

**Board members present:**  
George Jenkins (Chairman)  
David Johnston  
Marta Phillips  
Neil Swift  
Matthew Rees

**Others present:**  
Malcolm Botting  
David Galpin  
Ian McPherson  
Akhlq Shah (item 4)  
David Pottruff (item 5)  
Ben Johnson (item 6)

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## **1. Welcome, apologies, announcements and declarations of interest**

- 1.1. The Chairman welcomed members to the 16th meeting of the Board.
- 1.2. Apologies had been received from Terence Jagger and Marcine Waterman.

<p><b>There were no declarations of interest.</b></p>
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## **2. Minutes of 15<sup>th</sup> meeting of the Board and action tracker**

- 2.1. The Chairman introduced the minutes of the Board meeting held on 24 May 2017. Five actions from the meeting were recorded on the separate 'action tracker'.
- 2.2. The actions had been completed, and no other matters were arising.
- 2.3. The minutes of the 15<sup>th</sup> meeting of the Board were approved as a correct record.

## **3. Chief Operating Officer's report**

- 3.1. Neil Swift, Chief Operating Officer, presented his report to the Board, which provided an update on items not included elsewhere on the agenda.
- 3.2. The section in the report on stakeholder engagement provided a detailed update on the SSRO's progress against the stakeholder management strategy. The Board had previously asked for a full update to be provided every six months, but the Board stated that its requirements and the external environment had now changed. It therefore asked for a briefer version to be included in the Chief Executive's Report to the Board in future.
- 3.3. The SSRO had published two documents since the May Board meeting. These were the annual statistical bulletin on 12 June and the discussion paper on calibrating profit rates in single source contracts on 15 June. The Corporate Plan would be published shortly.

- 3.4. The last annual review of the Board's effectiveness had recommended that the Corporate Governance Framework and the Board's terms of reference should be amended to reflect a change to the Board's quorum. The Board agreed that paragraph 3.10 of the Corporate Governance Framework should be amended to: "At any meeting of the Board, the quorum will be three non-executive members present as a minimum, provided that more than half the members present are non-executive members". Following a recommendation from the SSRO's internal auditors, the Board terms of reference would include an additional sentence stating: "The Board's annual review of its effectiveness will include an assessment of whether quoracy at meetings of the Board and committees has been achieved".
- 3.5. The Chairman had written to the Secretary of State to submit the Board's final recommendations following the review of legislation. The proposed next steps would be for the SSRO to publish its recommendations in the autumn, as a response to its public consultation (in line with government guidance on such matters) and to facilitate ongoing engagement with stakeholders as the Secretary of State's review took place. The MOD had previously indicated that it would like to continue engagement on the details of the SSRO's recommendations with industry and the SSRO over the summer and autumn. MOD officials were due to write shortly with further information on this engagement.
- 3.6. The project to review the SSRO's statutory guidance on Allowable Costs was progressing, and three working papers had been circulated to stakeholders on cost accounting and financial reporting; Allowable Costs related to tangible and intangible assets; and individual cost types. There has been regular engagement throughout the project with the MOD and industry, as well as with professional bodies and the accountancy profession.
- 3.7. At its meeting on 21 March 2017, the Board had delegated to the Chairman the authority to appoint a Chair and members of the Regulatory Review Committee. The Chairman announced that he, Marta Phillips and the Chief Executive, Marcine Waterman, would be members of the Committee. The membership would be reconsidered once the current recruitment of additional non-executives had been concluded.
- 3.8. The SSRO had received the NAO's draft provisional audit findings on 'Improving value for money in non-competitive procurement on defence equipment', and was providing factual amendments to the draft before the NAO's deadline of 7 July.
- 3.9. The Board was provided with an update on the ongoing work to update the Wage Inflation study with a view to publication. **Action:** the Board would be provided with copies of the earlier versions of the report, for reference.
- 3.10. The Board asked about progress on responding to the points raised in the second staff survey and the development of an action plan to address them. **Action:** Progress on the staff survey would be reported to the September Board meeting.

#### **The Board:**

- a) considered and approved the amendment to the Board terms of reference and Corporate Governance Framework; and**
- b) noted the information provided in the report regarding stakeholder engagement, publications and events, the wage inflation study, guidance on Allowable Costs, the review of the legislation and membership of the Regulatory Review Committee.**

#### **4. Annual report on operation of the regime**

- 4.1. Matthew Rees, Director of Regulation and Economics, introduced a report setting out progress against the ten indicators that had previously been identified by the SSRO as a means of assessing the operation of the regulatory framework. The Board's guidance was sought on the content of the report, its publication and timing of its release.
- 4.2. The Board considered each indicator in turn, the data collected and conclusions drawn. The data for indicators 1-5 provided an indication of the extent to which reporting requirements were being complied with and how the provision of the regulatory framework was operating. The Board considered that these indicators provided a useful baseline for further analysis, with the data series developing as more information became available in the future.
- 4.3. The limited data for the remaining indicators did not currently allow the development of a similar baseline. The Board considered that these indicators would not assist the SSRO's understanding of whether the regulatory framework was operating as intended. The original aim of the indicator could not be met given the limited information available.
- 4.4. The indicator relating to compliance showed that 78 per cent of submissions were made by the deadline, increasing to 89 per cent within one month of the deadline. A significant number (1,877) of compliance queries had been raised with both contractors and the MOD on the quality of submissions. In 59 per cent of reporting queries these had been resolved with either no further action or a straightforward amendment to the original submission. The implementation of the DefCARS2 system was, in part, addressing compliance issues.
- 4.5. The Board considered the publication of individual contractor details as part of the report, and whether it was incidental or conducive to the SSRO's functions. It was agreed that individual contractor details should not be included in the published version of the report, but that the MOD should be informed of the SSRO's conclusions on individual contractors.

- 4.6. In discussion, the Board noted that care was needed with the presentation of the report to be clear that over the last year the operation of the regime had improved, largely as a result of the hard work of all involved in the regime. The SSRO should engage with stakeholders to allow for fact checking and consideration of wider context issues. Factoring time in for this further engagement meant that the publication of the report would need to be delayed to autumn 2017. Any delay in publication would be communicated through ongoing stakeholder engagement.
- 4.7. In the light of the report's findings and the operation of the regime to date the Executive should undertake a review of the approach to compliance work in the coming months to determine whether the efficiency or effectiveness of the work could be improved.
- 4.8. The Board delegated authority to the Chairman and Chief Executive to decide upon the content of the report for publication following engagement with stakeholders. Board members asked to see, informally, a developed version of the draft before publication. **Action:** a draft of the report would be shared with Board members.

**The Board:**

- a) **noted the progress against the ten indicators;**
- b) **considered which of the indicators it wished to include in the report;**
- c) **decided to not name individual contractors in a public report;**
- d) **considered whether there should be further engagement with the MOD on the content of the report;**
- e) **agreed the timeframe for publication of the report; and**
- f) **agreed that the Chairman and Chief Executive had delegated authority to decide upon the final content of the report for publication.**

**5. Risk study - update**

- 5.1. Matthew Rees, Director of Regulation and Economics, introduced a report updating the Board on progress with the study on the pricing of risk in single source defence contracts.
- 5.2. Concluding an informed, independent view on the pricing of risk in QDCs in the time available continued to pose a challenge given the level of stakeholder engagement to date and the limited evidence provided. The SSRO had made a formal request for information and would continue to reiterate the need for evidence to enable it to conclude the study.

- 5.3. The SSRO had adapted its initial study plans, and was revising the timetable initially agreed for this work. Work on the study had commenced in March, and the provisional report would be shared with stakeholders for comment in September. The SSRO was now working towards a November deadline, which matched well with the timetable for the Secretary of State's review of legislation.
- 5.4. The Board's attention was drawn to issues and risks associated with stakeholders' expectations about the scope of the work. The SSRO wished to better understand the evidence base underpinning proposals made by stakeholders, and there would be opportunities to discuss these further at meetings planned on 20 June and 19 July. In discussion, a view was expressed that the study should not state an opinion on the bandwidth of the cost risk adjustment. **Action:** The Chairman would seek to discuss the study in his forthcoming meeting with the Minister.

**The Board:**

- a) **noted the progress made on the risk study;**
- b) **noted the pressures on the study and the associated risks set out in the report; and**
- c) **noted that a provisional report of findings and recommendations would be presented to the SSRO Board in September; with publication of a final report expected in November 2017, following a period of consultation with stakeholders.**

**6. Baseline Profit Rate 2018/19**

- 6.1. Matthew Rees, Director of Regulation and Economics, introduced a report that made recommendations concerning the scope of work and approach to delivery for the baseline profit rate, capital servicing rates and funding adjustment for the financial year 2018/19. The report proposed that the existing methodology would be applied to assess the appropriate rates and adjustment for 2018/19, although the SSRO remained open to feedback. It also proposed the continuation of the successful in-house approach that was adopted in the previous year.
- 6.2. As in previous years, a 'composite rate' would be the SSRO's assessment of the appropriate BPR. The SSRO would calculate four profit rates for the 'develop and make', 'provide and maintain', 'ancillary services' and 'construction' activity types, with the composite rate derived from the 'develop and make' and 'provide and maintain' rates.
- 6.3. It was possible that the existing guidance on the application of the profit rate would require amendment driven by the outcome of the Secretary of State's review of the legislation. Engagement with stakeholders on the development of the guidance would begin in the autumn, alongside the calculation of the rates.

- 6.4. The work to recommend the rates had interdependencies with several of the SSRO's ongoing projects. The SSRO's study on risk was intended to provide the basis of the SSRO's thinking on the appropriate financial rewards for risk in contracts. The matter of risk contingency also had relevance to the guidance on Allowable Costs, which was being reviewed.
- 6.5. The Board discussed the procurement of access to data and external specialist advice. For the previous year, external specialist advice had been engaged to provide technical support to the project team and independent assurance on the SSRO's analysis to the Board. Options for external assurance for the new exercise were set out in the paper and the Board considered the issues, including whether a multi-year contract should be established, and agreed Option 5. The Board asked that quotes should be sought for external quality assurance, and that maximum value for money should be sought.

**The Board:**

- a) agreed to the application of the SSRO's published methodology to assess the appropriate BPR, CSRs and FA for 2018/19 and to seek ministerial support for this approach;**
- b) agreed that the SSRO should publish the underlying profit rates on its four activity types;**
- c) agreed to issuing a working paper on developments to the guidance in the autumn ahead of a formal consultation in December;**
- d) agreed to the procurement of data and quality assurance services to support assessment of the 2018/19 assessment in accordance with the procurement strategy set out in the report;**
- e) agreed Option 5 in Appendix 3 as the approach to external assurance for this project; and**
- f) noted the dependency on the delivery of updated guidance on the study on pricing of risk in single source defence contracts ('the risk study') and the Allowable Costs review.**

## **7. Annual Report and Accounts 2016/17**

- 7.1. Neil Swift, Chief Operating Officer, introduced a report presenting the Annual Report and Accounts 2016/17 to the Board for review and approval, before the document was submitted to the Comptroller and Auditor General. The Annual Report and Accounts had been presented to the Executive Committee on 5 June and Audit Committee on 12 June, and all revisions from the reviews by the Committees had been incorporated into the document at Appendix 1.

**The Board:**

- a) reviewed and approved the draft ARA 2016/17.

**8. Corporate Performance Report**

- 8.1. Neil Swift, Chief Operating Officer, introduced the report, which provided an update to the Board on how the organisation was delivering against its corporate priorities as set out in the Corporate Plan.

**The Board:**

- a) reviewed and commented on the Corporate Performance Report.

**9. Minutes from the Audit Committee meeting on 12 June 2017**

- 9.1. Marta Phillips, Chair of the Audit Committee, presented the minutes of the Audit Committee's meeting on 12 June 2017. The Committee had a full discussion on risk, and had asked the executive to reconsider the organisation's appetite for the risks set out on the corporate risk register.
- 9.2. The Committee had considered the annual report from the SSRO's internal auditors, GIAA, which had provided substantial assurance for 2016/17. The Committee acknowledged the outstanding performance by the whole organisation in achieving this. The Committee had also considered a positive report from the external auditor.

**The Board:**

- a) noted the draft minutes.

**10. Future Board agendas**

- 10.1. The draft agendas for Board and sub-committee meetings until December 2017 were presented to the Board.

**The Board:**

- a) Commented on the draft agendas.

**11. Any other business**

- 11.1. The Chairman provided an update on the recruitment process for additional non-executive Board members.

11.2. Following the meeting, there was a private discussion among the non-executive Board members.

**12. Date of the next meeting**

12.1. The next meeting of the Board would take place on 18 September 2017 at 2:00pm in Finlaison House.