National Defence

Quarterly Financial Report (QFR) for the Quarter ended December 31, 2023

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Quarterly Financial Report for the Quarter ended December 31, 2023

1. Introduction

This quarterly report has been prepared by management as required by section 65.1 of the *Financial Administration Act* and in the form and manner prescribed by the Treasury Board. This report should be read in conjunction with the *Main Estimates – 2023–24 Estimates*, *Supplementary Estimates (A), 2023–24* and *Supplementary Estimates (B), 2023–24*. This report has not been subject to an external audit or review.

Strong, Secure, Engaged (SSE) is the defence policy that presents a vision of and an approach to defence for the government that will make Canada:

- **strong at home**, with a military ready and able to defend its sovereignty and to assist in times of natural disaster, support search and rescue, or respond to other emergencies
- **secure in North America**, active in a renewed defence partnership in the North American Aerospace Defense Command (NORAD) and with the United States to monitor and defend continental airspace and ocean areas
- **engaged in the world**, with the Canadian Armed Forces (CAF) doing its part in Canada's contributions to a more stable, peaceful world, including through peace support operations and peacekeeping

The department continues to carry out its mandate to achieve results related to 7 core responsibilities including Internal Services. A summary description of these core responsibilities can be found in the *Departmental Plan 2023–24.*

1.1 Basis of presentation

This quarterly report has been prepared by management using an expenditure basis of accounting. The accompanying statement of authorities includes the department's spending authorities granted by Parliament and the Treasury Board Secretariat which are used by the department consistent with the *Main Estimates, Supplementary Estimates (A)* and *Supplementary Estimates (B)* for the 2023-24 fiscal year. This quarterly report has been prepared using a special-purpose financial reporting framework designed to meet financial information needs with respect to the use of spending authorities.

The authority of Parliament is required before money can be spent by the government. Approvals are given in the form of annually approved limits through appropriation acts, or through legislation in the form of statutory spending authority for specific purposes.

The department uses the full accrual method of accounting to prepare and present its annual consolidated departmental financial statements, which are part of the departmental results reporting process. However, the spending authorities voted by Parliament remain on an expenditure basis. The main difference between the quarterly financial reports and the consolidated departmental financial statements is the timing of when revenues and expenses are recognized. The quarterly financial report includes revenues only when the money is received and expenses only when the money is paid out. The consolidated departmental financial statements report revenues when they are earned and expenses when they are incurred. In the latter case, revenues are recorded even if cash has not been received and expenses are incurred even if cash has not yet been paid out.

2. Highlights of fiscal-quarter and fiscal-year-to-date results

This section provides financial highlights and explanations for differences between the fiscal-quarter and fiscal-year-to-date results for the quarter ended on December 31, 2023, and the results of the same period last year.

2.1 Statement of authorities

When compared to those of the same period of the previous year, the department's year-to-date budgetary authorities available for use have increased by $1,542.0 million. As reflected in Table 1: Statement of authorities, the total budgetary authorities increased from $27,527.9 million in 2022–23 to $29,069.9 million in 2023–24. Major reasons for the changes are outlined below.

Year-to-date variances in authorities available for use (in millions of dollars)

Initiative	Operating (Vote 1)	Capital (Vote 5)	Grants and contributions (Vote 10)	Budgetary statutory authorities	Total variances*
Pay administration – Federal public servants and Canadian Armed Forces	773.0	0	0	163.4	**936.4**
Operation and sustainment (fleet maintenance) of military capabilities and operating requirements	490.9	0	0	0	**490.9**
Budget 2021 initiatives	72.6	58.6	0	(0.9)	**130.3**
Implementation of SSE	79.5	30.0	(2.5)	14.2	**121.2**
North Atlantic Treaty Organization 2030 Initiative	2.5	0	116.0	0.1	**118.6**
Ukraine Operation	291.8	0.2	(242.2)	8.6	**58.4**
Budget 2022 initiatives	42.3	0.7	1.5	6.5	**51.0**
Miscellaneous departmental requirements	(45.3)	(6.8)	6.9	58.9	**13.7**
Major capital equipment and infrastructure projects	(27.6)	31.0	0.1	(6.7)	**(3.2)**
Heyder-Beattie Class Action	(375.3)	0.4	0	(0.4)	**(375.3)**
Cumulative variance in authorities available for use	**1,304.4**	**114.1**	**(120.2)**	**243.7**	**1,542.0**

*A positive variance indicates an increase in year-to-date cumulative authorities available for use in the nine-month period ending 31 December 2023 as compared to the same period in 2022–23.
A negative variance indicates a decrease in year-to-date cumulative authorities available for use in the nine-month period ending 31 December 2023 as compared to the same period in 2022–23.

Note: Numbers may not add up due to rounding.

The 2023-24 **year-to-date net increase in authorities of $1,542.0 million** indicates an increase in cumulative authorities available for use in the nine-month period ending 31 December 2023 as compared to the same period in 2022–23. This can be explained by variances in funding for a number of initiatives:

- **Pay administration – Federal public servants and Canadian Armed Forces (increase of $936.4 million)**

  The increase is due to adjustments to the rates of pay and allowances for CAF members and adjustments made to the terms and conditions of service or employment of the federal public administration in various collective agreements.

- **Operation and sustainment (fleet maintenance) of military capabilities and operating requirements (increase of $490.9 million)**

  In order to provide ongoing support for operating and capital requirements, the department received additional funding to offset sustainment growth and the inflationary impact on the defence budget.

- **Budget 2021 Initiatives (increase of $130.3 million)**

  Funding for initiatives that were announced in Budget 2021 pertaining to:

  - NORAD Modernization Initiative
  - Funding to Support the North Warning System
  - Modernizing the department's information management and information technology systems
  - The North Atlantic Treaty Organization (NATO) Readiness Initiative and the NATO Contribution programs
  - Sustaining health services for the CAF
  - Addressing sexual misconduct and gender-based violence in the military

- **Implementation of SSE (increase of $121.2 million)**

  The net increase in funding is primarily related to incremental demands required to execute the overall SSE policy commitments, including funding requirements for the expansion of the CAF and civilian support and for capital investments.

- **North Atlantic Treaty Organization 2030 Initiative (increase $118.6 million)**

  The NATO 2030 initiative is part of the collectively adopted NATO 2030 agenda to guide NATO's existing and future activities and reinforce collective defence. The funding will be used for the expanded contributions to NATO (Budget 2023).

- **Contributions to the Ukraine Operation (increase of $58.4 million)**

  The increase is due to Supplementary Estimates (B) 2023-24 funding to support Ukraine in its efforts to defend its sovereignty and funding to reinforce Canada's support for Ukraine through Operation UNIFIER. In Supplementary Estimates (B) 2022-23, the department internally reallocated $250 million from Vote 1 to Vote 10 to provide additional military aid to Ukraine.

- **Budget 2022 Initiatives (increase of $51.0 million)**

  Funding for initiatives that were announced in Budget 2022 pertaining to:

  - Women and Diversity Healthcare
  - Funding to support Culture Change in the CAF
  - Military Justice Modernization
  - Funding for the Implementation of the United Nations Declaration on the Rights of Indigenous Peoples Act

- **Miscellaneous departmental requirements (increase of $13.7 million)**

  The net increase is due to miscellaneous funding variances. The net increase in statutory authorities is mainly due to an increase in contributions to employee benefit plans for military and civilians related to negotiated pay increases. The net increase is partially offset by a decrease in operating, primarily pertaining to the decrease in the Operating Budget Carry Forward received in 2023-24 compared to 2022-23.

- **Major capital equipment and infrastructure projects (decrease of $3.2 million)**

  The net decrease in funding is due to modifications to the multi-year spending profile of major capital equipment and infrastructure projects. These adjustments serve to align financial resources with project acquisition timelines.

- **Heyder-Beattie Class Action Final Settlement Agreement (decrease of $375.3 million)**

  The Heyder and Beattie class actions sought damages related to gender-based discrimination, sexual assault and sexual harassment. The funding has been used to continue to fulfil obligations and payments under the final agreement, including compensating claimants, the administration of claims, and the implementation of the restorative engagement program. The decrease is largely related to the timing of expected payments to claimants.

2.2 Departmental budgetary expenditures by standard object

When compared to those of the same quarter of the previous fiscal year, the department’s year-to-date total net budgetary expenditures have increased by $2,307.8 million. As reflected in Table 2: Departmental budgetary expenditures by standard object, the expenditures increased from $17,342.9 million in 2022–23 to $19,650.7 million in 2023–24.

Year-to-date variances in net budgetary expenditures (presented by standard object) (in millions of dollars)

Standard object	2023–24 Year-to-date used at quarter end	2022–23 Year-to-date used at quarter end	Year-to-date variance
Personnel	9,067.9	8,067.2	1,000.7
Acquisition of machinery and equipment	2,861.7	1,899.1	962.6
Professional and special services	3,425.0	3,186.0	239.0
Repair and maintenance	1,191.6	1,054.9	136.7
Acquisition of land, buildings and works	417.1	317.3	99.9
Transportation and communications	603.2	549.8	53.4
Rentals	477.5	445.5	32.1
Transfer payments	464.9	653.6	(188.7)
Other subsidies and payments	518.4	572.2	(53.9)
Other net minor items	800.1	800.9	(0.8)
Revenues netted against expenditures	(176.7)	(203.6)	26.8
Total net budgetary expenditures	**19,650.7**	**17,342.9**	**2,307.8**

Note: Numbers may not add up due to rounding.

Year-to-date **net increase of $2,307.8 million** is attributable mainly to the following:

- **Personnel (increase of $1,000.7 million)**

The increase in spending is primarily due to the general pay increase which impacted expenditures for retroactive pay, pension and tax payments.

- **Acquisition of machinery and equipment (increase of $962.6 million)**

The increase in spending was mainly due to the ramp up of production in shipbuilding and new Foreign Military Sales (FMS) cases. In addition, higher milestone payments and aircraft-related payment schedule timing differences has contributed to the increase in spending.

- **Professional and special services (increase of $239.0 million)**

The increase in spending is primarily due to extra dock work on submarines and frigates as well as the Strategic Tanker Transport Capability project in the implementation phase. Inflation has led to increased utility expenditures, and there was a rise in operating and maintenance costs for engineering and integration. Additionally, this year, there are higher milestone payments for various projects and an increase in expenditures in training packages and courses for apprentices.

- **Repair and maintenance (increase of $136.7 million)**

The increase in expenditures is primarily due to aircrafts having both higher yearly flying rate (YFR) and cost per YFR, as well as increase contract costs for repairs and overhaul of equipment and FMS cases. Additionally, extra dock work periods on ships have contributed to the increase in spending.

- **Acquisition of land, buildings and works (increase of $99.9 million)**

The increase in spending is primarily due to various minor construction projects, many of which are in different phases of construction.

- **Transportation and communications (increase of $53.4 million)**

The increase in spending is primarily due to payment timing differences for the Mercury Global telecommunication data services project and the impact of inflation. Additionally, travel increased due to training to maintain operational readiness, an increase in operations, new exercises, and inflation affecting flights, hotels, and meal costs.

- **Rentals (increase of $32.1 million)**

The increase in spending is primarily due to various application/software rental services, as well as payment for rentals on CAF operations.

- **Transfer payments (decrease of $188.7 million)**

The decrease in spending is primarily due to timing variances for the budget and expenditures related to Ukraine. This decrease is offset by an increase in NATO spending due to 2021 Brussels Summit taskings.

- **Other subsidies and payments (decrease of $53.9 million)**

The decrease in expenditures is primarily due to the timing of scheduled payments for settlement agreements.

- **Revenues netted against expenditures (decrease of $26.8 million)**

The decrease is primarily due to changes in the invoice and billing management of visiting military forces, the timing difference of revenue recognition and the reduction of revenue from rations and quarters.

3. Risks and uncertainties

The department's financial transactions are exposed to a broad range of external financial and economic risks such as inflation, foreign exchange commodity price fluctuations and global supply chain. Currently, we are seeing economic risks give rise to increases in costs of goods and services, labour shortages, and supply chain delays. Depending on how these risks unfold, they could lead to significant fluctuations in anticipated spending.

While the department considers key economic and financial risk factors (including defence-specific inflation and foreign exchange) in developing expenditure strategies, these risks are outside the control of the department.

The department continues to address the financial risks associated with Phoenix pay issues through the implementation of new controls as required and the strengthening of existing ones. The Civilian Quality Assurance program continues to leverage the use of robotic process automation to analyze the current pay environment and lead to more timely corrective actions with the help of compensation agents. Initiatives such as the centralized data entry capability continue to ensure sustained payment accuracy.

The department's capital acquisition program includes a number of large multi-year acquisition projects, mainly comprising of advanced fighter aircrafts, naval ships and armored vehicles. Delays in contracting and procurement activities or delays in deliveries by suppliers for individual projects can reduce the CAF operational capability and lead to reduced expenditures or budgetary surpluses.

Risks also flow from claims and litigations involving the department's normal operations. When the department receives a claim or litigation alleging liability in tort or extra contractual responsibility to cover losses, expenditures or damages, it is analyzed and an appropriate position is developed, based on legal advice. Litigation or settlement may be pursued and these are tracked through the department's reporting.

The COVID-19 pandemic exacerbated the CAF's ability to grow its Force. As a result, the CAF is applying reconstitution measures at the tactical, operational, and strategic levels to restore units to an acceptable level of readiness to excel as a modern and combat-ready military force. This is intended to enable the CAF to adapt quickly to action when called for significant unexpected operational demands, which can occur at any time anywhere around the globe.

Additionally, significant unforecasted operational demands can occur at any time, requiring the department to respond anywhere in the world. Depending on the extent of the operational demand, the cost of unforecasted operations would be mitigated either through internal reallocations or by requesting incremental funding from the government.

The government is currently refocusing its spending and has announced that this initiative will roll out in two phases. Phase 1 was announced in Budget 2023 with spending being refocused in professional services and travel as well as operations and transfer payments. Phase 2 was announced in the *2023 Fall Economic Statement* indicating that the government will expand its Phase 1 efforts. Specific details about Phase 2 are still being developed and are not yet known to the department. This creates future uncertainty in operations as the department works to implement its share of the planned spending reductions going forward.

4. Significant changes in relation to programs, operations and personnel

In October 2023, Hamas conducted an attack on Israel. This attack and the ensuing conflict between Israel and Hamas have resulted in efforts by the government to put in place measures to help Canadians get to safety, including assisted departures. The CAF were involved in transporting Canadian citizens, permanent residents and their families leaving the region.

Approved by:

// Original signed by //	// Original signed by //
Bill Matthews Deputy Minister of National Defence	Cheri Crosby, CPA, CMA Chief Financial Officer

Dated: 28 February 2024

Ottawa, Canada

National Defence

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Table 1: Statement of authorities (unaudited) for the quarter ended December 31, 2023

Amounts are expressed in thousands of dollars	Fiscal year 2023-24			Fiscal year 2022-23		
	Total available for use for the year ending	Used during the quarter ended	Year-to-date used at quarter-end	Total available for use for the year ending	Used during the quarter ended	Year-to-date used at quarter-end
	Mar 31, 2024*	Dec 31, 2023	Dec 31, 2023	Mar 31, 2023*	Dec 31, 2022	Dec 31, 2022
Vote 1 - Net Operating expenditures	**19,674,598**	**5,208,373**	**13,558,891**	**18,370,042**	**4,346,819**	**12,413,601**
Vote 5 - Capital expenditures	**6,072,854**	**1,888,392**	**3,753,518**	**5,958,765**	**1,136,365**	**2,832,373**
Vote 10 - Grants and contributions	**944,128**	**330,667**	**464,734**	**1,064,401**	**289,576**	**653,467**
Vote 15 - Payments in respect of the long-term disability and life insurance plan for members of the Canadian Forces	**446,728**	**112,694**	**282,436**	**446,728**	**105,974**	**284,432**
Budgetary Statutory Authorities:						
Contributions to employee benefit plans - Members of the Military	**1,573,859**	321,321	1,050,600	**1,321,784**	302,342	900,299
Contributions to employee benefit plans	**330,763**	82,660	247,957	**336,665**	83,950	251,840
Spending of Amounts Equivalent to Proceeds from Disposal of Surplus Crown Assets	**26,193**	270	349	**28,370**	474	1,446
Payments under the *Supplementary Retirement Benefits Act*	**550**	140	399	**800**	148	338
Court awards - *Crown Liability and Proceedings Act*	**0**	284,053	291,680	**0**	0	5,000
Payments under Parts I-IV of the Defence Services Pension Continuation Act (R.S.C., 1970, c. D-3)	**120**	29	81	**200**	32	65
Minister and Associate Minister of National Defence - Salary and Motor Car Allowance	**95**	24	71	**93**	23	69
Total Budgetary statutory authorities	**1,931,580**	**688,497**	**1,591,137**	**1,687,912**	**386,969**	**1,159,057**
Total Budgetary Authorities	**29,069,888**	**8,228,623**	**19,650,716**	**27,527,848**	**6,265,703**	**17,342,930**
Non-budgetary Authorities	74,474	(2,254)	38,445	73,226	(785)	36,095
Total Authorities	**29,144,362**	**8,226,369**	**19,689,161**	**27,601,074**	**6,264,918**	**17,379,025**

*Includes only authorities available for use and granted by Parliament at quarter-end.

Note: Numbers may not add up due to rounding.

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Table 2: Departmental budgetary expenditures by standard object (unaudited) for the quarter ended December 31, 2023

Amounts are expressed in thousands of dollars.	Fiscal year 2023-24			Fiscal year 2022-23		
	Planned expenditures for the year ending Mar 31, 2024	Expended during the quarter ended Dec 31, 2023	Year-to-date used at quarter-end Dec 31, 2023	Planned expenditures for the year ending Mar 31, 2023	Expended during the quarter ended Dec 31, 2022	Year-to-date used at quarter-end Dec 31, 2022
Expenditures:						
Personnel	12,582,414	3,233,562	9,067,877	11,239,012	2,686,234	8,067,188
Transportation and communications	762,059	240,626	603,168	861,861	145,547	549,812
Information	28,043	4,461	16,142	26,372	5,437	13,814
Professional and special services	5,158,057	1,496,379	3,425,030	4,897,049	1,298,295	3,185,981
Rentals	702,343	175,483	477,531	729,852	153,715	445,473
Repair and maintenance	2,051,176	509,971	1,191,611	2,029,765	412,496	1,054,949
Utilities, materials and supplies	1,309,628	305,645	782,017	1,323,178	309,751	785,058
Acquisition of land, buildings and works	705,757	202,320	417,138	671,818	134,015	317,269
Acquisition of machinery and equipment	4,665,718	1,439,132	2,861,673	4,726,578	771,515	1,899,059
Transfer payments	944,798	330,837	464,914	1,065,401	289,756	653,569
Public debt charges	3,840	622	1,988	6,426	605	2,076
Other subsidies and payments	512,696	370,077	518,356	311,809	143,501	572,238
Total gross budgetary expenditures	**29,426,529**	**8,309,115**	**19,827,445**	**27,889,121**	**6,350,867**	**17,546,486**
Less Revenues netted against expenditures:						
Recoveries from Members	(168,688)	(40,076)	(104,204)	(163,427)	(44,131)	(115,644)
Recoveries from OGDs	(11,075)	(4,367)	(7,548)	(12,333)	(5,149)	(8,416)
Recoveries from Other Governments/UN/NATO	(93,659)	(17,872)	(20,605)	(98,194)	(15,435)	(36,194)
Other Recoveries	(83,219)	(18,177)	(44,372)	(87,319)	(20,449)	(43,302)
Total Revenues netted against expenditures:	**(356,641)**	**(80,492)**	**(176,729)**	**(361,273)**	**(85,164)**	**(203,556)**
Total net budgetary expenditures	**29,069,888**	**8,228,623**	**19,650,716**	**27,527,848**	**6,265,703**	**17,342,930**

Note: Numbers may not add up due to rounding.