

Industrial Participation Symposium

Industrial and Technological Benefits and Value Proposition

Opening Remarks

March 26th, 2015, The Westin Ottawa, Provinces Ballroom, Ottawa, Ontario

Check Against Delivery

GOOD MORNING LADIES AND GENTLEMEN, CADSI MEMBERS, GOVERNMENT PARTNERS AND INTERNATIONAL DELEGATES. WELCOME TO OUR INDUSTRIAL PARTICIPATION SYMPOSIUM. THE GOAL OF THIS SYMPOSIUM IS FOR US, A COMMUNITY OF OFFSET PRACTITIONERS, OBLIGORS AND RECIPIENTS, TO COME TOGETHER TO LEARN FROM EACH OTHER, TO DISCUSS THE CHANGES THAT ARE OCCURRING IN CANADA AND THE OUTCOMES WE WANT TO SEE ACHIEVED AND TO CONTINUE TO DEVELOP THOSE RELATIONSHIPS WITH THE MANAGERS OF THE PROGRAM AND THOSE AGENCIES THAT ACT AS PARTNERS. BUT BEFORE WE DIVE INTO THE VERY MEAT OF THE CONFERENCE PROGRAM, I THOUGHT THAT IT MIGHT BE WORTHWHILE TO GIVE PARTICIPANTS WHO ARE NOT A PART OF THE CADSI INDUSTRIAL PARTICIPATION COMMITTEE A BIT OF BACKGROUND AND CONTEXT.

AS MANY OF YOU ARE AWARE, CANADA HAS APPLIED AN OFFSET POLICY WHEN PROCURING GOODS AND SERVICES THAT ARE EXCLUDED OR EXEMPT FROM INTERNATIONAL TRADE AGREEMENTS. PRIOR TO 1986, THE POLICY WAS APPLIED IN AN AD HOC MANNER, BUT AT TIMES THE GOALS OF THE CANADIAN GOVERNMENT WITH RESPECT TO OUTCOMES FOR THE INDUSTRIAL BASE FORMED A PART OF UP FRONT CONTRACTUAL OBLIGATIONS. IN 1986, THE GOVERNMENT MOVED FROM AN AD-HOC APPROACH TO A FORMAL POLICY WHICH YOU HAVE COME TO KNOW AS THE INDUSTRIAL AND REGIONAL BENEFITS POLICY - THE IRB POLICY. UNTIL LAST YEAR, THE IRB POLICY HAS BEEN CANADA'S MAIN TOOL FOR LEVERAGING ECONOMIC BENEFITS FROM DEFENCE PROCUREMENTS.

AS WITH ANY POLICY, IT IS IMPORTANT TO REVIEW THE APPROACH AGAINST THE DESIRED OUTCOMES OVER THE YEARS IT IS APPLIED AND TO CONSIDER OUR MODEL IN THE CONTEXT OF WHAT OTHER COUNTRIES ARE DOING. THE GOVERNMENT HAS, OVER THE YEARS, MODIFIED THE IRB POLICY TO ENCOURAGE CONTRACTORS TO FULFIL THEIR OBLIGATIONS THROUGH HIGH-QUALITY INVESTMENTS IN CANADA. MULTIPLIERS AND OTHER MECHANISMS HAVE BEEN USED TO ENCOURAGE CONTRACTORS TO UNDERTAKE R&D, PROVIDE VALUABLE SUPPLY CHAIN AND EXPORT OPPORTUNITIES TO CANADIAN FIRMS, AND PROVIDE OPPORTUNITIES FOR SMALL AND MEDIUM-SIZED ENTERPRISES TO BECOME SUPPLIERS TO PRIME CONTRACTORS AND THEIR TIER ONE SUPPLIERS. IT IS IMPORTANT TO NOTE, HOWEVER, THAT THE OUTCOMES OF THIS POLICY WERE LARGELY

DETERMINED AFTER A SUCCESSFUL CONTRACTOR WAS SELECTED AND THAT IT DOES RELY MORE ON ENCOURAGEMENT AS OPPOSED TO CONTRACTUAL OBLIGATION WITH RESPECT TO THE ACTUAL ACTIVITIES UNDERTAKEN IN CANADA.

BUT AROUND THE WORLD, CONDITIONS ARE AND HAVE BEEN CHANGING; FOR THOSE OF YOU WHO HAVE READ THAT LITTLE MANAGEMENT BOOK WE CAN SAY THAT "THE CHEESE HAS MOVED". WHILE LEVERAGING DEFENCE PURCHASES IS NOT UNIQUE TO CANADA AT ALL AND IS DONE IN A VARIETY OF WAYS, THE STRONGER REGIMES INCLUDE THINGS LIKE DIRECT GOVERNMENT OWNERSHIP STAKES IN COMPANIES; DIRECTING CONTRACTS TO NATIONAL INCUMBENTS; REQUIRING IN-COUNTRY WORK SHARES. OFFSET POLICIES AND PRACTICES ARE CONSIDERED A MORE MODERATE APPROACH.

IN OTHER WORDS, WE KNOW THAT DEFENCE FIRMS OPERATE IN A MANAGED AND "REGULATED" MARKET WHERE GOVERNMENTS ARE THE PRIMARY CUSTOMER. DEFENCE IS BY NO MEANS A 'FREE MARKET'. THIS REGULATED ENVIRONMENT CAN AND IS USED BY GOVERNMENTS AROUND THE WORLD TO INCENTIVIZE COMPANIES TO COLLABORATE IN COUNTRY AND DRIVE A STRATEGIC NATIONAL AGENDA.

IN 2012, I WAS PART OF AN ADVISORY PANEL THAT WAS ESTABLISHED TO REVIEW, AMONG OTHER THINGS, DEFENCE PROCUREMENT, WITH A VIEW TO INCREASING OUR LEVERAGING POTENTIAL. THE OFTEN-REFERRED TO JENKINS REPORT, CANADA FIRST LEVERAGING DEFENCE PROCUREMENT THROUGH KEY INDUSTRIAL CAPABILITIES, RECOMMENDED THAT THE GOVERNMENT INCLUDE A CLEAR PRIORITY TO USE THE PROCUREMENT LEVER TO FOSTER MORE INNOVATIVE AND GLOBALLY COMPETITIVE COMPANIES IN CANADA. JENKINS WAS ALSO PREMISED ON THE ASSUMPTION THAT WE HAVE A UNIQUE WINDOW OF OPPORTUNITY OVER THE NEXT FEW YEARS TO CAPITALIZE ON MAJOR DEFENCE ACQUISITIONS LINKED TO THE CANADA FIRST DEFENCE STRATEGY. IN OTHER WORDS, WE HAVE DECIDED TO GET A LOT MORE "BANG FOR OUR DEFENCE BUCK" WITH THIS DEFENCE PROCUREMENT STRATEGY.

A CENTERPIECE OF THE STRATEGY IS A REVISION OF THE EXISTING INDUSTRIAL AND REGIONAL BENEFITS POLICY--NOW TRANSFORMED INTO "ITB" FOR INDUSTRIAL AND TECHNOLOGICAL BENEFITS. THE PRINCIPAL STRATEGIC ELEMENT WITHIN THE ITB POLICY IS CALLED THE VALUE PROPOSITION. THE VALUE PROPOSITION WILL BE A "RATED AND WEIGHTED" COMPONENT OF A CONTRACT BID. IT WILL REQUIRE THE WOULD-BE PRIME CONTRACTORS TO PUT FORWARD THEIR BEST PLAN--THAT IS, A VALUE PROPOSITION--TO PARTNER WITH CANADIANS IN WAYS THAT PROMOTE DEVELOPMENT OF SOPHISTICATED CAPABILITIES IN OUR ECONOMY. THESE PLANS WILL BE CENTRAL TO BID EVALUATION. THIS PARTNERSHIP THAT I SPEAK OF CAN LOOK LIKE:

- SUBCONTRACTING MANUFACTURING LABOUR IN CANADA USING SMALL/MEDIUM SIZED ENTERPRISES (SMES);
- OPENING A FULL MANUFACTURING LINE IN CANADA;
- TRANSFERRING OR EXECUTING A PORTION OF (OR ALL) R&D INTO CANADA
- COLLABORATING WITH SMES AND UNIVERSITIES;
- INCORPORATING MORE CANADIAN SMES INTO GLOBAL OEM SUPPLY CHAINS
- LICENSING INTELLECTUAL PROPERTY TO A SUPPLIER WHO THEN CAN EXPORT OUT OF CANADA;

FULLY TRANSFERRING INTELLECTUAL PROPERTY INTO CANADA THEREBY ESTABLISHING A CANADIAN FOOTPRINT AND A WORLD MANDATE FROM WHICH TO EXPORT.

THE ITB POLICY ALSO INCLUDES THE NON-VALUE PROPOSITION OFFSET OBLIGATION. IN SOME CASES, THIS COULD ALSO BE A SIGNIFICANT NEEDLE-MOVER WITH RESPECT TO WHAT TYPE OF WORK GETS PUT INTO CANADA. WHILE THE GOAL IS TO MAXIMIZE THE COMMITMENTS AT THE FRONT-END OF THE PROCUREMENT BEFORE THE CONTRACT IS SIGNED, THE REST OF THE OFFSET REQUIREMENT, IF MANAGED CORRECTLY WITH THE PROPER INCENTIVES, SHOULD STILL YIELD HIGH VALUE TRANSACTIONS WITHIN CANADA, ALTHOUGH POTENTIALLY MORE OF AN INDIRECT NATURE. IN FACT, I WOULD ARGUE THAT AS A PART OF THE OVERALL EVALUATION OF THE ITB POLICY, THE GREATER THE AMOUNT OF INDIRECT WORK, THE HARDER SCRUTINY THAT WORK SHOULD FALL UNDER IN ORDER TO ENSURE THAT IT REMAINS VALUABLE TO CANADA. FORTUNATELY, UNDER THE NEW POLICY, TRANSPARENCY WILL BE INCREASED THROUGH PUBLIC REPORTING OF CONTRACTUAL OBLIGATIONS AND THERE ARE ALSO TOUGHER ENFORCEMENT PROVISIONS.

BUT THE DEFENCE PROCUREMENT STRATEGY IS MORE THAN A VALUE PROPOSITION TOOL AND AN ITB POLICY. THE SUM OF THE PARTS THAT WE PROPOSED IN THE JENKINS' REPORT IS THE VISION FOR HOW IT SHOULD WORK. HERE'S MY TAKE ON THE VISION:

A VERY LARGE PROCUREMENT IS GOING TO BE MADE. PRIOR TO THE LAUNCH, THE NEW DEFENCE PROCUREMENT SECRETARIAT--MADE UP OF OFFICIALS FROM THE KEY STAKEHOLDERS NATIONAL DEFENCE, PUBLIC WORKS, INDUSTRY CANADA, TREASURY BOARD AND PERHAPS EVEN TRADE--REVIEWS THE OBJECTIVES AND EXPECTED OUTCOMES. THE RESULTS OF REVIEWS ON HIGH-LEVEL, MANDATORY REQUIREMENTS ARE BRIEFED. THE INDUSTRIAL LANDSCAPE, KICS OR MARKET SEGMENTS AND CAPABILITY GAPS ARE RAISED PERHAPS EVEN WITH DATA THAT HAS BEEN SOURCED FROM A FULLY-FUNCTIONING DEFENCE ANALYSIS INSTITUTE (DAI) AND THAT HAS FLOWED IN FROM STATISTICS CANADA, INDUSTRY CANADA AND THE REGIONAL DEVELOPMENT AGENCIES AND IN CONSULTATION WITH INDUSTRY ITSELF. PROCUREMENT TOOLS AND CONSIDERATIONS ARE PUT ON THE TABLE - NATIONAL SECURITY, CANADIAN CONTENT, SEGMENTATION OF THE PROCUREMENT INTO SUB-PROCUREMENTS, MANDATORY INDUSTRIAL PARTICIPATION, AND VALUE PROPOSITIONS. IT IS HERE WHERE THE PROCUREMENT STRATEGY IS CLARIFIED AND THE DESIRED OUTCOMES ARE SOLIDIFIED AND UNDERSTOOD BY ALL.

AS THE PROCUREMENT IS ESTABLISHED, THE INDIVIDUAL DEPARTMENTS EXECUTE ON THEIR TASKS. DND OUTLINES ITS REQUIREMENTS, INDUSTRY CANADA ARTICULATES THE VALUE PROPOSITION AND ENGAGES WITH INDUSTRY, AND PUBLIC WORKS RUNS THE PROCUREMENT PROCESS. SENIOR OFFICIALS AND THE KEY PORTFOLIO MINISTERS ARE INVOLVED AT VARIOUS STAGES OF THE PROCESS TO KEEP IT MOVING AND FOCUSED ON THE STRATEGIC OBJECTIVES.

A WINNING BIDDER(S) IS SELECTED. THERE IS A GOOD UNDERSTANDING OF WHAT WILL BE DELIVERED AND WHEN. THE DEGREE TO WHICH THE INDUSTRIAL BASE IN CANADA WILL DEVELOP, DELIVER, MAINTAIN, REPAIR, SERVICE AND TRAIN IS WELL-UNDERSTOOD AND CONTRACTUALLY OBLIGATED. WE KNOW WHERE WE WILL BE MAINTAINING

CAPACITY IN CANADA'S INDUSTRIAL BASE OR CREATING IT AND WE KNOW WHAT THE OBLIGATIONS ARE ON THE PRIME CONTRACTOR AND ITS SUB-CONTRACTORS AND SUPPLIERS. IN SOME CASES, THE STRUCTURE OF THE PROCUREMENT ITSELF LED TO THE CONCLUSION.

NOW IMAGINE THAT APPROACH PLAYING OUT ON THE LARGEST PROCUREMENT IN CANADIAN HISTORY - THE CANADIAN SURFACE COMBATANT - A \$24B MEGAPROJECT THAT CAN AND SHOULD BE USED TO SHAPE PARTS OF OUR DEFENCE INDUSTRY AND OUR NATIONAL INTERESTS LONG INTO THE FUTURE. IT IS QUITE CRITICAL THAT WE ALL WORK TOGETHER TO GET AS CLOSE TO THIS PLACE AS POSSIBLE AS QUICKLY AS WE CAN TO SEIZE THAT OPPORTUNITY. EVEN A BACK-OF-THE-ENVELOPE CALCULATION TELLS US THAT THERE IS PROBABLY AN ADDRESSABLE \$5-10B OF CANADIAN WORK SHARE IN THE CSC AND WE KNOW THAT WHAT HAPPENS IN THE ACQUISITION PHASE OF A PROCUREMENT THIS LARGER PORTION WILL BE THE "GIFT THAT KEEPS ON GIVING" THROUGHOUT THE NEXT 20-35 YEARS. THAT IS HOW YOU SUSTAIN A PERMANENT SHIPBUILDING CAPABILITY IN CANADA, WHICH IS A CENTRAL GOAL OF THE NSPS.

AS WE GO THROUGH THIS DAY, I'D ENCOURAGE YOU TO KEEP IN THE BACK OF YOUR MINDS WHAT WE ARE TRYING TO ACHIEVE. WHAT HAS WORKED IN THE PAST TO GET US CLOSER TO THIS TYPE OF OUTCOME AND WHAT WE HAVE DONE THAT HAS TAKEN AWAY FROM IT. HOW CAN WE WORK WITH THE FEDERAL GOVERNMENT DEPARTMENTS AND THE REGIONAL DEVELOPMENT AGENCIES TO PROACTIVELY IDENTIFY AND SHOWCASE THE CAPABILITY WE HAVE IN CANADA AND TO SOME EXTENT HELP FORECAST WHERE WE BELIEVE WE NEED TO BE IN 20 YEARS' TIME.

AND ON BEHALF OF CADSI, OUR MEMBERS AND OUR PARTNERS, I'D LIKE TO THANK-YOU FOR COMING AND CONTRIBUTING TO THIS VERY IMPORTANT CONVERSATION.