



THE FISCAL IMPACT OF THE CANADIAN MISSION IN AFGHANISTAN

Statement by Kevin Page
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Good morning ladies and gentleman. Thank you for being here.

My role as the Parliamentary Budget Officer is to support Parliament in exercising its oversight of the government's stewardship of public funds. The Officer does so by ensuring budget transparency and promoting informed public dialogue. The Parliamentary Budget Officer is an independent position created by the Federal Accountability Act.

In this regard, I am here today to present the findings of a study examining the fiscal impact of the Canadian mission in Afghanistan. The study was requested by the Member of Parliament for Ottawa-Centre, in June 2008. All party leaders have provided their consent for this study to be available for public debate during the current election period.

This report on the incremental costs of Canada's mission in Afghanistan is the first comprehensive costing of its kind backed by a rigorous and accepted methodology. It covers the cost of running the military operations, aid and reconstruction costs, and the long-term cost of taking care of Canada's veterans.

The report released today is a financial analysis. Its purpose is not to assess - nor does it make recommendations on Canada's policy with regard to the Afghanistan mission.

I would like to highlight three key observations from the study.

- **One, estimating the fiscal impact of the Canadian mission is complex and difficult, but necessary.** It required the development of a sound methodology and the provision of relevant and reliable data for analysis.
- **Two, the estimated fiscal costs of the Canadian mission are financially significant.** Estimates from the Office of the Parliamentary Budget Officer range from \$7.7 billion to \$10.5 billion over the 2001-02 to 2007-08 period. When the period is extended to 2010-11, the cost is projected to range from \$13.9 billion to \$18.1 billion, assuming current deployment strength remains unchanged.

The total projected mission cost of up to \$18.1 billion over the 2001-02 to 2010-11 period, represents close to \$1,500 dollars per Canadian household.

- **Three, budgetary transparency for Parliamentarians and Canadians needs to be improved.** Although Canada is in the seventh year of the Afghanistan mission, Parliament and Canadians have not been provided with accurate and comprehensive departmental cost estimates.

Appropriate and adequate fiscal transparency in the Government's Estimates should require separate reporting on the mission by relevant departments. This reporting should be based on a common costing methodology and the explicit acknowledgment of the net present value of future liabilities related to veterans' benefits.

APPROACH

My Office undertook the following to estimate the fiscal impact of the Canadian mission in Afghanistan.

- First, the development of a methodology to capture the incremental fiscal costs to Canada's fiscal framework;
- Second, the estimation of incremental fiscal costs using the methodology with publicly available data, assumptions that are benchmarked on the experience of other countries (such as the United States) and statistical analysis. We call this a *top-down* approach.

The Report and methodology released today have been peer reviewed by an independent panel of distinguished international experts on accounting and the costing of military engagements. Going forward, the Office of the Parliamentary Budget Officer looks forward to working with federal government departments on a detailed, bottom-up financial costing.

The purpose of the methodology is to identify the *incremental* costs on an accrual accounting basis. [Accrual accounting records financial events based on economic activity rather than financial activity. Cash-based accounting recognizes income and expenses only when cash is received or paid out.]

Incremental costs represent those costs that are being incurred, and will be incurred by the government for the Canadian mission in Afghanistan. These costs would be equivalent to the fiscal savings to the Government of Canada (GC) had Canada not been involved in the Afghanistan mission. The various kinds of incremental costs can be broadly grouped under the following four headings:

- The cost of running the military operations;
- The cost of aid and reconstruction;

- The cost of taking care of veterans; and
- The cost of diplomatic efforts.

Our study focuses on the first three cost categories, as they represent the bulk of incurred costs. The methodology was developed, in part, by leveraging the experiences and best practices of organizations in other jurisdictions that have costed military engagements.

Incremental costs are distinguished from *full* costs, as reported by the Department of National Defence (DND) and various other sources, which include incremental costs plus steady state costs (i.e. costs that the government would have incurred regardless of the Afghanistan mission).

The broader economic and social costs to Canada resulting from the mission are considered outside the scope of this study. In this regard, the study does not provide an assessment of the economic opportunity costs that may have been lost as a result of expenditures on the mission, nor will it presume to put a monetary value on the heroic efforts of brave Canadian soldiers who have given up their life in service to Canada.

KEY OBSERVATIONS

The first observation to be highlighted from the study is that estimating the fiscal impact of the Canadian mission is complex and difficult. There have been many challenges including:

- **Distinguishing incremental costs related to the higher operational tempo of war from the more normal ongoing costs.** This means focussing on spending components like accelerated capital asset depreciation, capital reset costs, higher operational costs, like fuel, maintenance and danger pay, and higher veterans' benefits related to death and disability due to the theatre of war; and
- **Estimating the present value of future liabilities of veterans' benefits when the state of knowledge on issues like post traumatic stress disorder and the appropriate treatment are evolving.** Past experience on the incidence and severity of the problem may not provide useful benchmarks for the future.

The challenges in Canada for estimating the fiscal impact of the Afghanistan mission were further augmented by factors such as:

- **The lack of mission-specific Parliamentary appropriations by department;**

- **Second, the use of cash-based Parliamentary appropriations rather than an accrual-based system as called for by the Auditor General of Canada; and**
- **Third, the lack of consistency and transparency on methodology and cost information provided to Parliament in Departmental Performance Reports (DPRs) and Reports on Plans and Priorities (RPPs).**

To address some of these challenges, The Office of the Parliamentary Budget Officer has deployed a number of strategies and statistical methodologies:

- We engaged with the Department of National Defence (DND), Veterans Affairs Canada (VAC) and the Canadian International Development Agency (CIDA) to better understand methodology and data issues. We retained an international human resources and benefits advisory firm, Mercer Canada, to assist in calculating the estimated costs related to veterans' benefits;
- Second, we worked with publicly available data, used benchmark assumptions based on the experiences of partner countries. [These include assumptions related to the use of capital deployed in Afghanistan and the possible depreciation rates in the theatre of war, as well as assumptions related to projected deployments and the incidence and severity of injuries to soldiers. The range of reasonable assumptions used in this Report, result in a range of cost estimates.] We have reviewed our assumptions with the international group of experts that make up our peer review panel to ensure they were reasonable and that the data used were adequate and sufficient for a top-down estimation of costs.
- Third, it's important to note that certain costs, such as accelerated procurement of capital and danger pay, have been excluded from the study due to a lack of reliable data. This then suggests that the estimates provided may understate the costs of Canada's mission in Afghanistan.

The second key observation is that the estimated fiscal costs of the Canadian mission are financially significant.

Cost estimates provided by my Office are aligned with the methodology we are releasing today. The report is comprehensive in that it reflects military, reconstruction and development components as well as support for veterans. From a fiscal impact vantage point, the scope of this study is at least as comprehensive as exists in other countries that we have surveyed (such as the United States, Australia and the United Kingdom), and, perhaps broader with the inclusion of incremental veterans' benefits.

There are a number of cost estimates for Canada's mission in Afghanistan in the public domain. Comparing other figures with those in this report requires a careful comparison of methodologies and data used.

The estimated fiscal costs from 2001-02 to 2007-08 range from \$7.7 billion (\$5.9 billion for military operations; \$0.8 billion for veterans' benefits and \$1.0 billion for foreign aid) to \$10.5 billion (\$7.4 billion for military operations; \$2.1 billion for veterans' benefits and \$1.0 billion for foreign aid).

As noted earlier, the range in fiscal estimates reflects differing assumptions with respect to the capital employed in Afghanistan (4 and 8 percent of the DND adjusted capital base) and the level of incidence and severity of injuries related to the war (assumed to be 25 and 50 percent higher than the low estimate) calculated on a present value basis.

Assuming that the current average deployment of 2,500 Canadian soldiers until 2010-11 remains unchanged, the estimated incremental fiscal costs for the period from 2001-02 to 2010-11, range from \$13.9 billion to \$18.1 billion.

For illustrative purposes, an increase in deployed Canadian troops to an annual average of 3,500 would yield a range of \$16.2 billion to \$21.0 billion over the same period.

The third key observation is that budget transparency for Parliamentarians and Canadians needs to be improved.

Canada should strive to attain the best international practises of budget transparency. In this regard, it is the role of the Parliamentary Budget Officer to highlight examples of best practises and to inform Parliamentarians on how these practises could be achieved based on international experiences.

Budget and Estimates reporting to Parliament on Canada's mission in Afghanistan have not met any appropriate standard or best practice.

The Report notes that although Canada is in the seventh year of the mission, Parliament has not been provided with estimates by successive governments on the fiscal costs incurred by all relevant departments.

When compared with international experience, Canada appears to lag behind the best practices of other jurisdictions in terms of the quality and frequency of war cost reporting to their respective legislatures.

In this context, the next Parliament should consider the following three recommendations:

- One, that the next President of the Treasury Board and the officials of the Treasury Board Secretariat work with federal departments involved in the Afghanistan Mission and agree on a common methodology for costing the fiscal impact and make this methodology fully transparent to Parliamentarians and Canadians.

- Two, that detailed financial and non-financial information be used to generate fiscal costs on the Canadian Mission in Afghanistan using a published methodology and that these costs be reported in a consistent fashion to Parliament beginning with the 2009-10 Reports on Plans and Priorities (RPP) and Departmental Performance Reports (DPR). This would give Parliamentarians the information they need for an informed debate on the mission and enable them to undertake their oversight role with respect to the stewardship of public funds on behalf of all Canadians.
- Third, that the next Parliament move to an accrual-based appropriation system from the current cash-based appropriation system. This would provide greater fiscal transparency and a more informed parliamentary and public debate.

MOVING FORWARD

In conclusion, we hope that this study will support an informed Parliamentary and public debate within the broader context of Canada's role in Afghanistan and contribute to improved fiscal transparency.

I wish to thank the distinguished advisory group of international experts who provided their time and expertise in support of better parliamentary discourse. These individuals include: Dr. Nola Buhr, Professor at the University of Saskatchewan and Chair of the Public Sector Accounting Board; Dr. Michele Chwastiak, Associate Professor at the University of New Mexico, Dr. Douglas Bland, Professor at Queen's University and Chair of the Defence Management Studies Program, Frances Lussier at the U.S. Congressional Budget Office and Amy Belasco at the U.S. Congressional Research Service.