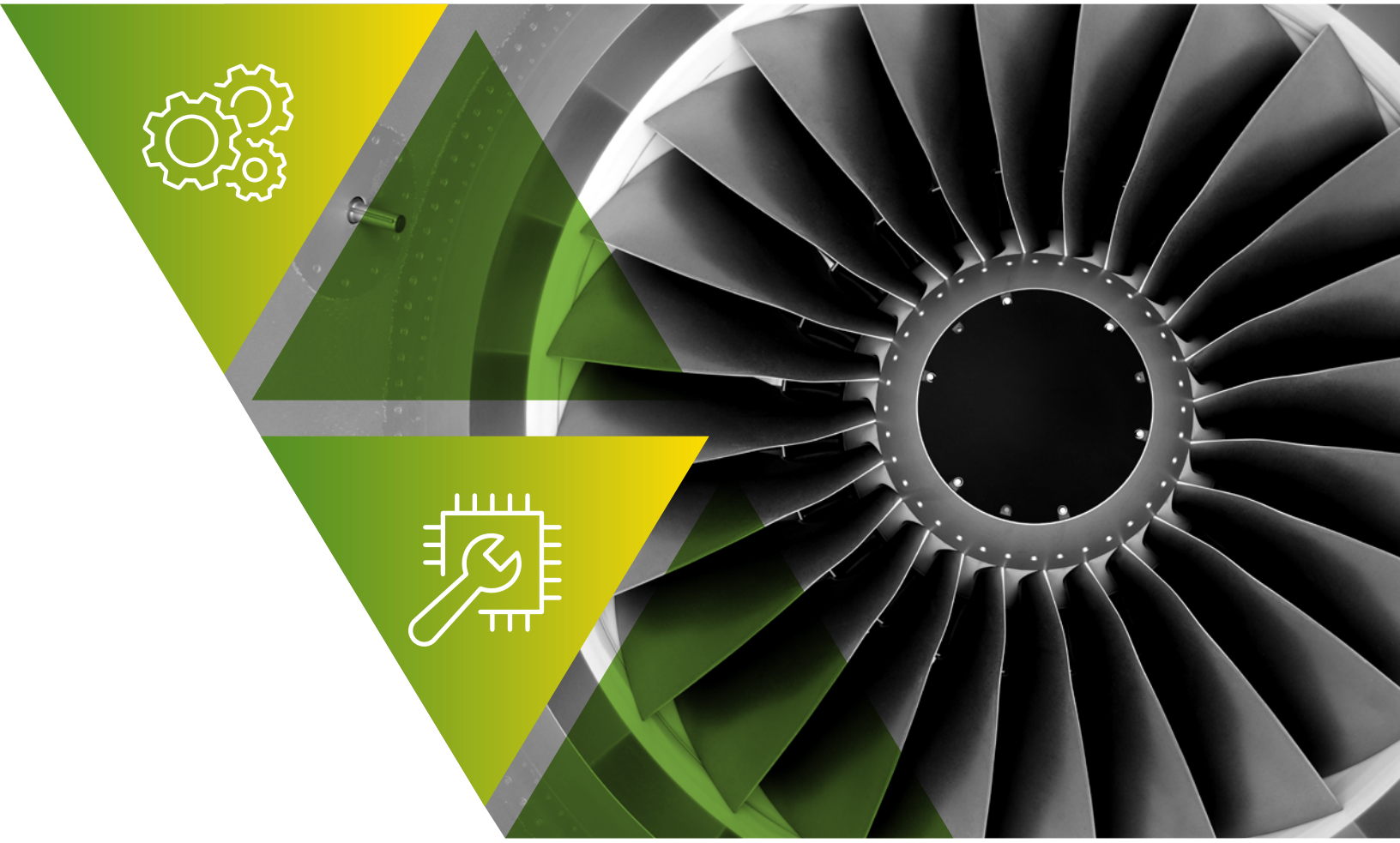
Reports of the Auditor General of Canada
to the Parliament of Canada

Report 10

Industrial and Technological Benefits



Independent Auditor's Report | 2024

Office of the Auditor General of Canada

Bureau du vérificateur général du Canada

Performance audit reports

This report presents the results of a performance audit conducted by the Office of the Auditor General of Canada (OAG) under the authority of the *Auditor General Act*.

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Performance audits are planned, performed, and reported in accordance with professional auditing standards and OAG policies. They are conducted by qualified auditors who

- establish audit objectives and criteria for the assessment of performance
- gather the evidence necessary to assess performance against the criteria
- report both positive and negative findings
- conclude against the established audit objectives
- make recommendations for improvement when there are significant differences between criteria and assessed performance

Performance audits contribute to a public service that is ethical and effective and a government that is accountable to Parliament and Canadians.

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At a Glance

Overall message

The Industrial and Technological Benefits Policy applies to defence procurements over $100 million with some exceptions and may be applied to defence procurements between $20 million and $100 million. Industrial and technological benefits form part of the bidding process that determines who is awarded major defence contracts. While the policy states that an equal amount of an awarded contract's value is to be invested back into the Canadian economy by a contractor, we found 10 procurements out of 60 over $100 million where either the policy was not applied or the investment in the economy was less than 100% of the awarded contract's value.

Innovation, Science and Economic Development Canada—responsible for administering the Industrial and Technological Benefits Policy—was unable to demonstrate that the policy met its objectives, which included supporting the long-term viability and growth of the defence industry. Delays in procurement process negotiations and additional costs stemming from contractors managing their industrial and technological benefits obligations conflicted with the goal of the Defence Procurement Strategy to deliver the right equipment to the Canadian Armed Forces in a timely manner.

We found that Innovation, Science and Economic Development Canada lacked some elements to ensure sound administration of the policy, such as clear rules and guidance on how to apply the policy and good tracking of contract obligations, economic benefits, and job creation.

Key facts and findings

- From 2014 to 2023, 99 contracts worth at least $39 billion were awarded that included industrial and regional benefit and industrial and technological benefit obligations of more than $36 billion.
- Innovation, Science and Economic Development Canada did not have clear rules and guidance for applying the Industrial and Technological Benefits Policy.
- For the 60 eligible procurements over $100 million that we identified, 2 procurements had industrial and technological benefits commitments that were less than 100% of the contract value and 8 procurements had no obligations.
- Both the specific benefits and the full costs of the Industrial and Technological Benefits Policy were unknown.

See **Recommendations and Responses** at the end of this report.

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Introduction

Background

Industrial and Technological Benefits Policy

10.1 In 2014, the Defence **Procurement**[1] Strategy was established as a government-wide initiative to improve defence procurement by

- delivering the right equipment to the Canadian Armed Forces and Canadian Coast Guard in a timely manner
- streamlining and modernizing defence procurement processes and ensuring coordinated decision making
- leveraging defence equipment purchases to create jobs and economic growth for Canadians

10.2 Also in 2014, the Industrial and Technological Benefits Policy replaced the Industrial and Regional Benefits Policy. The Industrial and Technological Benefits Policy aims to leverage defence procurement and strengthen Canada's economy through research and development, job creation, and economic growth for Canadians.

10.3 Innovation, Science and Economic Development Canada is responsible for implementing the policy. The policy requires companies awarded defence and Canadian Coast Guard procurement contracts, both competitive and non-competitive, to engage in business activity in Canada for an amount equal to the value of the contracts. The policy applies to certain procurements worth more than $100 million and may be applied to contracts worth between $20 million and $100 million.

10.4 Globally, industrial and technological benefit policies typically include common elements such as monetary thresholds under which the policy does not apply, defined investment requirements, multipliers for specific types of investments, and use of direct and indirect business activities to meet industrial and technological benefit contracting **obligations**.[2] Canada's policy has all these characteristics. While some North Atlantic Treaty Organization (NATO) member countries and other key allies of Canada have a similar policy, others do not.

1 **Procurement**—For this audit, a process to acquire a defence capability and assess whether the Industrial and Technological Benefits Policy is applicable. If successful, the result is the signing of 1 or more contracts or other agreements.

2 **Obligations**—For contracts with industrial and technological benefits requirements, a contractor has contractual commitments toward the delivery of the goods and/or services and contractual obligations toward industrial and technological benefit amounts and business activities to be undertaken. For this report, "obligation" refers to the industrial and technological benefit amounts and activities.

10.5 Under the policy, companies seeking defence contracts in Canada, through procurement processes, must include with their offer an economic proposal. The economic proposal should demonstrate how the companies' business activities will contribute to 1 or more of the following objectives:

- support the long-term growth and sustainability of Canada's defence industry
- support the growth of **prime contractors**[3] and suppliers in Canada, including small and medium-sized enterprises in all regions of the country
- boost innovation through research and development in Canada
- increase the export potential of Canadian-based firms
- leverage opportunities in skills development and training to advance employment opportunities for Canadians

10.6 The economic proposal, known as a value proposition, is a required component of the competitive procurement process. The request for proposal for each competitive procurement defines the weighting of the 3 components to be assessed against the requirements: technical, cost, and value proposition. For contracts awarded under a competitive process, the weighting of the value proposition is typically set at about 10% of the overall bid evaluation score. For contracts awarded under a non-competitive process, Innovation, Science and Economic Development Canada negotiates Industrial and Technological Benefits terms and conditions with the contractor. In both procurements, the resulting contract will describe the obligations on the contractor to engage in business activities in Canada that would be aligned with its value proposition.

10.7 Under the policy, for each procurement, Innovation, Science and Economic Development Canada is responsible for determining the applicable **Key Industrial Capabilities**[4] that are considered areas of strategic interest to Canada. Relevant Key Industrial Capabilities are indicated on the request for proposal or the sole-source request, and potential contractors are asked to explain how their proposal would support each Key Industrial Capability.

10.8 In May 2018, providing a gender and diversity plan was introduced as an additional mandatory requirement of the value proposition. Contractors must describe in the plans their approach to increasing gender balance and diversity in their Canadian corporate structure and/or broader supply chains within the defence industry in Canada.

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3 **Prime contractor**—An organization that is awarded the contract to implement a procurement. The organization may employ sub-contractors or suppliers to support implementing the contract.

4 **Key Industrial Capabilities**—Introduced in 2018, Key Industrial Capabilities are included in the final request for proposal. They are areas of emerging technology with the potential for rapid growth, established industrial capabilities in Canada, and where domestic capacity is essential to national security.

10.9 From 2014 to 2023, 99 defence procurements worth at least $39 billion were awarded that included industrial and regional benefit and industrial and technological benefit obligations that were worth more than $36 billion.

Roles and responsibilities

10.10 **Innovation, Science and Economic Development Canada.** The department is responsible for administering the Industrial and Technological Benefits Policy. Specifically, the department is responsible for

- determining Canada's economic approach for certain Canadian defence procurements
- making recommendations on the application of the policy to procurements
- determining the evaluation criteria for and evaluating Industrial and Technological Benefits proposals (value propositions) submitted by bidders seeking defence contracts
- validating industrial and technological benefits business activities against obligations

10.11 **National Defence.** The department is responsible for

- defining the requirements and developing the specifications for defence procurements
- analyzing the associated options and cost estimates
- obtaining policy and funding approval
- providing technical expertise and bringing the equipment or services into use during the procurement process

10.12 **Public Services and Procurement Canada.** The department supports the Government of Canada by being its central purchasing and contracting authority. Its roles include acquiring equipment and services on behalf of National Defence and Fisheries and Oceans Canada by

- leading the stakeholder and industry engagement before and during the procurement process
- developing the procurement strategy
- leading the solicitation bid process
- overseeing the entire evaluation, including evaluating the financial proposals submitted by bidders
- managing the resulting procurement, contract, and amendments

Focus of the audit

10.13 This audit focused on whether Innovation, Science and Economic Development Canada ensured the Industrial and Technological Benefits Policy met its objectives, as part of the Defence Procurement Strategy, for contracts managed in partnership with National Defence and Public Services and Procurement Canada. This audit did not include Industrial and Technological Benefits Policy contracts involving the Canadian Coast Guard.

10.14 This audit is important because applying the Industrial and Technological Benefits Policy can result in billions of dollars of business activities. In its 2024 budget, the Government of Canada committed to more than $125 billion from 2022 to 2042 in incremental funding toward national defence. When the policy applies to defence spending, business activities take place in Canada's economy by the contractor in various areas.

10.15 More details about the audit objective, scope, approach, and criteria are in **About the Audit** at the end of this report.

Findings and Recommendations

Innovation, Science and Economic Development Canada did not establish clear rules and guidance for applying the policy

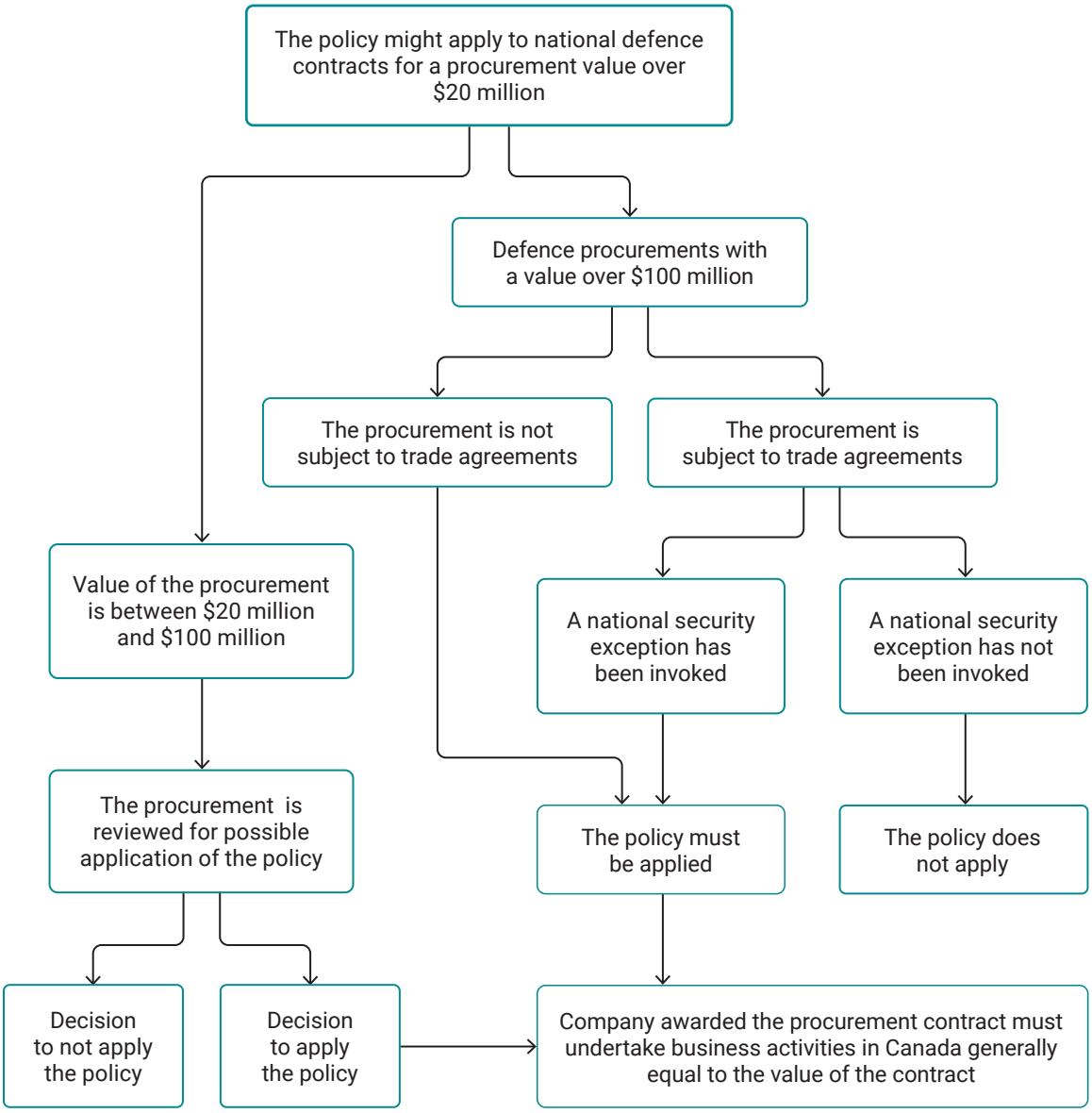
Why this finding matters

10.16 A policy that clearly outlines its objectives, roles and responsibilities, rules, definitions, exceptions, and how it will be applied provides clarity and consistency and limits interpretation. Without including these elements, policies are open to misunderstanding and irregularities in their application.

Context

10.17 Decisions on whether to apply the Industrial and Technological Benefits Policy are made at the beginning of the procurement process (Exhibit 10.1) by the Defence Procurement Strategy governance committees, composed of representatives of Innovation, Science and Economic Development Canada, National Defence, and Public Services and Procurement Canada. Once the decision whether to apply the policy or not is made, the request for proposal process can start.

Exhibit 10.1—Decision tree on the applicability of the Industrial and Technological Benefits Policy to defence procurements



Note: Procurements for the Canadian Coast Guard also follow this decision tree, but this audit did not include Industrial and Technological Benefits Policy contracts involving the Canadian Coast Guard.

Source: Based on information from Innovation, Science and Economic Development Canada

Exhibit 10.1—Decision tree on the applicability of the Industrial and Technological Benefits Policy to defence procurements—Text description

This flow chart shows 2 streams of defence procurement values and whether the Industrial and Technological Benefits Policy applies.

First stream

Value of the procurement is between $20 million and $100 million:

The procurement is reviewed for possible application of the policy.

- Decision to not apply the policy.
- Or, decision to apply the policy
  - Company awarded the procurement contract must undertake business activities in Canada generally equal to the value of the contract.

Second stream

Defence procurements with a value over $100 million:

The procurement is not subject to trade agreements.

- The policy must be applied.
- Company awarded the procurement contract must undertake business activities in Canada generally equal to the value of the contract.

The procurement is subject to trade agreements.

- A national security exception has been invoked.
- The policy must be applied.
- Company awarded the procurement contract must undertake business activities in Canada generally equal to the value of the contract.

If the procurement is subject to trade agreements but a national security exception has not been invoked, the policy does not apply.

Note: Procurements for the Canadian Coast Guard also follow this decision tree, but this audit did not include Industrial and Technological Benefits Policy contracts involving the Canadian Coast Guard.

Source: Based on information from Innovation, Science and Economic Development Canada

Missing clarity and guidance on applying the policy

Findings

10.18 We found that the Industrial and Technological Benefits Policy provided limited information on when and how it should be applied.

10.19 According to the policy, industrial and technological benefits obligations apply on all defence procurements worth more than $100 million that are not subject to trade agreements. In those cases where the defence procurement is subject to a trade agreement, but the national security exception is invoked, the procurement is subject to the Industrial and Technological Benefits Policy (Exhibit 10.1). The policy further requires that industrial and technological benefits obligations be equal to the value of the resulting contract.

10.20 We analyzed Innovation, Science and Economic Development Canada's database on 60 defence procurements over $100 million from 2014 to 2023. We identified

- 2 procurements where the industrial and technological benefits obligation was less than 100% of the value of the contract
- 8 procurements where the policy was not applied

Instead, in some cases, different approaches were applied with the intent to generate economic benefits, but these approaches were not identified as alternatives or exceptions in the Industrial and Technological Benefits Policy and would not necessarily contribute to meeting the policy's objectives.

10.21 The policy may be applied to procurements between $20 million and $100 million. In Innovation, Science and Economic Development Canada's database, we identified 39 defence procurements, over $20 million and less than $100 million, awarded from 2014 to 2023, to which the policy was applied. We found that it was unclear under what circumstances the Industrial and Technological Benefits Policy was applied.

10.22 Innovation, Science and Economic Development Canada developed an Industrial and Technological Benefit manual, but it did not include any instruction, definition, conditions, or criteria on which to base the decision whether to apply the policy to procurements between $20 million and $100 million. As well, for all procurements, it was not clear from our review of Innovation, Science and Economic Development Canada's manual whether the value of the procurement, for the purposes of applying the policy, should include option years or taxes, or whether the policy should be applied to all related contracts derived from procurements to which industrial and technological benefits were applied.

10.23 We examined 20 procurements from 2014 to 2023 with a value of $20 million or more where the policy was considered (Exhibit 10.2).

Exhibit 10.2—Details of industrial and technological benefits samples (2014 to 2023)

Sample information	Industrial and Technological Benefits Policy applied	Industrial and Technological Benefits Policy not applied
Number of procurements valued between $20 million and $100 million examined	3	6
Number of procurements valued at more than $100 million examined	7	4*
Total contract value of procurements examined	$2 billion	$1.5 billion

* These 4 samples are included in the 8 procurements identified in paragraph 10.20.

10.24 We found concerns with how the Industrial and Technological Benefits Policy was applied and documented for 9 of the 20 procurements reviewed, demonstrating a need for clearer guidance and standardization. We identified the following:

- 3 cases where the committee's decision about whether to apply the Industrial and Technological Benefits Policy was not documented (in 2 of these cases, the policy was applied)
- 2 cases where the committee decided that the Industrial and Technological Benefits Policy should be applied but it was not
- 4 cases where the policy was applied to the main procurement but was not applied to related contracts

Recommendation

10.25 Innovation, Science and Economic Development Canada should update and clarify the Industrial and Technological Benefits Policy and guidelines to include information about scope, application, and documentation requirements to support the consistent application of the policy to defence procurements.

Innovation, Science and Economic Development Canada's response. *Agreed.*

See **Recommendations and Responses** at the end of this report for detailed responses.

No rating or use of required gender and diversity plans

Findings

10.26 Since 1995, the federal government has committed to advancing gender equality. We found that, while bidders had been required since 2018 to submit a gender and diversity plan as part of their value proposition, the Industrial and Technological Benefits Policy did not require that the plan and its information be used for the evaluation of the procurement process. Specifically, the gender and diversity plan was not assessed as part of the evaluation of bids and its contents did not have an impact on the results of the competitive process. For example, 1 company was awarded a contract even though its gender and diversity plan stated that gender was not taken into consideration when hiring personnel. In our opinion, failing to use the plans to inform contract awards is a missed opportunity to advance diversity and inclusion in defence procurements.

The department lacked effective ways to measure the policy's economic benefits and creation of jobs

Why this finding matters

10.27 To determine whether a policy achieves expected outcomes, results must be measured against its objectives. Given the significant spending by Canada in the Canadian Armed Forces through defence procurements, and the extent of the industrial and technological benefits obligations of contractors, it is important that the Industrial and Technological Benefits Policy achieves its intended results to contribute to jobs, innovation, and economic growth across the country.

Context

10.28 To ensure that industrial and technological benefits obligations support the development of a globally competitive defence and security sector, Innovation, Science and Economic Development Canada directs the obligations into areas of strategic interest to Canada called Key Industrial Capabilities. As of 2024, Innovation, Science and Economic Development Canada had identified 17 Key Industrial Capabilities (Exhibit 10.3).

Exhibit 10.3—Key Industrial Capabilities that may be included in a request for proposal

Emerging technologies	Leading competencies and critical industrial services
• Advanced materials • Artificial Intelligence • Clean technology • Cyber resilience • Remotely piloted systems and autonomous technologies • Space systems	• Aerospace systems and components • Armour • Defence systems integration • Electro-optical / infrared systems • Ground vehicle solutions • In-service support • Marine ship-borne mission and platform systems • Munitions • Shipbuilding, design, and engineering services • Sonar and acoustic systems • Training and simulation

Source: Based on information from Industrial and Technological Benefits (ITB)—Model Terms and Conditions

10.29 In addition to reporting publicly on the policy through its parliamentary accountability documents, the department also produces an annual report on the Industrial and Technological Benefits Policy. This report aims to highlight the economic and innovation impacts from the policy.

Measurement of the policy against its objectives was ineffective

Findings

10.30 We found that the indicators developed by Innovation, Science and Economic Development Canada to measure the performance of the Industrial and Technological Benefits Policy were ineffective for determining whether the policy met its objectives because

- the indicator reported in the Departmental Results Report, used to outline progress and accomplishments, did not align with any policy objective or performance indicator in the department's performance measurement framework for the policy
- none of the medium- and long-term results in the framework could be exclusively attributed to the policy or activities of Innovation, Science and Economic Development Canada

10.31 For example, 1 long-term outcome of the policy was to increase Canada's defence sector revenues by 40% from 2014 to 2024. Though the target was met, Innovation, Science and Economic Development Canada was unable to demonstrate what proportion was attributable to the policy or to other efforts. We also note that the industry's growth could be due to unrelated reasons, such as inflation and global conflicts increasing demand for military supplies, equipment, and technology.

10.32 We found that some short-term performance indicators in the framework, used to measure the policy's impact, had targets that either were set below the baseline used as a starting point or were not aligned with what the indicator was measuring. Therefore, the targets would not improve or increase outcomes (Exhibit 10.4).

10.33 For another objective of the Industrial and Technological Benefits Policy, to develop skilled jobs, we found that Innovation, Science and Economic Development Canada had no performance indicators to assess whether this objective was met. In reviewing Statistics Canada data, we noted that, during our audit period, total employment increased in the defence industry; however, the number of highly skilled jobs in the defence sector declined.

Exhibit 10.4—The Industrial and Technological Benefits Policy's short-term performance indicators used targets that were at or below the baseline or did not align with the measurement

Indicator	Baseline (2021)	Target
Percentage of small and medium-sized businesses that benefit from procurements with a value proposition	Prime contractors involved small and medium-sized businesses in fulfilling 15.1% of their overall obligations	Prime contractors involve small and medium-sized businesses in fulfilling at least 15% of their overall obligations
Number of investments in skills development under the Industrial and Technological Benefits Policy	6 commitments in skills development and training	Over 5 commitments in skills development and training
Number of post-secondary and research institutions that benefit from the policy	33 post-secondary and research institutions benefiting from active projects	Over 30 post-secondary and research institutions benefiting from active projects

Source: Based on information from Innovation, Science and Economic Development Canada

10.34 Innovation, Science and Economic Development Canada's annual Industrial and Technological Benefits report provided an estimate of industrial and technological benefits' impact on the Canadian economy, but we found that the information in the report did not measure the policy's performance against its objectives. For example, the report identified how many research organizations participated in activities but not how that had changed or been boosted over time.

10.35 We also had concerns about the accuracy of the information in the report. For example, the inflation rate used to develop the estimates did not reflect actual rates, and the estimates were reported as averages over 5 years because lengthy validation processes meant that accurate annual results were not available.

Recommendation

10.36 Innovation, Science and Economic Development Canada should update its performance measurement framework to define specific indicators and targets to measure whether the Industrial and Technological Benefits Policy is meeting its objectives and use these measures to monitor the policy's performance.

Innovation, Science and Economic Development Canada's response. *Agreed.*

See **Recommendations and Responses** at the end of this report for detailed responses.

Unclear impacts on areas of strategic interest to Canada

Findings

10.37 We found that there was misalignment between the list of Key Industrial Capabilities used in requests for proposal and the needs identified by National Defence. For example, the munitions key industrial capability was never included in a request for proposal, during the period we audited, yet it had been identified by National Defence to be a current and emerging priority to increase domestic development and access to munitions.

10.38 In addition, Innovation, Science and Economic Development Canada did not establish targets or indicators to measure the impact that each key industrial capability was having on the defence industry. Consequently, Innovation, Science and Economic Development Canada could not determine whether any of the Key Industrial Capabilities had contributed to the long-term growth and sustainability of Canada's defence industry.

Recommendation

10.39 Innovation, Science and Economic Development Canada, in collaboration with National Defence, should ensure that the Key Industrial Capabilities align with Canada's defence needs. In addition, outcomes and indicators for Key Industrial Capabilities should be developed to measure their contributions to the Industrial and Technological Benefits Policy's results.

Innovation, Science and Economic Development Canada's response. *Agreed.*

See **Recommendations and Responses** at the end of this report for detailed responses.

Industrial and Technological Benefits contract obligations were not accurately tracked

Why this finding matters

10.40 Knowing whether a policy or program will meet its objectives requires following its progress and making adjustments in a timely manner. To do so, complete, accurate, and up-to-date information needs to be compiled to allow effective decision making and to provide an overview of progress toward the objectives.

Context

10.41 Innovation, Science and Economic Development Canada maintains a database to track industrial and technological benefits obligations, as well as to monitor contractors' progress in meeting their obligations. Contractors are required to provide an industrial and technological benefits report annually. Also, most defence contracts are issued through Public Services and Procurement Canada, which tracks contracts through its own database.

10.42 Contractors' activities can be reported in their annual report only once the activities have been approved by Innovation, Science and Economic Development Canada as eligible to discharge the contractors' industrial and technological benefits obligations. Innovation, Science and Economic Development Canada has a service standard to review annual reports in 180 calendar days, 80% of the time, and verify that the activities have taken place to fulfill the contractors' obligations. If the activities are not approved, the contractors remain responsible for fulfilling the obligation.

Incomplete and inaccurate benefits data

Findings

10.43 We found that some fields in Innovation, Science and Economic Development Canada's Industrial and Technological Benefits database contained gaps and errors. For example, most procurements in the database did not include contract numbers. This meant that we could not reconcile the industrial and technological benefits information with the detailed contract information from Public Services and Procurement Canada. We could not confirm completeness of either data set because we also found that Public Services and Procurement Canada's database did not include all the contracts with industrial and technological benefits.

10.44 While Innovation, Science and Economic Development Canada conducted an annual manual reconciliation of contractors' obligation information and contract amendments, errors and gaps remained in some fields of the database. For example,

- there were inconsistencies between the industrial and technological benefits obligation value reflected in the database and the contract, including 1 being understated by almost 50%, representing a $33-million understatement of the obligation
- most contracts that we sampled had inaccurate values in the database

10.45 We also found that Innovation, Science and Economic Development Canada did not include all the industrial and technological benefits–related procurements within its database. The department's intention was to enter information on all defence procurements in the database even when a decision was made to not apply the policy. These procurements should be marked with a status—Industrial and Technological Benefits do not apply. However, this was not always done; therefore, the rationale to not apply the policy was not always documented or tracked by Innovation, Science and Economic Development Canada. This contributed to the difficulty in determining the effectiveness of the policy and the completeness of its application.

Recommendation

10.46 To improve the accuracy of data, tracking, and reporting for the Industrial and Technological Benefits Policy, Innovation, Science and Economic Development Canada, in collaboration with Public Services and Procurement Canada and National Defence, should ensure appropriate controls are in place for completeness and accuracy of the information in the databases and reporting.

Innovation, Science and Economic Development Canada's response. *Agreed.*

See **Recommendations and Responses** at the end of this report for detailed responses.

Improvement to the service standards calculation required

Findings

10.47 We found that Innovation, Science and Economic Development Canada had not established a service standard for approving the eligibility of activities proposed by contractors, to discharge their industrial and technological benefits obligations. Our calculation showed that it took Innovation, Science and Economic Development Canada on average 107 days to confirm the eligibility of activities. This waiting created a burden and pressure for contractors to meet their obligations.

10.48 Contractors must also submit an annual report detailing activities completed to fulfill their obligations. The department has a service standard target to verify the report's content within 180 days of receipt, 80% of the time. Although we found the service standard was met each year, we also found that the calculation could be improved.

10.49 We found that the service standard calculation started only when the acknowledgement letter was sent to the contractor, as opposed to when the annual report was received by Innovation, Science and Economic Development Canada. According to the department's process, the acknowledgement letter should be sent within 10 days of receiving an annual report. However, we found that, from July 2020 to March 2024, the average time to send the letter was 42 calendar days, ranging from 1 to 336 calendar days.

10.50 Once the acknowledgement letter was sent, Innovation, Science and Economic Development Canada established a verification plan to review the activities included in the annual report. On average, during the period between July 2020 and March 2024, the department took 33 days to establish how it would verify the information provided, ranging from 1 to 211 days. The verification plan includes the use of a risk assessment tool to determine the appropriate method for verifying activities. For example, activities could be verified through a desk review, a phone call, an email, or an on-site visit. We found that the results from the risk assessment tool were rarely followed, and that the verification method used was always less rigorous. Given that our audit period included the coronavirus disease (COVID-19) pandemic, it is understandable that different approaches had to be adopted. However, in our view, obstacles to on-site visits have been reduced in recent years, and the method identified by the risk assessment tool should be followed.

10.51 Also, in its service standard calculation, Innovation, Science and Economic Development Canada excluded time, known as "stopping the clock," for several reasons. These reasons could be due to the contractor, such as not providing a response after 10 days to an information request, or due to the department, such as internal system maintenance. Prolonging the review time meant that contractors had less time to identify alternative activities to meet their obligations if their submitted activities were not approved.

10.52 We also found that, at the time of our audit, Innovation, Science and Economic Development Canada had not publicly reported its performance against its 180-day service standard since the 2016–17 fiscal year.

Recommendation

10.53 To help identify where improvements could be made in the process to verify industrial and technological benefits obligations, Innovation, Science and Economic Development Canada should review its service standards and how it calculates its performance against them by

- using the received date instead of the acknowledgement date
- implementing a service standard for confirming the eligibility of activities
- not subtracting days that are within its control
- making the current average time for this process available to contractors

Innovation, Science and Economic Development Canada's response. *Agreed.*

See **Recommendations and Responses** at the end of this report for detailed responses.

No tracking of potential policy impacts on defence procurement

Why this finding matters

10.54 Public funds need to be used economically, effectively, and efficiently to achieve results. Additional cost and delays could affect the acquisition of the goods and services needed by the military.

No assessment of policy's impacts on timing and cost of defence procurements

Findings

10.55 We found that in most of the procurements we reviewed, contractors' costs to administer the industrial and technological benefits requirements were not made explicit in bids or in contracts. As a result, we could not determine the overall impact on prices paid for goods or services or the extent of additional costs or other impacts due to application of the Industrial and Technological Benefits Policy on defence procurements. However, with information provided by National Defence officials and Public Services and Procurement Canada, we found 6 defence procurements where applying the policy had an impact on the cost, timeliness, or competitiveness of the procurement.

10.56 For 3 non-competitive procurements, with contracts either signed or in negotiations, an increased cost was identified because of the requirements placed on the contractor to meet the policy. For 1 of the 3, a management fee for industrial and technological benefits, payable to the contractor, was included in a contract, representing 4% of the $9-million contract value. Given that the value of the 3 non-competitive procurements amounted to several billion dollars, management fees could therefore amount to hundreds of millions of dollars in costs as a result of applying the policy.

10.57 As well, for 2 of the 3 non-competitive procurements, the application of the Industrial and Technological Benefits Policy was 1 factor that contributed to negotiation delays. For 1 of them, the delay had already resulted in a year of slippage for the delivery of key military equipment. As a result, the Canadian Armed Forces' ability to have the right equipment when needed could be impacted.

10.58 For 3 other procurements, National Defence documentation showed that potential bidders did not apply at least in part because they thought that the industrial and technological benefits requirements in the request for proposal could not be met, or that it would be too risky to do so. If the number of bids received is reduced due to industrial and technological benefits requirements, this lessens competition and could have an impact on the price of the products and services.

10.59 Since its introduction, Innovation, Science and Economic Development Canada had not conducted a comprehensive cost-benefit analysis of the Industrial and Technological Benefits Policy. While the department had completed a cost-benefit evaluation, only expenses incurred within the department for managing the policy were considered. The evaluation did not consider additional costs, like the cost of lost opportunity or management fees imposed by defence contractors.

Recommendation

10.60 Recognizing that there are many factors that contribute to the costs of defence procurements, Innovation, Science and Economic Development Canada, in collaboration with Public Services and Procurement Canada, should conduct a rigorous analysis to determine the costs of the Industrial and Technological Benefits Policy for the Government of Canada.

Innovation, Science and Economic Development Canada's response. *Agreed.*

See **Recommendations and Responses** at the end of this report for detailed responses.

Conclusion

10.61 We concluded that Innovation, Science and Economic Development Canada had not ensured that the Industrial and Technological Benefits Policy met its objectives, as part of the Defence Procurement Strategy, for contracts managed in partnership with National Defence and Public Services and Procurement Canada.

About the Audit

This independent assurance report was prepared by the Office of the Auditor General of Canada on the Industrial and Technological Benefits Policy. Our responsibility was to provide objective information, advice, and assurance to assist Parliament in its scrutiny of the government's management of resources and programs and to conclude on whether the Industrial and Technological Benefits Policy complied in all significant respects with the applicable criteria.

All work in this audit was performed to a reasonable level of assurance in accordance with the Canadian Standard on Assurance Engagements (CSAE) 3001—Direct Engagements, set out by the Chartered Professional Accountants of Canada (CPA Canada) in the CPA Canada Handbook—Assurance.

The Office of the Auditor General of Canada applies the Canadian Standard on Quality Management 1—Quality Management for Firms That Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements. This standard requires our office to design, implement, and operate a system of quality management, including policies or procedures regarding compliance with ethical requirements, professional standards, and applicable legal and regulatory requirements.

In conducting the audit work, we complied with the independence and other ethical requirements of the relevant rules of professional conduct applicable to the practice of public accounting in Canada, which are founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality, and professional behaviour.

In accordance with our regular audit process, we obtained the following from entity management:

- confirmation of management's responsibility for the subject under audit
- acknowledgement of the suitability of the criteria used in the audit
- confirmation that all known information that has been requested, or that could affect the findings or audit conclusion, has been provided
- confirmation that the audit report is factually accurate

Audit objective

The objective of this audit was to determine whether Innovation, Science and Economic Development Canada ensured the Industrial and Technological Benefits Policy met its objectives, as part of the Defence Procurement Strategy, for contracts managed in partnership with National Defence and Public Services and Procurement Canada.

Scope and approach

The audit focused on the management of the Industrial and Technological Benefits Policy on National Defence procurements of $20 million and more. This includes contracts awarded through competitive procurements, non-competitive procurements, including contractual arrangements (for example, the United States government's Foreign Military Sales program), and contract renewals

and extensions. The audit excluded Canadian Coast Guard procurements (worth less than 3% of the contracts with industrial and technological benefits, amounting to 4% of the value of industrial and technological benefits obligations).

The audit approach included document reviews, data analytics, sampling of procurement files, and interviews with organization officials.

We also performed data analytics on 2 data sets:

- 60 procurements worth more than $100 million
- 39 procurements worth between $20 million and $100 million

The approach also included 3 samples of defence procurements worth more than $20 million:

- 10 procurements with industrial and technological benefits obligations (4 selected at random, 6 selected based on risk)
- 10 procurements with no industrial and technological benefits obligations (5 selected at random, 5 selected based on risk)
- 3 procurements provided by departments with impacts of the Industrial and Technological Benefits Policy on the procurement

The results of these samples cannot be extrapolated across all defence contracts because our samples were not entirely randomly selected and there were issues with the accuracy and completeness of the databases maintained by the departments.

Criteria

We used the following criteria to conclude against our audit objective:

Criteria	Sources
National Defence equipment and services contracts awarded with a value over $100 million consistently include industrial and technological benefits obligations, and contracts awarded with a value between $20 million and $100 million are reviewed for possible application of the policy. This includes non-competitive procurements.	• Industrial and Technological Benefits Policy, Innovation, Science and Economic Development Canada • Defence Procurement Strategy, Public Services and Procurement Canada • Policy on Results, Treasury Board • Directive on Results, Treasury Board • Industrial and Technological Benefits Policy: Value Proposition Guide, Innovation, Science and Economic Development Canada

Criteria	Sources
Innovation, Science and Economic Development Canada has a strategy to measure the achievement of all the Industrial and Technological Benefits Policy objectives.	• Industrial and Technological Benefits Policy, Innovation, Science and Economic Development Canada • Defence Procurement Strategy, Public Services and Procurement Canada • Policy on Results, Treasury Board • Directive on Results, Treasury Board • Industrial and Technological Benefits Policy: Value Proposition Guide, Innovation, Science and Economic Development Canada
Innovation, Science and Economic Development Canada collects valid, reliable and useful data to evaluate contractors' fulfillment of their obligations and to measure their results.	• Industrial and Technological Benefits Policy, Innovation, Science and Economic Development Canada • Industrial and Technological Benefits Policy: Value Proposition Guide, Innovation, Science and Economic Development Canada • Policy on Results, Treasury Board • Directive on Results, Treasury Board • Defence Procurement Strategy, Public Services and Procurement Canada
Innovation, Science and Economic Development Canada measures results against Industrial and Technological Benefits Policy objectives based on valid, reliable, and useful performance data.	• Industrial and Technological Benefits Policy, Innovation, Science and Economic Development Canada • Industrial and Technological Benefits Policy: Value Proposition Guide, Innovation, Science and Economic Development Canada • Policy on Results, Treasury Board • Directive on Results, Treasury Board • Defence Procurement Strategy, Public Services and Procurement Canada
Innovation, Science and Economic Development Canada ensures that the gender and diversity mandatory plans were included in the value propositions of bidders and reviewed under the Industrial and Technological Benefits Policy.	• Industrial and Technological Benefits Policy, Innovation, Science and Economic Development Canada • Industrial and Technological Benefits Policy: Value Proposition Guide, Innovation, Science and Economic Development Canada • Policy on Results, Treasury Board • Directive on Results, Treasury Board • Defence Procurement Strategy, Public Services and Procurement Canada

Criteria	Sources
Industrial and technological benefits obligations did not detract from the Defence Procurement Strategy's strategic goal to deliver the right equipment to the Canadian Armed Forces in a timely manner.	• Industrial and Technological Benefits Policy, Innovation, Science and Economic Development Canada • Policy on Results, Treasury Board • Directive on Results, Treasury Board • Defence Procurement Strategy, Public Services and Procurement Canada

Period covered by the audit

The audit covered the period from 1 April 2020 to 15 June 2024. This is the period to which the audit conclusion applies. However, to gain a more complete understanding of the subject matter of the audit, we also examined certain matters that preceded the start date of this period.

Date of the report

We obtained sufficient and appropriate audit evidence on which to base our conclusion on 14 November 2024, in Ottawa, Canada.

Audit team

This audit was completed by a multidisciplinary team from across the Office of the Auditor General of Canada led by Nicholas Swales, Principal. The principal has overall responsibility for audit quality, including conducting the audit in accordance with professional standards, applicable legal and regulatory requirements, and the office's policies and system of quality management.

Recommendations and Responses

Responses appear as they were received by the Office of the Auditor General of Canada.

In the following table, the paragraph number preceding the recommendation indicates the location of the recommendation in the report.

Recommendation	Response
10.25 Innovation, Science and Economic Development Canada should update and clarify the Industrial and Technological Benefits Policy and guidelines to include information about scope, application, and documentation requirements to support the consistent application of the policy to defence procurements.	**Innovation, Science and Economic Development Canada's response.** Agreed. Innovation, Science and Economic Development Canada (ISED) acknowledges the importance of documented decision-making and having in place established, detailed processes. Decisions regarding the application of the Industrial and Technological Benefits (ITB) Policy are made interdepartmentally on a case-by-case basis through the Defence Procurement Strategy (DPS) Governance, chaired by Public Services and Procurement Canada (PSPC) and with National Defence (DND) and ISED as core members. Regarding the 10 instances where the Office of the Auditor General of Canada indicates that the ITB Policy was partially or not applied, the procurements were leveraged through alternative methods like the Canadian Content Policy, which accomplishes similar goals by ensuring defence procurement dollars are spent in Canada and growing Canadian small and medium-sized businesses. While ISED has a guidebook and internal training, the Department recognizes the benefits of clarity on when the policy applies, or when other policies with similar goals are to be used. As a result, in July 2024, ISED developed a standardized assessment tool that records ISED's assessment as well as ISED's recommendations for internal decision-making. This assessment tool will be accompanied by guidelines concerning when and how the ITB Policy should be applied.

Recommendation	Response
10.36 Innovation, Science and Economic Development Canada should update its performance measurement framework to define specific indicators and targets to measure whether the Industrial and Technological Benefits Policy is meeting its objectives and use these measures to monitor the policy's performance.	**Innovation, Science and Economic Development Canada's response.** Agreed. Innovation, Science and Economic Development Canada (ISED) tracks specific indicators and targets to measure whether the Industrial and Technological Benefits (ITB) Policy is meeting its objectives. These ITB-specific indicators are found in the ITB Policy Annual Report, which provides an estimate of the Policy's impact on the Canadian economy (jobs and contribution to the gross domestic product by ITB recipients, Canadian suppliers to ITB recipients and consumer spending by associated employees), based on recognized international best practices. As per Treasury Board of Canada Secretariat guidelines, departmental reporting to Parliament focuses on providing parliamentarians with a clear understanding of the broader departmental results, which are typically achieved through the collective impacts of a range of programs and related activities. It is not the intent or the objective of Parliamentary reports to provide detailed performance information on individual programs and initiatives. As such, the performance impacts of the ITB Policy are not outlined in detail in ISED's Parliamentary reports. While the ITB Annual Report is based on international best practices, ISED acknowledges the report's findings and that further improvements could be made. ISED will review the existing suite of indicators tracked and reported both internally and publicly through the ITB Annual Report to determine how best to improve the specific measurement of ITB Policy objectives and outcomes, which the department has recently done with respect to Key Industrial Capabilities (KICs), as noted below.

Recommendation	Response
10.39 Innovation, Science and Economic Development Canada, in collaboration with National Defence, should ensure that the Key Industrial Capabilities align with Canada's defence needs. In addition, outcomes and indicators for Key Industrial Capabilities should be developed to measure their contributions to the Industrial and Technological Benefits Policy's results.	**Innovation, Science and Economic Development Canada's response.** Agreed. Innovation, Science and Economic Development Canada (ISED) recognizes the importance of supporting the readiness of the Canadian Armed Forces, and the Industrial and Technological Benefits (ITB) Policy's support for Canada's defence industrial base is a key component of that support. ISED's Key Industrial Capabilities (KICs) were developed after extensive consultation, including with the Department of National Defence. Close to 40% of the value of ITB obligations from Department of National Defence contracts is direct work on procurement, which supports the Canadian defence industrial base and, ultimately, the Canadian Armed Forces. Close to 95% of indirect ITB activity supports the defence, aerospace, space, land and marine ecosystem, bolstering the Canadian industry's resilience and its ability to meet future requirements. KICs are applied on Requests for Proposal following research, market analysis, and feedback from industry engagement completed as part of the Defence Procurement Strategy process. Since 2023, ISED has been measuring KICs as a share of associated ITB Obligation in terms of research and development, supplier development, exports, as well as skills and training. As of Fall 2024, ISED is publicly reporting on the impact of KICs resulting from Defence procurements to which the ITB Policy applies. ISED will work with the Department of National Defence to further support Canada's defence requirements by reviewing the list of KICs to enhance alignment between the operational requirements of the Canadian Armed Forces and other governmental priorities, while continuing to generate jobs and economic growth across Canada.

Recommendation	Response
10.46 To improve the accuracy of data, tracking, and reporting for the Industrial and Technological Benefits Policy, Innovation, Science and Economic Development Canada, in collaboration with Public Services and Procurement Canada and National Defence, should ensure appropriate controls are in place for completeness and accuracy of the information in the databases and reporting.	**Innovation, Science and Economic Development Canada's response.** Agreed. Innovation, Science and Economic Development Canada (ISED) is committed to ensuring that the data fields required to administer the Industrial and Technological Benefits Policy are up to date and accurate. Decision making and implementation of the Policy is a horizontal initiative with a shared responsibility for effective information collection, management and reporting. ISED will support and collaborate with its partners, including Public Services and Procurement Canada, to review and refine the process for documenting decisions, sharing procurement information to ensure completeness and accuracy across each department's databases and information management systems. ISED will also work to further modernize its processes and controls to ensure accurate tracking and reporting.
10.53 To help identify where improvements could be made in the process to verify industrial and technological benefits obligations, Innovation, Science and Economic Development Canada should review its service standards and how it calculates its performance against them by • using the received date instead of the acknowledgement date • implementing a service standard for confirming the eligibility of activities • not subtracting days that are within its control • making the current average time for this process available to contractors	**Innovation, Science and Economic Development Canada's response.** Agreed. Innovation, Science and Economic Development Canada (ISED) agrees with the importance of transparent and timely delivery of services. The Department has a service standard target to verify the reports' content within 6 months, 80% of the time. ISED is committed to meeting its service standards every year and has been doing so successfully since 2016-2017. In fact, for the audit period, ISED met its service standard in 86% of cases. That said, ISED acknowledges that there is opportunity to further improve the way service standards are calculated and communicated. ISED will review the current service standard guidelines including how they are calculated. Additionally, ISED will review the approvals process for transaction submission and explore the feasibility of adopting service standards for confirming the eligibility of transactions. The Department will update the Industrial and Technological Benefits website to publicly report on its performance related to the service standard.

Recommendation	Response
10.60 Recognizing that there are many factors that contribute to the costs of defence procurements, Innovation, Science and Economic Development Canada, in collaboration with Public Services and Procurement Canada, should conduct a rigorous analysis to determine the costs of the Industrial and Technological Benefits Policy for the Government of Canada.	**Innovation, Science and Economic Development Canada's response.** Agreed. Innovation, Science and Economic Development Canada (ISED) recognizes the importance of sound management of public funds. In defence procurement, as the report acknowledges, there are many factors that contribute to the costs of defence procurement. These factors can include market availability, inflation, contract structures, global supply chain limitations, procurement strategies, schedule constraints, and specific technical requirements and technological maturity, which can increase costs unpredictably. The Industrial and Technological Benefits (ITB) Policy's impacts on a procurement are intertwined with other government requirements, making it difficult to isolate and itemize costs. Notwithstanding these challenges, ISED will work with Public Services and Procurement Canada as the lead department on contracting to explore options to better identify the cost of the application of the ITB Policy.