming. I would like some confirmation one way or the other and/or some explanation for that statement. The PBO claimed that you did not fully respond to his requests. Is that true? And would you care to respond to that in some particular manner?

**Mr. Robert Fonberg:** To the best of my knowledge, we fully responded to the PBO's request, Mr. Chairman. I have the timelines of all the correspondence back and forth, starting in November 17, 2010, and ending with his report on March 10, 2011. I don't believe that he raised issues with us on the substantive response, including the latest one of March 3. I'm not sure what conclusion he was drawing, Mr. Chairman.

**Mr. Daryl Kramp:** Okay, thank you very much.

Mr. Kennedy, you alluded to some of the industrial benefits going forward, and I think it is important. There's no doubt that the major focus of this committee hearing and our examination of the issue from both the Auditor General and the PBO has obviously to ascertain, as close as possible, given the nature of this acquisition, the expenses, the cost of this aircraft, the cost of operation acquisition, development, etc. I also know, from being a person in business for many years, that your expenses are of course crucial. You have to control them. You have to know what they are. But also, if you have any potential income you have to factor that into it as well. A government has to factor in all of the potential possibilities going forward.

I would like to expand a little bit on the industrial benefits. We have close to a hundred companies, I'm led to believe, across this country that are regionally spread out and that are participating in that. Can you confirm that?

**Mr. Simon Kennedy (Senior Associate Deputy Minister, Department of Industry):** At the moment, 70 companies have won work on this particular project. I have some information I could share with the committee. They are spread all across the country.

**Mr. Daryl Kramp:** I can understand for reasons of security and particular sensitivities that you're not able to identify those companies, but I do think it is important to recognize that there is a potentially significant level of income with this. Would you accept that fact?

**Mr. Simon Kennedy:** The estimate right now for the potential opportunities for Canadian firms is \$9.85 billion U.S.; that's for the production of the aircraft and does not include sustainment and some of the service. For the actual manufacture, if we have the 3,100 or so

planes that are estimated to be produced, it's just under \$10 billion in terms of opportunities for Canadian companies.

**Mr. Daryl Kramp:** How would you come to that?

As an example, when the PBO took the costing and then extrapolated that over the next 20 years, have you done a similar process based on the success to date, the fact that we've spent close to \$300 million in upfront costs and yet we've received \$435 million in contractual guarantees and contractual programs that are a benefit to Canada?

Did you extrapolate from these numbers? How did you come to that figure?

• (1010)

**Mr. Simon Kennedy:** Mr. Chair, I could say two things to that.

The first is if you look at the current contracts for work on production of the JSF, and you assume that the Canadian companies that have won those contracts will continue to be successful and will continue to be part of the supply chain—in other words, they won't lose the work they've already won—if you extrapolate the work they're already doing to the full run of the aircraft production, that amounts to just under \$7.5 billion U.S.

In a sense, of the just under \$10 billion that has been identified as potential opportunities for Canadian companies, if the Canadian firms that have already won work continue to keep that work through the production of the aircraft, that's about 75% of the identified opportunities that would be locked up.

We think that Canadian companies have done very well to date.

Twice a year we get detailed information from the prime contractors on the available opportunities and all the Canadian firms that they feel stand a good chance to participate. We sit down with the prime contractors and we validate all that information. We also have regular meetings with major Canadian suppliers to do some triangulation, in a sense.

We talk to Canadian firms who are vying for business and we can ask them questions about whether or not what we're hearing from the prime contractors matches up.

To date we haven't had any reason to experience concern.

**Mr. Daryl Kramp:** Approximately \$9 billion, give or take a little...

**Mr. Simon Kennedy:** Just under \$10 billion U.S.

**Mr. Daryl Kramp:** Thank you.

On the asset side, coming through with potential contractual opportunities for Canadians, might there be some intangibles too? What about sharing of technology, sharing of research, R and D, investment, other opportunities, collaborations? Is that included in this, or would this be over and above that?

**Mr. Simon Kennedy:** That is one of the significant differences with this approach. We're not using traditional IRBs, industrial and regional benefits, but we're involved in a consortium to develop the technology, because the Canadian firms are in on the ground floor on the development of that technology.



I'll give you one example: a firm here in Ottawa that, as part of the JSF work, has developed a sensor for the engines. They've now been able to turn around that technology and are selling it for civilian use. This has nothing to do with the F-35, but because they are part of the F-35 program, they have been able to develop this technology, which is now going to be sold to Airbus and Bombardier and others on a commercial basis.

The technology being developed is in some cases very advanced technology, and these companies have been able to use that in their other lines of business.

**Mr. Daryl Kramp:** Thank you very kindly.

**The Chair:** We'll now go over to Mr. Ravignat. You have the floor, sir.

[Translation]

**Mr. Mathieu Ravignat:** Thank you, Mr. Chair.

My question is for Ms. d'Auray.

If the CF-18s are operational for 40 years, why do you say that 20 years is a reasonable estimate when it comes to calculating full life cycle costs for the F-35 fighters?

**Ms. Michelle d'Auray:** Thank you, Mr. Chair.

For the purposes of presenting a procurement project to Treasury Board, we use a 20-year cycle to predict costs, especially for maintenance contracts. As I pointed out, it is difficult to calculate maintenance costs for more than 20 years.

So the life cycle of an asset can be calculated for a longer term for planning purposes, but for procurement purposes...

**Mr. Mathieu Ravignat:** Is there a difference between maintenance costs and full life cycle costs of a procurement?

**Ms. Michelle d'Auray:** Full life cycle costs are used at different stages of planning.

**Mr. Mathieu Ravignat:** So you are saying that the 20-year period is for maintenance. It is not necessarily the aircraft's full life cycle. Is that right?

**Ms. Michelle d'Auray:** Mr. Chair, I was asked what Treasury Board uses in making decisions. For acquisition projects, in making decisions, we use the duration. For planning purposes, if a department has to...

**Mr. Mathieu Ravignat:** I understood completely. Thank you for the answer.

Did the Department of National Defence specifically ask you if a 20-year period was reasonable?

**Ms. Michelle d'Auray:** Mr. Chair, we are neither at the acquisition stage nor the project stage. So we have not yet received a submission for this acquisition.

**Mr. Mathieu Ravignat:** So, there were no consultations on the subject between the Department of National Defence and your office.

**Ms. Michelle d'Auray:** The F-35s are not yet at the acquisition stage.

• (1015)

**Mr. Mathieu Ravignat:** I am not going to...

**Ms. Michelle d'Auray:** Can I finish my answer?

**Mr. Mathieu Ravignat:** Yes, but quickly, please.

**Ms. Michelle d'Auray:** Those discussions have not started yet. In the past, for previous submissions, we definitely used the life cycle.

**Mr. Mathieu Ravignat:** Fine.

[English]

My next question is for the lieutenant-general.

Of course, thank you for being here.

The elephant in the room here is that on Tuesday you said that you were still working on the assumption that the F-35 was the plane that we needed. Now, apart from what the Americans need and apart from what Lockheed Martin needs, what domestic defence needs does Canada have in order to prefer the F-35s above all other planes?

**LGen André Deschamps:** Thank you for that question.

To go back to what I said on Tuesday, when we look at the needs of the future we have to look at both domestic and international environments where technology will cause us some significant challenges.

It's important to remember that one of the things we're doing is buying a single fleet of fighters. To have, let's say, a home fleet and an away fleet is very expensive. We went away from that in the 1980s, with the F-18, and to go back that way would be even more expensive. So no matter what we consider as the future option, we have to look at a single fleet, multi-rolled aircraft to meet all of Canada's needs.

**Mr. Mathieu Ravignat:** If you were so sure that the F-35 was the plane, why didn't you go ahead with an open tendering process?

**LGen André Deschamps:** To go back to 2010 and the analysis we did, we looked at our requirements. We looked at the type of technology that would be required for us to be agile enough to deal with future threats. The analysis led us to a set of requirements.

**Mr. Mathieu Ravignat:** Could you be a little bit clearer about what those threats are?

**LGen André Deschamps:** Certainly. In an unclassified way, there are very advanced surface-to-air missile systems currently being fielded by countries. That will proliferate. We see them now proliferating. We expect them to continue proliferating. The technology challenges the airplanes available today. It's very deadly. It's very accurate, and it has very long ranges.

**Mr. Mathieu Ravignat:** In your opinion, there's a clear and present threat to Canadian national security with regard to these missiles.

**LGen André Deschamps:** I don't define national security, sir. What I do, though, is present government with options should it need to exercise those options 30 years from now. I can't predict the future. All I can do is predict where challenges will arise around the world, and at home potentially. Other things that we need to be concerned with—cruise missiles—their technology is proliferating. They were the first automatic UAVs. They were that first generation. UAVs now are very popular. Cruise missiles were that very first version. They only go one way.

The challenge with cruise missile technology is accessible now to many nations, and people are working on building those things to be fired off ships or off airplanes.

**Mr. Mathieu Ravignat:** So—

**The Chair:** Your time has expired. Thank you.

Mr. Hawn, you have the floor, sir.

**Hon. Laurie Hawn:** Thank you very much, Mr. Chair.

Thanks for coming back.

I have a number of questions. First of all, for Madam d'Auray, Treasury Board has guidelines with respect to predictions and so on, is that correct?

**Ms. Michelle d'Auray:** Treasury Board has a number of policies and directives and guidelines. They cover a wide range of activities and initiatives.

**Hon. Laurie Hawn:** Thank you. A guideline is simply that: it's a guideline. It doesn't mean everything is going to be cut that way.

**Ms. Michelle d'Auray:** A guideline is designed to give guidance.

**Hon. Laurie Hawn:** Thank you.

With respect to some costs that were brought up, my understanding of sunk costs is they are things that are there for the F-18 and will be there for the F-35, whether it's pilots, technicians. I guess, Mr. Fonberg, is that what we're defining as sunk costs, or what DND is defining as sunk costs?

**Mr. Robert Fonberg:** Defining as operating costs—yes, sir.

**Hon. Laurie Hawn:** Okay. So it's here for the F-18 today and it will be there for the F-35 tomorrow.

There's obviously a lot of confusion around this. To go back to the operating costs for the F-18 versus the F-35, Mr. Lindsey, I don't know if you have the answer to this or not, but there are two figures for every airplane. There's one that's the sort of hourly operating cost in terms of POL, which is fuel, oil and lubricants, and so on, and then there's what we used to call—I don't know if we still do—the log guide figure, which is a much bigger number and includes salaries and pensions and the whole nine yards. That's the figure I think Mr. Allen was looking for—the log guide figure.

Do you have that off the top of your head for the F-18?

**Mr. Kevin Lindsey (Assistant Deputy Minister, Chief Financial Officer, Finance and Corporate Services, Department of National Defence):** No, sir, I don't have that figure for the F-18. What I could affirm, though, is that the combination of those cost factors you've just identified are those costs that form the costs in this \$10 billion in operating costs.

•(1020)

**Hon. Laurie Hawn:** A big chunk of that is sunk costs, which we just described.

**Mr. Kevin Lindsey:** Sir, I wouldn't characterize them as sunk costs. I would categorize them as ongoing operating costs—a cost of operating a fighter fleet.

**Hon. Laurie Hawn:** Right, which some people have termed sunk costs; but yes, yours is much more correct.

With respect to the F-35 program being a development program, going back to the F-18, there were far fewer F-18s flying at the time when we made the decision to buy that airplane than there are F-35s flying now. So I would suggest, maybe to Mr. Ross, that, yes, it's a development program, but we've been there with development programs before, which turned out just fine, thank you, meaning the F-18. Is that a fair statement?

**Mr. Dan Ross:** Yes, it is.

**Hon. Laurie Hawn:** Now, with respect to going back 20 years and so on, the reason we don't use more than 20 years is because it's so unpredictable. There are so many unknowables out there that it really becomes a meaningless number. But I'm not sure who I'd ask about this....

I'll ask Mr. Fonberg. You can pass it on.

You can take that number and extrapolate it to anything you want. You can extrapolate it to 30 years, 40 years, or 50 years, but for sound planning, you have to go with something that at least has some predictability to it. Is that a fair statement?

**Mr. Robert Fonberg:** Yes, absolutely.

**Hon. Laurie Hawn:** Okay.

Mr. Kennedy, we talked about industrial benefits and so on, and technology. Is it fair to say that if we don't participate in the level of technology that is available to us through the F-35, and in all the things that go into that airplane in supporting it, we will not be in a position to be a part of whatever the next level of technology is? Is that a fair statement?

**Mr. Simon Kennedy:** I think what I would say is that we certainly see, from an Industry Canada perspective, certain advantages to being part of this consortium because of the access to the very advanced technologies and the ability to develop them that it provides, which you wouldn't have with another process.

**Hon. Laurie Hawn:** With respect to suggestions we've just had that if we think the F-35 is the airplane, why don't we just do an open competition if we're so sure, one of the things we would lose by doing that and getting out of the memorandum of understanding is access to that technology.

**Mr. Simon Kennedy:** I think that's well understood: that the purchase of the aircraft has being part of that consortium as part of the arrangement.

**Hon. Laurie Hawn:** On the purchase price within the MOU, Mr. Fonberg, we may not be able to get a definitive number, but can you give a ballpark number as to how much less we will pay within the MOU, as opposed to buying it in foreign military sales directly from the U.S. government?

**Mr. Robert Fonberg:** Thank you for the question.

I believe Dan Ross would have the nature of the premium we would pay through a foreign military sales purchase.

**Mr. Dan Ross:** Thank you, sir.

Our understanding is about \$800 million for foreign military fees and other things. You'd also forgo the royalties that come to Canada when the U.S. government sells planes through FMS to other non-partner countries.

**Hon. Laurie Hawn:** So with Israel and Japan buying airplanes, or planning to buy airplanes, we will get money from the U.S. government when Israel and Japan buy their F-35s.

**Mr. Dan Ross:** Yes, sir. We receive royalties on those sales.

**Hon. Laurie Hawn:** Perfect.

**The Chair:** Thank you.

Moving on, the floor is now Mr. McKay's. As the substituted member of the committee, he is deferring his time to Mr. Rae.

Mr. Rae, sir, you now have the floor.

**Hon. Bob Rae (Toronto Centre, Lib.):** Thank you.

Mr. Fonberg, I'd like to ask you to look at the chart on page 27 of the Auditor General's report.

In that chart, that's the sort of I suppose now famous discrepancy between the number that the Auditor General says was your estimate used for decision-making in June of 2010, and the public response that the department gave to the Parliamentary Budget Officer's report in March of 2011, which I gather was on the DND website in 2011. Is that correct?

**Mr. Robert Fonberg:** I believe that's correct.

**Hon. Bob Rae:** Well, in his testimony this morning.... If you multiply 65 by \$85 million, you don't get \$9 billion, you get under \$6 billion. And that's the number that's also on that chart, the 5,580 number. And as my friend Mr. Hawn points out, if you divide \$9 billion by 65, you get \$138 million. So when the Parliamentary Budget Officer came up with his higher number, Minister MacKay said in the House on March 23 that his methodologies were flawed, his findings were flawed, his numbers were completely out of line and they bore no relationship to the numbers of DND. But in fact, with great respect, Mr. Fonberg, they do bear considerable relationship to the numbers you set out, with respect to the total 20-year costs, when the government made its decision in June of 2010.

My question is, why would you not have admitted to that number? Why would the government not have admitted to that number when it was engaging in the debate with the Parliamentary Budget Officer? Rather than attacking the Parliamentary Budget Officer, why would the department not have said, "Well, there are different ways of calculating this actual cost, but yes, it could be somewhere in the \$25 billion to \$35 billion range, if you include the full life cycle costs over a period of time". And then if you add the period of time, you might get a different number.

But let's not get away from the fact that when Parliament was in the middle of a critical debate, the Department of National Defence seriously undercut the credibility of the Parliamentary Budget Officer, when for many outside observers you'd say the discrepancies are not in fact that huge. What's huge is the fact that \$10 billion went missing when the debate with the Parliamentary Budget Officer started. Who made that decision?

•(1025)

**Mr. Robert Fonberg:** Mr. Chairman, if I could ask for the question....

There were many numbers the member referred to. I'm not sure what clarification he wants on which particular number. If it's the \$6

billion, which is the \$75 million times the 65 aircraft at the time, or the discrepancy between the \$6 billion and the \$9 billion and how the PBO dealt with that, we can talk about that. If it is the issue of operating costs and the discrepancy between \$14.7 billion and \$24.7 billion, we can talk to that too. I'm just not sure which clarification—

**The Chair:** You've got a minute and a half.

**Hon. Bob Rae:** I think it's pretty clear.

Let me ask you very directly, because I don't think it's an obscure question. How do you account for the difference between the number given to the cabinet and to the government in June of 2010, according to the Auditor General of Canada, and the number given by the department and by the minister in the debate surrounding the report of the Parliamentary Budget Officer? Why were those two numbers so different? Why was there a \$10 billion gap in that discussion? That's the question. And who authorized the different accounts?

**Mr. Robert Fonberg:** Sorry, Mr. Chairman, just to clarify, there were no different accounts.

As I said on Tuesday, our last four major asset acquisitions have spoken to sustainment costs and acquisition costs, which is exactly what we did in the case of the F-35 and how we responded. Operating costs are within our departmental budget.

In fact, if you go back and look at the press releases for the last four major asset acquisitions, they all refer to sustainment costs and acquisition costs. So we communicated exactly the same way we've communicated over the last four major asset acquisitions.

**Hon. Bob Rae:** Well, with great respect, sir, you did not, because the number you gave to cabinet and the number given to the government included the operating costs as well as the personnel costs—that was the \$25 billion number. That was also the basis for the number of the Parliamentary Budget Officer. But instead of admitting that, what happened was the government attacked the Parliamentary Budget Officer, saying that his numbers were out by a factor of 100%, when in fact there was a relatively minor difference of opinion between the internal numbers that the department had and the numbers that the Parliamentary Budget Officer proposed.

Why was the number on the website so different from the internal numbers that the government in fact had and that were the basis of the cabinet decision?

**Mr. Robert Fonberg:** Thank you.

I may ask the CFO speak to it, but I would say this. Our understanding at the time, and frankly it continues to be so, notwithstanding the comments of the PBO, is that operating costs were not included. We can find no evidence of operating costs. We asked them to clarify that issue two weeks ago—

**Hon. Bob Rae:** That's completely contrary—

**The Chair:** Sorry, Mr. Rae.

**Hon. Bob Rae:** That's completely contrary to what he said today.

**The Chair:** Mr. Rae, please.

Thank you.

Over now to Mr. Aspin. You have the floor, sir.

**Mr. Jay Aspin:** Thank you, Chairman.

And welcome, everybody.

Much has been made of the sole-source argument. Before you leave, gentlemen and lady, I'd like you to explain the process that led to the sole-source decision—I know it has a history of several governments, at least two—and how it played out here.

Mr. Guimont, can you address that for me, please?

• (1030)

**Mr. François Guimont:** Yes. I'll say a few words and then I'll turn to Mr. Ring, who actually administers the acquisition program.

The only point I would make is that sole source is a legitimate procurement strategy under certain conditions.

Mr. Ring will explain the general approach to sole-sourcing, and specifically in this case how it applies.

**Mr. Tom Ring (Assistant Deputy Minister, Acquisitions Branch, Department of Public Works and Government Services):** Thank you very much for the question.

I will at some point turn to my colleague Mr. Ross, because he and I have worked together on this operation for some time and we share both elements of the decision-making process, if you will.

If you look at a government considering an acquisition, in the first instance one of the things we'll do is look at what is either the capability that you're trying to replace or new capability that you would look to acquire. We would then together look at what was the policy rationale for either buying a new capability or replacing an existing capability. I don't think there's been any debate on that particular issue with respect to the need to replace the CF-18 fleet.

We then go to a third phase of the procurement process. The Auditor General in some of his work has actually laid out quite extensively what the phases in the procurement process and the phases in the acquisition process are.

The next phase of the process is needs and options identification, and there are four or five different steps in that process that we went through. We worked collectively with our colleagues in the Department of National Defence.

Here I would ask Mr. Ross to speak to some of the preliminary work that was done in those phases that eventually gets you to a point where you ask if there is a competitive field that is available to you, and should you then seek a competitive procurement, as the Treasury Board guidelines suggest you should do, if one exists?

Dan, do you want to talk about the options there?

**Mr. Dan Ross:** Thank you.

Effectively, in that early options analysis piece, before you go to government for approval in principle to begin a project, we ask, in this case the air force, to identify their high-level mandatory requirements, what they really need that particular platform to be able to do. We take that and we look out at the market, with our colleagues in Public Works, and identify reasonable solutions, and have preliminary estimates of cost, performance, availability, etc.

In this case, that examination came back with a view that in terms of technology, looking forward 30 years, there was only one solution.

**Mr. Jay Aspin:** When did this whole process start, under which government?

**Mr. Tom Ring:** The joint strike fighter project started with the signing of the first MOU in 1997.

**Mr. Jay Aspin:** Under which government?

**Mr. Tom Ring:** A previous government.

**Mr. Jay Aspin:** Okay.

The other question I had was with regard to the secretariat that you pointed out, and the seven-point plan. Can you identify to me how this will help, in terms of communication between Public Works and National Defence, Mr. Guimont, please?

**Mr. François Guimont:** Thank you for the question.

As I mentioned earlier, the secretariat at the working level will draw from the various departments, so they will be co-located. It's quite obvious to me that if people are together, instead of being separated in their respective departments, they're going to be working as a team. That's the first thing.

The second thing is Mr. Ring will be chairing and will be responsible for the assistant deputy ministers' committee, which will then report to the DMs' committee. In all cases, we are going to work together. I'll be calling regular meetings of the deputy ministers' coordinating committee. The frequency of those meetings is a function of decisions to be made. I've made reference to consensus decision-making, like we did for shipbuilding, and these meetings will draw, in terms of frequency and content, on the work done by the assistant deputy ministers' coordinating committee as well.

So the key characteristic is people working together and the use of third parties to validate, when need be and as required. There will be a clear effort to work on transparency, as we did for shipbuilding. And the terms of reference, which we are finalizing, will essentially expand on the seven-point action plan and show how we are going to operationalize the various elements that have been outlined by the government's seven-point action plan.

• (1035)

**The Chair:** All right. Time has expired, Mr. Aspin.

We will go over to Mr. Allen, who now has the floor.

**Mr. Malcolm Allen:** Thank you, Chair.

I will be sharing some of my time with my colleague Ms. Duncan, provided the committee agrees, of course. Thank you.

Mr. Kennedy, earlier in response to a question you said—I don't have the exact quote clearly, so I'm paraphrasing here—that when you signed the MOU in 2006, which is the industrial piece, your expectation was that we were actually going to sign on to buy an F-35. Is that a fair characterization of what you said?

**Mr. Simon Kennedy:** I think what I was saying was that it's well understood that access to the industrial participation for Canadian companies is contingent upon participation in the process. So that's what I meant to say. If it was unclear, I do apologize.

**Mr. Malcolm Allen:** So you didn't have an expectation or you weren't led to believe we were going to buy the F-35 by any of the other departments or deputy ministers or anyone else in that end of the business?

**Mr. Simon Kennedy:** Our interest is primarily in the industrial opportunities for Canadian companies, and it has been well understood by the—

**Mr. Malcolm Allen:** Thank you, Mr. Kennedy. Thank you. I appreciate that.

Mr. Fonberg, we talked Tuesday, you and I, about \$25 billion and \$14.7 billion, etc. We do know that the Minister of National Defence, Minister MacKay, used the number of \$15 billion. I'm not going to argue when and where and under what circumstances.

Did you give him that number, sir?

**Mr. Robert Fonberg:** We would have given the Minister of National Defence and cabinet three numbers, \$5.7 billion for sustainment, \$9 billion for acquisition, \$10 billion for operating. So 5.7 plus 9 is close to the 15 that I believe the member is referring to, Mr. Chair.

**Mr. Malcolm Allen:** So you gave him three numbers and you didn't make a recommendation. You allowed the minister to juggle them any which way he chose?

**Mr. Robert Fonberg:** I think it's fair to say that based on how we communicated all of these things going back eight years, we communicated exactly the same way, with acquisition costs and 20 years' worth of sustainment costs.

**Mr. Malcolm Allen:** So you would have told him that \$25 billion was acquisition sustainment or operating life cycle, whatever terminology you were using. You would have told him that was that number and you would have said the \$15 billion was simply acquisition and sustainment. Is that what you're telling me?

**Mr. Robert Fonberg:** The decision-making process and the documents that were involved included the full 20-year life cycle costs, which included acquisition, sustainment for 20 years, and operating for 20 years.

As we have done in the past, and if I could, I would just read an excerpt from one of our—

**Mr. Malcolm Allen:** No, that's okay, I don't think you need to. Thank you, Mr. Fonberg. You can just reference it for us. We'll go to it.

Lieutenant-Colonel Deschamps, when it comes to our other NATO partners, primarily Britain and France, are they buying the F-35?

**LGen André Deschamps:** All I can say is that within the nine-nation partnership right now, the United Kingdom is part of that nine-nation group. France is not. France has not indicated its intent to procure the F-35.

**Mr. Malcolm Allen:** My apologies, sir. Lieutenant-General.

**LGen André Deschamps:** That's okay, sir.

**Mr. Malcolm Allen:** You can tell I was never in the forces, obviously. I didn't get the ranks right.

My apologies to you, sir.

**LGen André Deschamps:** No problem.

**Mr. Malcolm Allen:** I'll try not to make the mistake again.

So you were saying that the U.K. is in, but are they purchasing?

**LGen André Deschamps:** As we've seen reported recently, much like Canada, the United Kingdom will make a decision of acquisition at the appropriate time for their budgets and government.

**Mr. Malcolm Allen:** Fair enough.

I'm sharing a limited amount of time. Let me pass it to Madam Duncan.

**The Chair:** You have over a minute.

**Ms. Linda Duncan (Edmonton—Strathcona, NDP):** Thank you.

My question is to the Deputy Minister of Public Works. My concern is more a broad one rather than the specifics of the matter of the F-35.

The Auditor General was very clear in his determination that Public Works did not demonstrate due diligence in its oversight role in this matter, and the department has challenged that finding, as reported in the Auditor General's report. Do you continue to hold the view that you can rely on such short-circuited procedures as applied here, or would you follow in future, as the Auditor General has recommended, Treasury Board rules and the principles of good management and due diligence?

**Mr. François Guimont:** Thank you for the question.

I explained this Tuesday, when I was before the committee, that when the Auditor General came before the committee he stated, and I quoted him, that some due diligence had been applied by Public Works. I also explained that the reason we had a disagreement had to do with the fact that "did not demonstrate", under recommendation 2.81, is an absolute, and I am comfortable with the fact that he has recognized that some due diligence has been applied. This, to me, was the position that we took with him in the course of the interaction we had with his office.

Now, in all fairness, this is a unique procurement process, no question about that. In retrospect, we collectively—but I'll speak for myself—if we were to look back, a different frame would have been put in place to carry out our responsibilities. And I would—

• (1040)

**Ms. Linda Duncan:** If I might intervene, Mr. Guimont—

**The Chair:** Madam Duncan, time has expired.

Over to Madam Bateman, who now has the floor.

**Ms. Joyce Bateman:** Thank you very much, Mr. Chair.

Mr. Fonberg, you were discussing the three kinds of costs, and my colleague Mr. Allen wasn't able to allow you to finish. I think it would be very useful to this committee if you could table the facts and the details of the composition of the costs for all the members of this committee.

What I'm hearing very clearly is that your analysis, right from the start, has included acquisition costs and sustainment costs for 20 years. Then you, as we did here, heard from the Auditor General, who is now suggesting that we also include operating costs. If you could table with this committee for our report the composition of those, that would be helpful.

Thank you, Mr. Chair.

I have a few quick questions, short questions, but I want to understand. Have we purchased any fighter aircraft to replace the fleet of CF-18s yet?

**Mr. Robert Fonberg:** No, we haven't.

**Ms. Joyce Bateman:** Okay, thank you, sir.

Have we paid out any money for an airplane, or actually placed a procurement order?

**Mr. Robert Fonberg:** We have placed no procurement order and have spent no money on acquisition. We continue to be part of the MOU and we pay into the development costs.

**Ms. Joyce Bateman:** Excellent.

I'm glad, sir, that you mentioned the MOU, because I have a few questions. First, when did we first join the joint strike fighter program? Would you be kind enough to explain what the joint project office is, who runs it, and what it does?

**Mr. Robert Fonberg:** That's a good question. It's a very structured governance approach. I would ask Mr. Ross to speak to that question. He's intimately involved with the office.

To clarify, in 1997, when we joined the program, it was not called the joint strike fighter...

Was it called the joint strike fighter program?

**Mr. Dan Ross:** It was called the joint air capability technology project.

**Mr. Robert Fonberg:** Could you speak to the...?

**Ms. Joyce Bateman:** Forgive me, Mr. Ross and Mr. Fonberg, but could you also include the benefits that accrue to Canada in your description of how this works, and exactly what role we play?

Thank you.

**Mr. Robert Fonberg:** Absolutely.

**Mr. Dan Ross:** In terms of the joint project office, it was created in the mid-1990s under the Americans, because they were pursuing a lightweight fighter replacement for a number of fleets, F-14, F-15s, F-16s, and their Harriers used by the United States Marine Corps. They stated the requirement for a stealthy supersonic aircraft that could meet all those roles.

The JPO, the joint strike fighter program office, has grown to 1,700 people: 1,600 Americans and 100 military and civilian personnel from the partner countries. It's composed of world-class experts in aircraft design, in technology development, testing, costing, and program management. We have five full-time members in the joint project office in Washington. Our first member joined in 1998.

Thank you.

**Ms. Joyce Bateman:** I appreciate the time is running out, Mr. Chair. The questions I asked regarding the costing and the estimates and the benefits, who runs it, what it does, may I through the chair respectfully request the Department of National Defence to table that information for all of us?

• (1045)

**The Chair:** Thank you.

Any problem with that, Deputy?

**Mr. Robert Fonberg:** No, Mr. Chairman.

**The Chair:** Very well, that will be carried out. Thank you.

**Ms. Joyce Bateman:** Thank you very much.

**The Chair:** Madam Bateman, you still have the floor. You're good for a minute.

**Ms. Joyce Bateman:** Oh, well, then.... Okay, I'm good for a minute. Was that the bell?

**The Chair:** Go ahead.

**Ms. Joyce Bateman:** To clarify, if I could, sir, the request that we've made in writing—and I thank you for this latitude—how does membership in this joint project office benefit Canada? That's of real interest to me. What role does the joint project office play in Canada's costing and estimates?

Now, of course I respect the bell and the chair.

**The Chair:** We're okay. We're not voting for a while yet. We're only down the hall, so we can conclude our time. You still have a couple of moments if you want. Are you good?

**Ms. Joyce Bateman:** Yes, I'm good.

**The Chair:** I want to ask a couple of quick questions.

I want to confirm the \$9 billion to \$10 billion that's available, potentially, for Canadian industry. That's a global figure, correct? Everybody participating in the development would also be available to bid on that, right? That's not just a captive market for Canada?

**Mr. Simon Kennedy:** That's an estimate of the opportunities to Canadian firms as a result of their participation in this process, given the estimated build of 3,100 planes.

**The Chair:** But it's not an exclusive bidding by us, is it? There is a competition that others will be participating in, isn't that correct?

**Mr. Simon Kennedy:** This is the estimated slice of the pie for Canada. The actual cost of building this and the contracts available internationally would be much larger. This is an estimate of the opportunities Canada would be able to capture.

**The Chair:** This is the portion of it that you believe we will get, but there are no guarantees. It's still a competition, isn't it?

**Mr. Simon Kennedy:** There are no guarantees.

**The Chair:** The last question is—

**Mr. Andrew Saxton:** Mr. Chair, the bells are ringing. I think we should get going.

**The Chair:** I understand that, but let me ask one more question.

I know that no money has been spent on acquisition. There has been over \$300 million spent. If we don't go ahead with the development of the F-35, do we get any of that hundreds of millions of dollars back?

**Mr. Dan Ross:** No.

**The Chair:** Thank you. That's what I wanted to know.

With that, the bells are ringing, and our time has expired. My thanks to our guests. We appreciate your being here, especially twice in a row.

Colleagues, this meeting stands adjourned.

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