



# Preparing for Takeoff

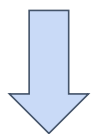
Launching a Transparent Process for Canadian Military Procurement

Interdepartmental Working Group on CF-18 Replacement:  
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February 18, 2017

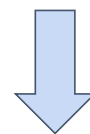


## Policy Problem

Canada's procurement process has failed to deliver a replacement for our aging CF-18 fleet



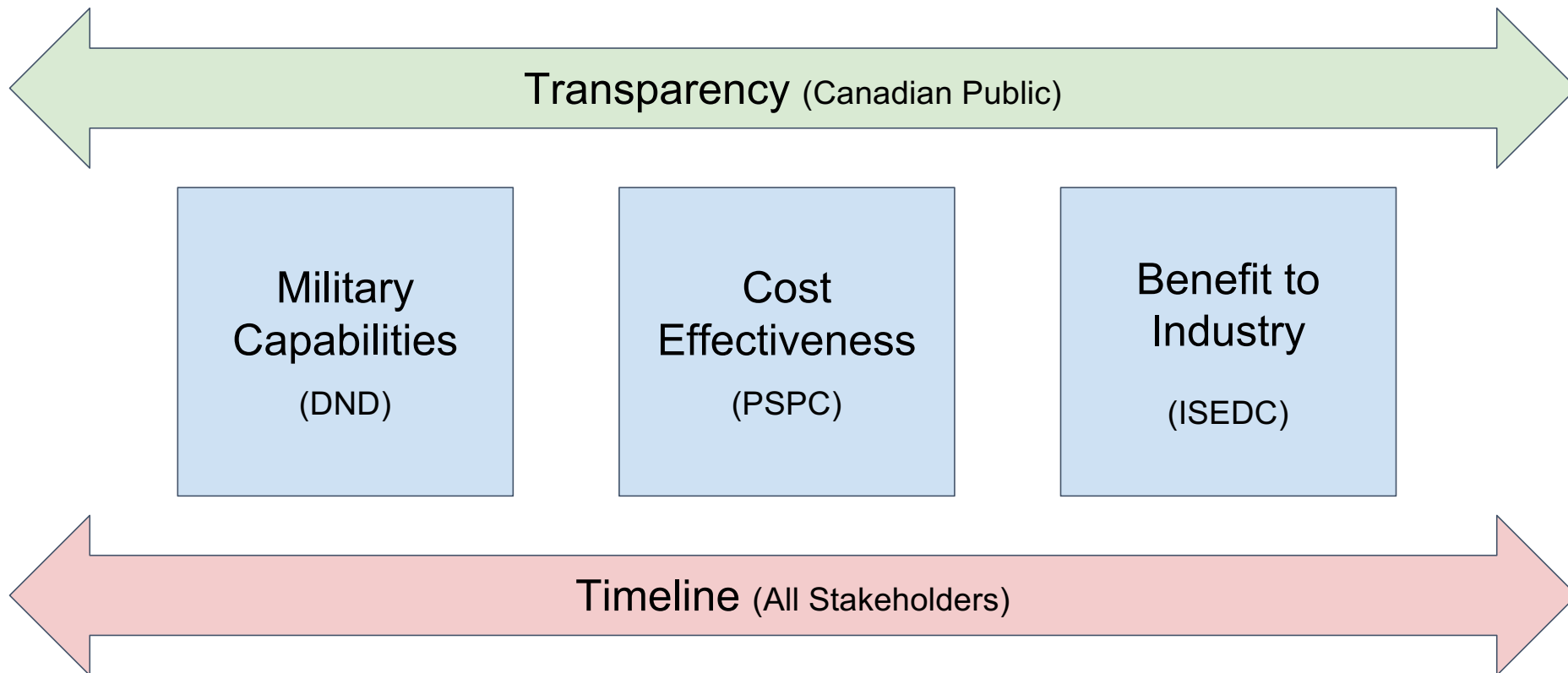
Process ✓



Product ✗



## Evaluation Criteria (Stakeholder Groups)





# Outline

- 1) Background
- 2) Three policy options
- 3) Recommendation and rationale
- 4) Highlights of our recommended option
- 5) Implementation plan
- 6) Assessment and Mitigation of Risk
- 7) Communications Strategy





# Background: Government Commitment

## Canada's Commitments

### Joint Strike Fighter Program

- 1997 - present
- Sunk cost: CAD\$448M

### Canada First Strategy, 2008

- CAD\$240B over 20 years

## Flawed F-35 Process

Inconsistent costing figures

Siloed decision-making

Public Opinion Poll

- Nanos: 97% of Canadians want transparency

## Nov. 22, 2016 Announcement

Sole source 18 Super Hornets

- CAD\$1.43B

Fair & Open Process for future procurement



## Background: Cost of Not Acting

Canada's CF-18 Fleet is Aging and needs replacement

- Extended lifetime
- Sovereignty concerns

Loss of public trust

- JSF biased to F-35

Canada's current procurement process not working



## Option 1: Sole-source F-35 (Status Quo)

*Proceed with the JSF program; immediately negotiate and sign a contract for the purchase of 65 F-35 fighter jets.*

- Acquisition cost CAD\$9.89B
- CAD\$152.2M/unit
- CAD\$45.8B lifecycle over 42 years

Criteria	Analysis
Transparency	Low public confidence
Military Capability	DND recommended
Cost Effectiveness	No competitive bidding
Industry Benefit	Maintain existing contracts
Timeline	Immediate decision



## Option 2: Staggered Procurement

*Immediately procure 18 Super Hornets to fill capability gap; create an open competition schedule, half of the fleet replaced every 21 years.*

- Acquisition cost CAD\$1.43B
- CAD\$79.6M/unit
- Nov. 22, 2016, announcement

Criteria	Analysis
Transparency	Open bidding
Military Capability	Mixed fleet
Cost Effectiveness	No economies of scale
Industry Benefit	Smaller offsets
Timeline	Delayed decision making





## Option 3: Open and Transparent Procurement Process

*Create a new Department to oversee an open bidding using clear measures for cost-effectiveness and performance.*

- “Defence Procurement Canada”
- Request for Proposal using \$ per flight hour, including life-cycle maintenance cost
- Negotiate competing contracts

Criteria	Analysis
Transparency	Open, comparable bidding
Military Capability	DND Input Balanced
Cost Effectiveness	More complete costing
Industry Benefit	Possible JSF Withdrawal
Timeline	Procurement in 24 months





## Recommendation

We recommend **Option 3: Open and Transparent Procurement Process**

## Rationale

Only policy option that delivers an open and transparent process while balancing military capability, cost effectiveness, and industry considerations



# Creating a New Department

Status Quo: Multi Departmental Model

Centralized, streamlined Defence Procurement Model



- Independent Department
- Ministerial Responsibility
- Single point of accountability
- Streamlined process
- Performance Measures
- Specialized knowledge
- Legacy: *Canada First* capital modernization (CAD\$240B) to 2028



# Request For Proposal (RFP) Process

- Based on 491,400 flight hours (*planned yearly flying rate \* service life*)
- Includes all acquisition and maintenance costs
- Punitive measures for delays

## Military

- Payload
- Range
- Sensors

## Cost

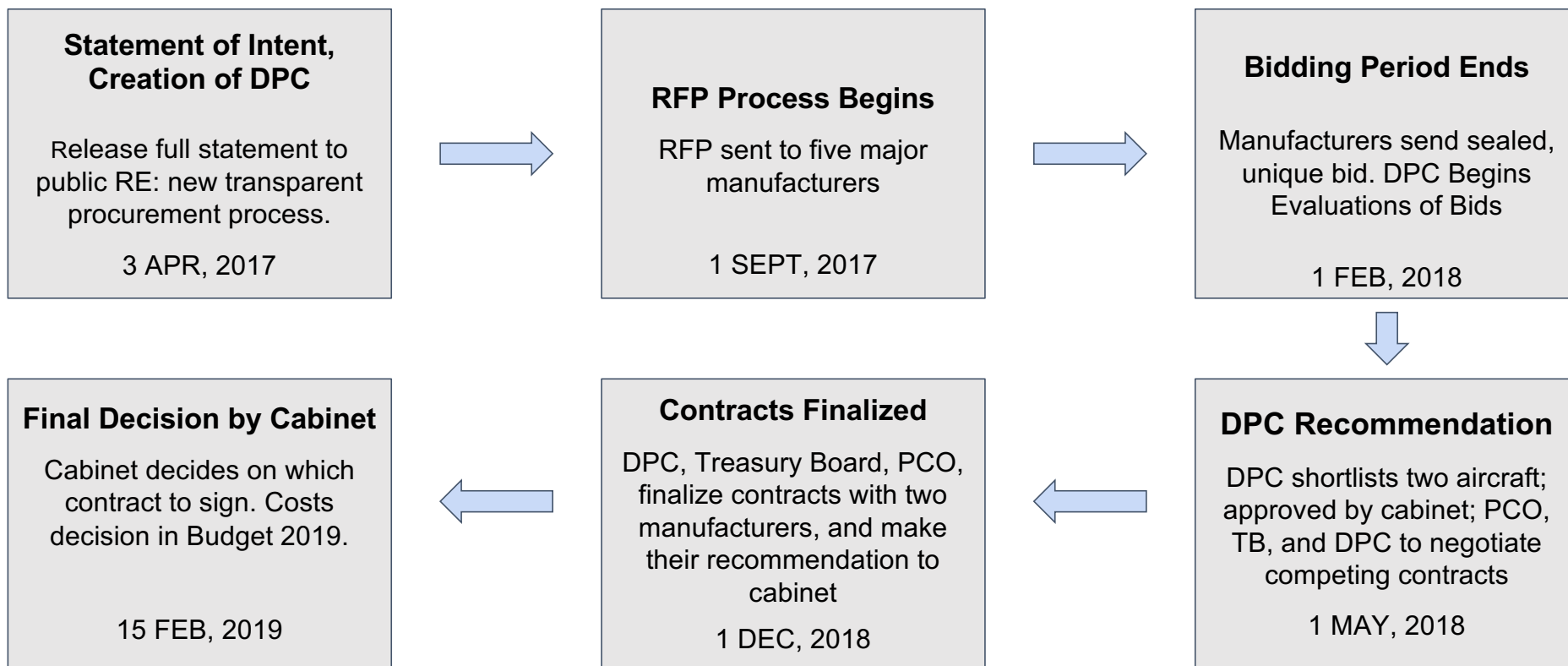
- Acquisition
- Sustainment
- Operation

## Industry

- Offset investments
- Job creation
- Origin of supplies



# Implementation Plan





## Policy Considerations

- Is implementation feasible?
  - Yes - Precedent for completing project on specified timeline, new department
- Balancing military capabilities, cost effectiveness, industry benefits
- Transparency of RFP (via \$/flight hour) balanced with protection of proprietary information
- Creation of DPC for future military procurement



# Assessment and Mitigation of Risks

Risk Category	Assessed Risks (Initial Risk Level)	Mitigation Strategy (Mitigated Risk Level)
Budgetary	<ul style="list-style-type: none"> <li>• Cost overruns/"gold plating"</li> <li>• High lifecycle cost</li> <li>• Collusion/Cartel behavior in RFP</li> </ul>	<ul style="list-style-type: none"> <li>• Off-the-shelf purchasing</li> <li>• Maintenance costs included in RFP, contract</li> <li>• Game Theory: No chance for collusion</li> </ul>
Political	<ul style="list-style-type: none"> <li>• Perceived lack of transparency</li> <li>• Media/lobby group pressure</li> </ul>	<ul style="list-style-type: none"> <li>• Publish \$ <i>per flight hour</i> for all bidders as a standard, transparent measure of value</li> </ul>
International	<ul style="list-style-type: none"> <li>• Strategic integration with allies</li> <li>• International industry lobby</li> </ul>	<ul style="list-style-type: none"> <li>• Strategic considerations in RFP</li> <li>• Some risk regardless of decision</li> </ul>
Procedural	<ul style="list-style-type: none"> <li>• Creation of new ministry</li> <li>• Length of RFP process</li> </ul>	<ul style="list-style-type: none"> <li>• Organized from existing bureaucracy</li> <li>• Precedent for &lt; 30 months</li> </ul>
Economic	<ul style="list-style-type: none"> <li>• Loss of industrial contracts</li> </ul>	<ul style="list-style-type: none"> <li>• High opportunity cost of aerospace investment</li> </ul>



# Communications Strategy - Key Messages

	Internal	External
Military Capability	One line of accountability, uniform goals	<i>Streamlined delivery of military equipment</i>
Cost Effectiveness	Process will drive down costs as firms compete for the contract	<i>Popular support for fair, open competition</i>
Industrial Benefit	Low ROI (\$0.82 per \$1 spent)	<i>Industrial offsets create jobs, but the Government is purchasing a plane based on capabilities</i>



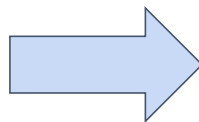




# Conclusion

## Focusing on the Process

- Single department
- Open, detailed RFP
- Comparable cost figure

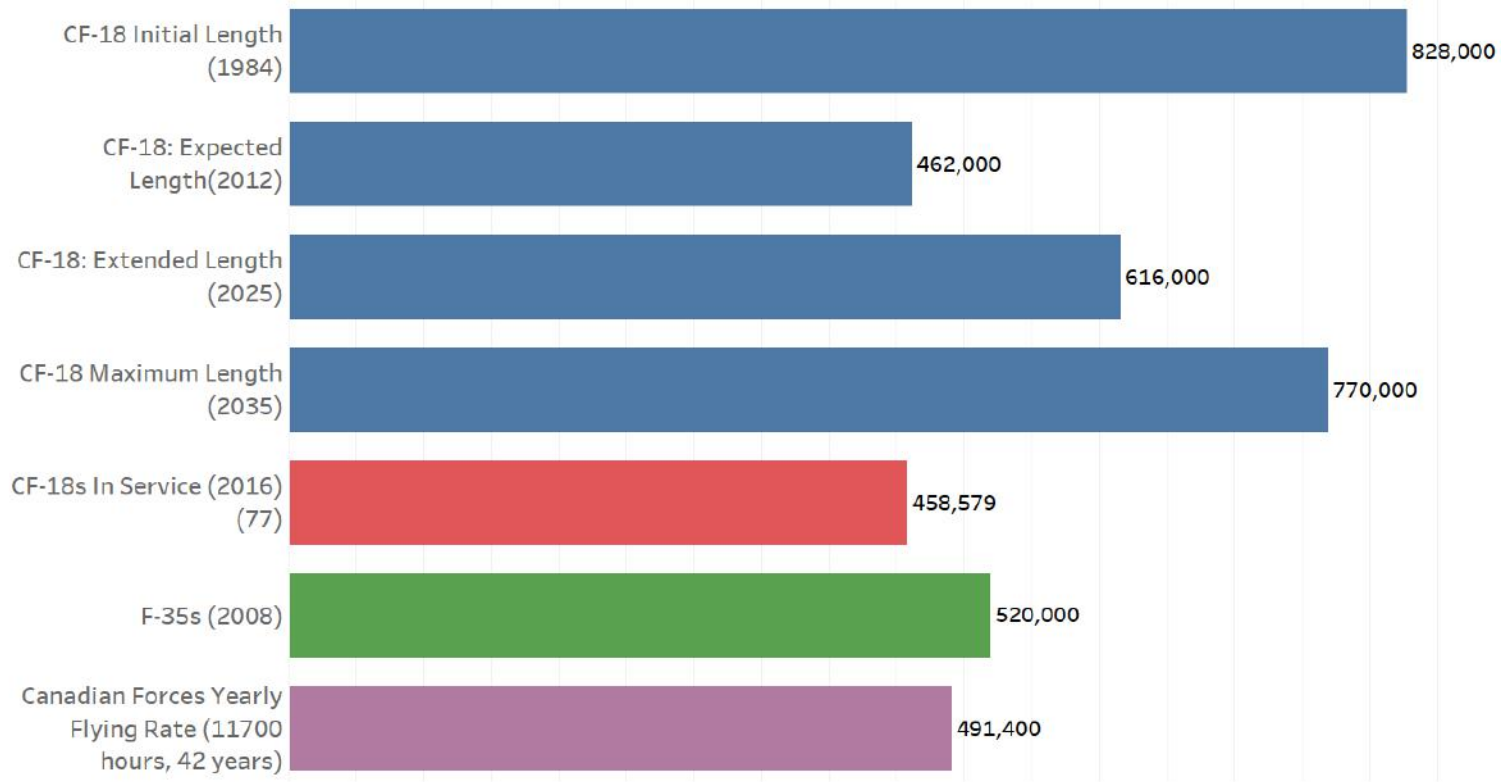


## Delivers the Product

- Capable aircraft
- Cost effective
- Timely and transparent

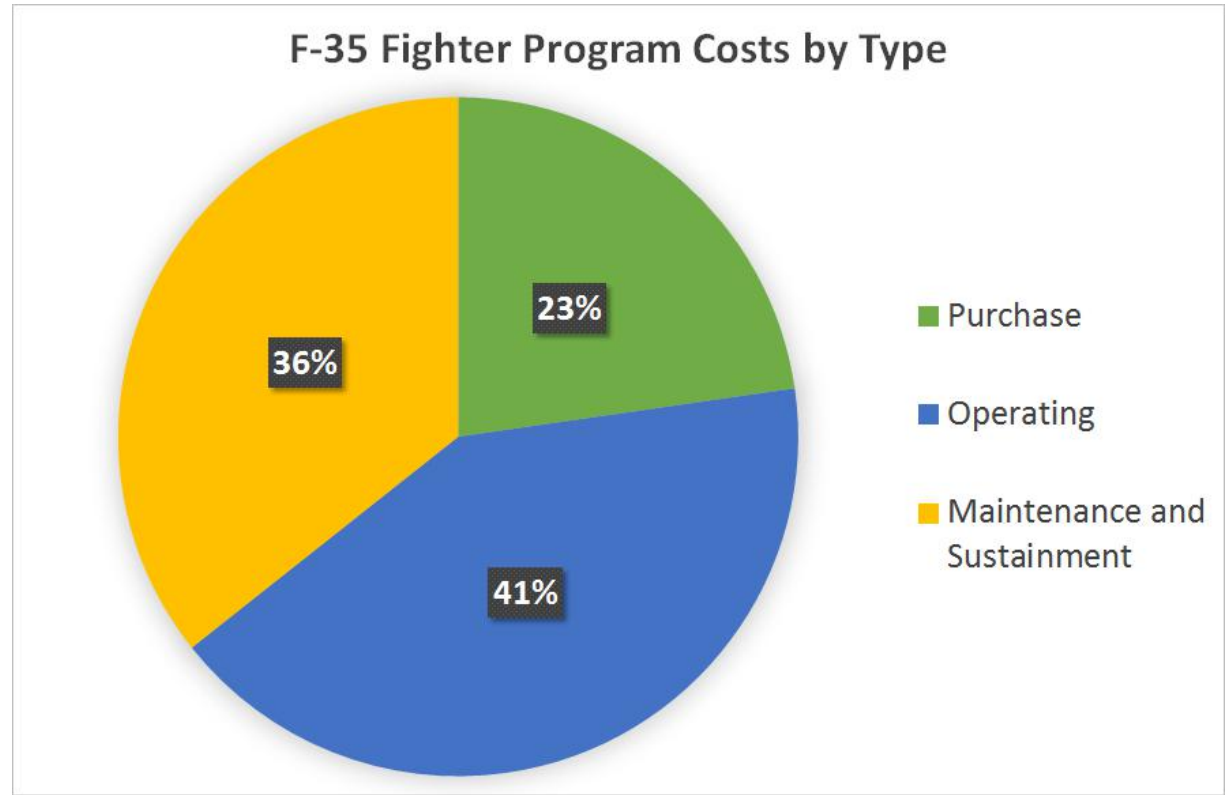


# Appendix A: Canadian Fighter Jet Service Hours



# Appendix B: DND F-35 Costing (2012)

Source: Department of National Defence





## Appendix C: Input-Output Multipliers

INDUSTRY	OUTPUT (per \$1.00)	GDP (per \$1.00)	WAGES (per \$1.00)	JOBS CREATED (per \$1 million)
Aerospace Product and Parts Manufacturing	\$1.74	<b>\$0.82</b>	<b>\$0.50</b>	7.14
All Industries	\$2.00	<b>\$1.09</b>	\$0.60	10.65
Defence Services	\$2.06	\$1.24	\$0.83	12.76
Other Federal Government Services (Except Defence)	\$2.05	\$1.25	\$0.86	11.76
Provincial and Territorial Government Services	\$2.29	\$1.16	\$0.74	11.58
Ship and Boat Building	\$2.08	<b>\$0.97</b>	\$0.69	12.27

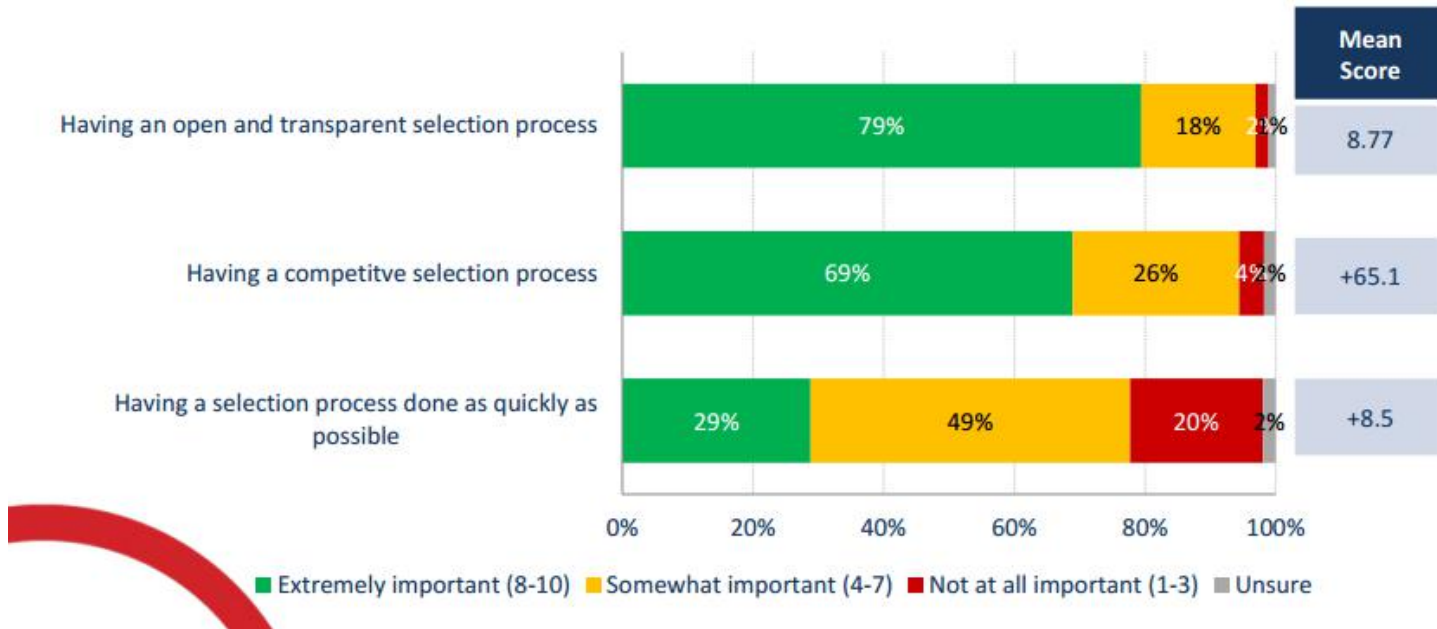
Source: Statistics Canada, 15F0046X



# Appendix D: Preferences on New jet Fighters selection process

## New jet fighters selection process

Source: Nanos Research, RDD dual frame hybrid telephone and online random survey, June 24<sup>th</sup> to 26<sup>th</sup>, 2016, n=1,000, accurate 3.1 percentage points plus or minus, 19 times out of 20.



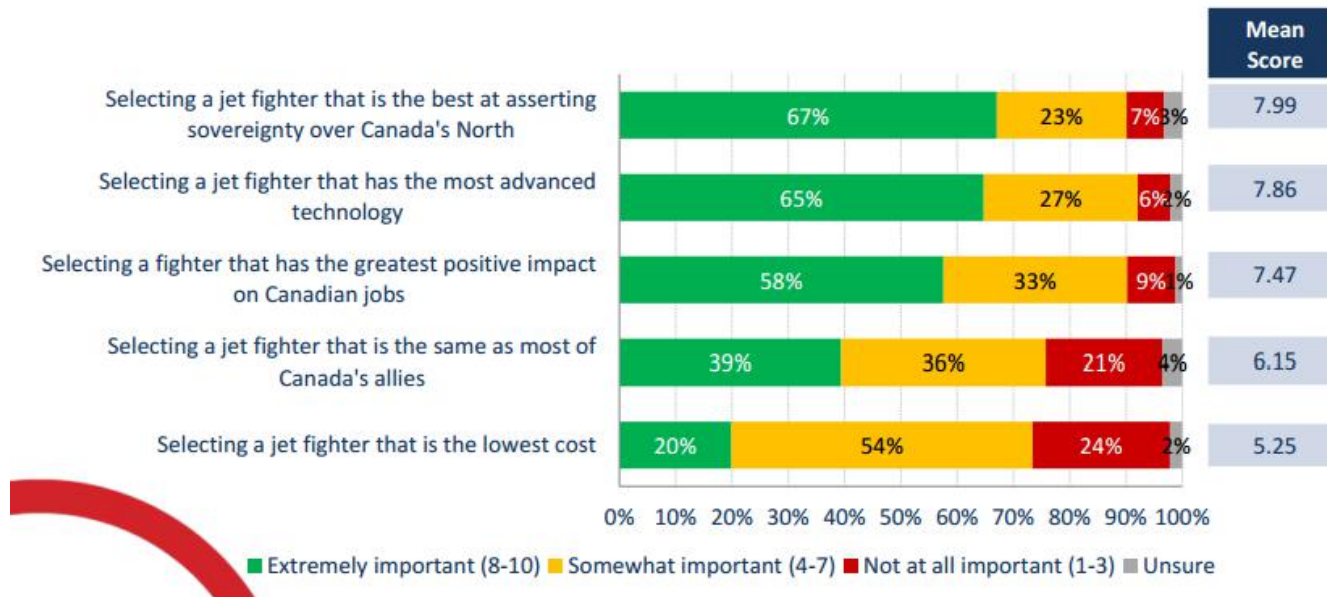
Source: <http://www.nanosresearch.com/sites/default/files/POLNAT-S15-T689.pdf>, page 11



# Appendix E: Preferences on Acquiring new fighter jets

## Acquiring new fighter jets

Source: Nanos Research, RDD dual frame hybrid telephone and online random survey, June 24<sup>th</sup> to 26<sup>th</sup>, 2016, n=1,000, accurate 3.1 percentage points plus or minus, 19 times out of 20.



Source: <http://www.nanosresearch.com/sites/default/files/POLNAT-S15-T689.pdf>, page 5



# Appendix F: Defence Procurement Canada Structure

