

**Board members present:**

Jeremy Newman (Chair)  
Marta Phillips  
Clive Tucker  
Marcine Waterman (Interim Chief  
Executive)

**Others present:**

Malcolm Botting (minutes)  
John Sandhu

**Apologies:**

Jane Attwood

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**1. Welcome, Apologies and Announcements**

- 1.1. The Chair welcomed Board members and colleagues to the Extraordinary SSRO Board meeting.
- 1.2. Apologies had been received from Jane Attwood, who had submitted comments that would be fed into the Board's discussion.
- 1.3. There were no announcements or declarations of interest.

1.4. <b>There were no declarations of interest.</b>
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**2. Contract Profit Rate**

**a) Review Board for Government Contracts - recommended 2015 baseline profit rate**

- 2.2. John Sandhu introduced the item, outlining the steps taken by the Review Board for Government Contracts in its calculation of the baseline profit rate and capital servicing allowance.
- 2.3. Since the December Board meeting, the Chair and SSRO officials had met with the Review Board on three occasions, and with Deloitte twice. At the Review Board's 11 December meeting, it issued an indicative profit rate of 10.55 per cent, but this was heavily caveated as there remained unresolved issues. On 30 December, the Review Board met to finalise the profit rate following resolution of the final outstanding material issues. It subsequently released figures to the MOD and JRBAC, also on 30 December.
- 2.4. The Review Board's final 2015 baseline profit rate figure was 10.6 per cent. An addendum report was circulated to provide a longitudinal analysis of the baseline profit rate figure, showing the impact of the 3 year rolling average calculation on the headline figure.
- 2.5. In discussion, the Board considered the Review Board's process for setting the rate; the inclusion of companies within the reference group used to calculate the prevailing profit rate across UK industry as a whole; and the resolution of the

queries raised. The Board also considered the implications of the baseline profit rate being reduced from its previous level. The use of a 3 year rolling average had dampened the reduction in the rate.

**The Board approved the recommended rates to be submitted to the Secretary of State.**

**b) SSRO's due diligence, and review of Review Board's methodology and process**

- 2.6. The Board had agreed at its October 2014 meeting that the SSRO should request access to the methodology, model and data used to calculate the baseline profit rate and capital servicing allowance, so that the SSRO could conduct due diligence of the Review Board's processes.
- 2.7. Following a process of due diligence described to the Board, John Sandhu reported that he had been provided with adequate assurance on the process and data used to produce the baseline profit rate and capital servicing allowance. The methodology was documented, papers for the last three years had been provided, and where necessary pragmatic steps had been taken, with Review Board approval, to develop the methodology. As part of the due diligence, John Sandhu had undertaken a range of activities, including reviewing the data provided by Worldscope; requesting summary data to allow sensitivity analysis; and reviewing the formulae used to generate the baseline profit rate.
- 2.8. The Board discussed the due diligence, and potential developments to the process in future.

**The Board agreed that the steps taken provide an adequate level of assurance on the calculation of the rates.**

**c) SSRO's recommendation to the Secretary of State**

- 2.9. The Interim Chief Executive recommended to the Board that the Chair should write to the Secretary of State by the end of January stating that:
  - The SSRO had shadowed the work of the Review Board for Government Contracts in calculating a baseline profit rate and capital service allowance.
  - The SSRO would endorse the Review Board's recommended baseline profit rate of 10.6 per cent.
  - The SSRO would start work early in 2015 to conduct a full review of the principles and methodology used to calculate the baseline profit rate.
  - The SSRO would review a number of areas including: the principle of comparability; the exclusion of companies under price regulation; the inclusion of companies that are UK based but whose activities are predominately overseas; the use of R&D tax credits; and the use of simple rolling averages.

- 2.10. The Board discussed the content of the letter to the Secretary of State, as well as the process for reviewing the principles and methodology used to calculate the baseline profit rate. In discussion, it was noted that the method of calculation, once reviewed, should be fixed; it should not be revised yearly, unlike other statutory functions such as the Allowable Costs guidance.
- 2.11. As well as a letter to the Secretary of State, the SSRO was also required to issue guidance, which would be published on its website. The letter and guidance would both be dispatched by 23 January.

**The Board agreed the proposed content in the letter to the Secretary of State.**

### **3. Any other business**

- 3.1. Board members were informed of the requested timetable for their final review of the guidance on Allowable Costs, as well as the requirements for the first SSRO Senior Forum on 5 February.