

Board members present:

Clive Tucker (Interim Chair)
Jane Attwood
David Johnston
Marta Phillips
Marcine Waterman (Chief Executive)
Neil Swift (Director of Corporate Resources)

Others present:

Ian McPherson (Director of Compliance and Investigations) (items 1-6)
Matthew Rees (Director of Analysis and Reporting)
Malcolm Botting (Head of Governance)
David Galpin (Head of Legal)

1. Welcome, apologies, announcements and declarations of interest

- 1.1. The Chair welcomed Board members to the 10th SSRO Board meeting, and introduced David Johnston, who was attending his first Board meeting as a newly appointed non-executive member. The Chair noted that David brought with him a wealth of experience from the international aerospace and defence sectors, as well as from industrial services around the world.
- 1.2. No apologies had been received.

There were no declarations of interest

2. Minutes of 9th meeting of the Board

- 2.1. The minutes of the 9th meeting of the Board were approved as a correct record.

3. Chief Executive's report

- 3.1. Marcine Waterman, Chief Executive, presented her report to the Board, which provided an update to the Board on items not presented elsewhere on the agenda.
- 3.2. The Chief Executive noted that the additional funding required for the Defence Contracts and Analysis System (DefCARS) had not been agreed by the MOD at the time of the meeting. Approval for the higher than anticipated programme costs of the next stage of DefCARS was subject to an internal MOD business case that was being drafted by the SSAT.
- 3.3. The SSRO had received a positive response to the request from the Chair for contributions to the SSRO's forthcoming discussion paper on when, why and how to single source. All scheduled interviews had now been held, and several written contributions had been received. The SSRO would draw the contributions together and the report would be considered by the Regulatory Review Committee on 19 July. The discussion paper would be published following approval by the Chief Executive and interim Chair.

- 3.4. At its meeting in March 2016, the Board had agreed changes to the SSRO's existing maternity policy, and at this point requested that a review should be undertaken of the policies on paternity, adoption and shared parental leave and pay. The Executive Committee had now considered and made changes to the existing 'paternity leave and pay policy', 'adoption leave and pay policy' and 'shared parental leave and pay policy'.
- 3.5. The Chair had spoken at the RUSI Defence Acquisition Conference on 16 June 2016 on the subject of 'Single source procurement: what's working, what isn't and what needs to change'. The speech explored the benefits brought by the new single source regime; findings from monitoring QDCs; the move to multiple rates; and the Review of the Regulations. The speech had been well received, and had generated discussion with stakeholders.
- 3.6. The Board considered recent discussions with the MOD regarding the SSRO's compliance role, and the Chief Executive presented the key messages from the Interim Compliance Statement, which was due to be published in July 2016. Following discussion on the content, presentation and timing of the statement, it was agreed that the SSRO would share the statement with named parties before the report was published. The press statement would be clear that parties would have an opportunity to correct issues before the full compliance report was published in January. The Board delegated to the Chief Executive and interim Chair the approval of a final version prior to publication.

The Board:

- a) **delegated final approval of the interim compliance statement to the Interim Chair and Chief Executive; and**
- b) **noted the information provided in other sections of the report, including meetings with stakeholders, publications and the updated adoption and paternity policy.**

4. Baseline profit rate

- 4.1. Matthew Rees, Director of Analysis and Reporting, introduced the report on the baseline profit rate. The Director of Analysis and Reporting presented the Board with the recommendations set out in the cover report concerning the proposed six baseline profit rates, their method of calculation and application, and the approach to setting the 2017/18 SSRO funding adjustment.
- 4.2. The Board had resolved at its 18 May 2016 meeting that the SSRO should recommend the six rates that it had developed ahead of the receipt of statutory guidance from the Secretary of State in January 2016. The report set out the proposed six rates, their method of calculation and application, and the approach to setting the 2017/18 SSRO funding adjustment. The report also contained a consultation document on the proposed rates, which would be issued subject to the Board's agreement.

- 4.3. Industry had raised a number of questions relating to the search strategy, the turnover threshold, the choice of average and the company credit rating used in the process of calculating the BPR. A workshop with stakeholders had been held on 15 June 2016, which addressed all of these issues.
- 4.4. Section 19(2) of the Act required the SSRO to provide the Secretary of State with its assessment of the appropriate funding adjustment rate, with up to half of its funding being derived from deductions to the price payable under QDCs from 2017. The Board approved the consultation document, which included the methodology for calculating the adjustment as set out in the paper, as well as the wider methodology for calculating the six baseline profit rates.
- 4.5. The proposals would be consulted on in the summer, and the Board would be asked to consider consultation responses and approve the final methodology at its September 2016 meeting. The Board would then be asked to make an assessment of appropriate profit rates in January 2017, in order to make recommendations to the Secretary of State in advance of the statutory deadline of 31 January 2017.

The Board:

- a) considered the methodology to calculate the six BPRs and the SSRO funding adjustment to apply in 2017/18;**
- b) considered the updated 'Step 1' and 'Step 4' in the process for adjusting the baseline profit rate to apply in 2017/18; and**
- c) approved the draft consultation document, and delegated to the Chair and Chief Executive authority to approve the final document and the illustrative methodology and guidance documents for publication.**

5. Single Source Cost Standards

- 5.1. Ian McPherson, Director of Compliance and Investigations, introduced the report regarding the SSRO's updated guidance on Allowable Costs, the Single Source Cost Standards. The SSRO was required by Section 20(1) of the Defence Reform Act 2014 to issue guidance on Allowable Costs for qualifying defence contracts. The SSRO first published its Single Source Cost Standards in January 2015.
- 5.2. The Single Source Cost Standards had been updated to reflect the SSRO's experience of qualifying defence contracts and qualifying sub-contracts, as well as the feedback it had received through meetings with industry and its helpdesk. Following the SSRO's recent consultation on the document, and a review of interaction with the sector over the last 18 months, an updated version of the guidance had been drafted.

- 5.3. The new version restructured the format of the guidance to enhance both clarity and understanding, and to reduce repetition. The updated guidance also: made a distinction between marketing and sales costs and bid costs; articulated the distinction between risk being treated as a potential Allowable Cost and the risk that may be subject to an adjustment to the Baseline Profit Rate; merged areas with common topics to avoid repetition and inconsistency; and clarified that when the qualifying sub-contract is awarded the burden of proof shifts from the prime contractor to the sub-contractor.
- 5.4. The Board approved the updated Single Source Cost Standards, and the revised guidance would be published on 1 July 2016.

The Board:

- a) **noted the issues that have been raised through the helpdesk;**
- b) **noted consultation responses received and our recommendations highlighted in the slide deck at Appendix 1;**
- c) **approved the updated Single Source Cost Standards; and**
- d) **delegated approval of the production and issuing of a consultation response document and the issue of the final guidance to the Chief Executive and Interim Chairman.**

6. Wage inflation analytical request

- 6.1. Matthew Rees, the Director of Analysis and Reporting, introduced the interim findings of the SSRO's research on wage inflation. In December 2015, the Secretary of State had asked the SSRO to carry out research into current and future wage inflation in single source contracts under Section 37 of the Defence Reform Act. The purpose of the analysis was to: assess defence sector wage inflation relative to other industries and the wider UK economy; understand the drivers behind industry wage inflation; and provide a knowledge base on wage inflation and policy to support the setting of future wage inflation estimates in single source contracting.
- 6.2. The research had been conducted from March to June 2016, incorporating a survey of suppliers, interviews with suppliers and the MOD, and analysis of other data on earnings and pay awards. There had been a disappointing response from industry to the SSRO's invitation to participate in the work, and the SSRO used publically available information from company accounts to support the analysis, which was a robust source of data.
- 6.3. The Director of Analysis and Reporting set out the findings of the research, and the Board discussed the report. The Board agreed that it was excellent work, asked detailed questions and suggested that a case study could be produced alongside the report. The Board agreed that the SSRO should publish the findings, in agreement with the Secretary of State, by the end of July.

The Board:

- a) considered and commented on the analysis, findings and recommendations presented in Appendix 1;**
- b) approved, and provided direction to the study team on, the presentation of findings to the MOD; and**
- c) delegated authority to the Chair and Chief Executive to approve the final report for publication.**

7. Monitoring the impact and performance of the regime

- 7.1. Matthew Rees, the Director of Analysis and Reporting, introduced a report that contained a proposal for monitoring the impact and performance of the regime, further developing the ten factors considered by the Board in October 2015. It proposed how these could be monitored and set out where further work was required, and provided some early lead indicators on performance.
- 7.2. The report proposed that the SSRO should publish the measures it would use to monitor the impact and performance of the regime. The SSRO would publish its monitoring of impact and performance in order to provide a transparent and up to date commentary on the regime as part of its work to review the Act and Regulations.
- 7.3. The report did not recommend publishing 2015/16 data, because the small amount available did not lend itself to credible judgements about the regime. The SSRO should be in a position to publish this information in June 2017. The Board agreed that it was not worth publishing this data at the current time.
- 7.4. The Board discussed the indicators within the report, and questioned whether international regulators had similar schemes. The SSRO agreed to write to international partners and inquire.

The Board:

- a) considered the proposals for monitoring the impact and performance of the regime;**
- b) approved the publication of the report that sets out the proposed measures and delegate to the Chief Executive and Interim Chair the final sign off of that document for publication;**
- c) noted the data available for 2015/16; and**
- d) agreed that given the paucity of data for 2015/16 it would not be appropriate to publish the regime's impact and performance this year.**

8. Annual Report and Accounts 2015/16

- 8.1. Neil Swift, Director of Corporate Resources, introduced the Annual Report and Accounts (ARA) for 2015/16, which was presented to the Board for its review and comment.
- 8.2. The Audit Committee had reviewed the ARA at its meeting on 8 June 2015, and recommendations from that meeting had been reflected in the final ARA presented to the Board. The Chair of the Audit Committee, Marta Phillips, reported that the Committee had noted that producing an interim ARA document and working with the NAO immediately after year-end had been a challenging target for SSRO staff but had worked well. The SSRO was on target for the ARA to be laid in Parliament before the summer recess. The Audit Committee considered the ARA to be a well presented and readable document, and extended its thanks to the team who had worked on the report and to the NAO and GIAA.
- 8.3. Having considered the Audit Committee minutes elsewhere on the agenda, the Board approved the ARA. The Audit Committee Chair was content to recommend the ARA to the Board and Accounting Officer.
- 8.4. Following the Board's approval, the document would be signed by the Chief Executive and issued to the Comptroller and Auditor General for final sign-off. The ARA would then be printed and laid in Parliament.

The Board:

- a) reviewed and approved the ARA 2015/16.**

9. Corporate Performance Report

- 9.1. Neil Swift, Director of Corporate Resources, presented the regular Corporate Performance Report to the Board. The report described how the organisation was delivering against its corporate priorities as at 31 March 2016. The report set out all relevant matters relating to the SSRO's performance, including progress against key performance indicators, budgetary updates and the delivery of corporate priorities with associated objectives and tasks.
- 9.2. Overall performance was on target and, where it could be measured against the KPIs in the SSRO's published Corporate Plan, had been rated 'green'.
- 9.3. Work during this period included publishing a final determination; launching a public consultation on the updated Single Source Cost Standards; work towards the wage inflation study; a call for input on the Review of the Act and Regulations; developing and procuring the successor to the DefCARS database; an further update to SSRO Answers; various meetings with industry and the MOD; conducting QDC analysis and compliance assessments; and managing a substantial number of helpdesk queries.

9.4. The Board discussed the content of the report, as well as the information provided and its presentation. It asked for the report to be developed to include more detail and information.

The Board:

- a) noted the progress to date; and**
- b) noted and commented on the updated appendices.**

10. Minutes from the Audit Committee

10.1. Marta Phillips, Chair of the Audit Committee, introduced the minutes from the last meeting of the Committee. The most significant item on the agenda was the ARA, which was reported on elsewhere.

10.2. The Committee had considered the Internal Audit Annual Report from GIAA, which provided substantial assurance that the SSRO's framework of governance, risk management and control was adequate and effective. It had also considered a paper on risk management, and the Committee continued to recommend a low risk appetite on all types of risk. The Board agreed that the SSRO's risk appetite should remain low.

The Board:

- a) noted the draft minutes.**

11. Any other business

11.1. The Chief Executive reported that it was likely that a referral for an opinion would be made in the coming weeks.

12. Date of the next meeting

12.1. The next meeting of the Board would take place on 26 September 2016 in Finlaison House.