

Board members present:

Jeremy Newman (Chair)
Jane Attwood
Clive Tucker
Marcine Waterman (Chief Executive)
Philip Davies (Director of Regulation)
Neil Swift (Director of Corporate Services)

Others present:

Justine Wharton (minutes)
Malcolm Botting
Sion Jones
Andy Mahon
Anton Hume

1. Welcome, Apologies and Announcements

- 1.1. The Chair welcomed Board members and colleagues to the extraordinary SSRO Board meeting.
- 1.2. Marta Philips sent her apologies and, in advance of the meeting, had submitted written comments on the papers to the Chair for consideration.
- 1.3. There were no announcements or declarations of interest.

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2. Profit methodology consultation

- 2.1. The Chief Executive introduced the profit rate methodology consultation. Section 19 of the Defence Reform Act 2014 ('the Act') stated that, for each financial year, the SSRO must provide the Secretary of State with its assessment of the appropriate baseline profit rate and capital servicing rates.
- 2.2. The Board resolved at its 8 December 2014 meeting that the SSRO should review the process for the calculation of an appropriate baseline profit rate from first principles and determine its own methodology. At the extraordinary Board meeting on 14 January 2015, the Board approved the questions the review should consider.
- 2.3. A workshop had been held on 31 July 2015, including members of the Board, SSRO officials and advisors. The workshop considered the review's findings and presented a range of options for consideration. The consensus at the workshop was that the current methodology was not suitable because one baseline profit rate was not appropriate for the different types of work involved. Following the workshop, this methodology had been developed further and set out in the consultation document.

- 2.4. The Director of Regulation summarised the proposed methodology contained within the consultation document, which was based on the principles for 'transfer pricing'. The proposed approach will be based on comparable work with several baseline profit rates proposed for different types of work. An overview was also given of the proposed set of principles on which companies would be included and excluded from the comparator set, and a summary was provided of the review's findings on international approaches.
- 2.5. The Board discussed the findings of the review and the proposed new methodology, including the issue of capital servicing allowance and use of simple rolling averages. The Board considered the risks inherent in this proposed new methodology and the required mitigation.
- 2.6. The Board was advised that the legal advice the SSRO had received to date stated that the Act did not preclude the Secretary of State from setting more than one rate, or the SSRO from making such a recommendation. This advice had been shared with the MOD.
- 2.7. The Board agreed that the proposed methodology was rigorous and better reflected the different levels of risk in different types of work. The Board was content that the approach to deciding which companies would be included or excluded from the comparator set was transparent and would further increase objectivity compared to the current approach. The Board requested that a question on the feedback form was re-drafted for clarity and noted a matter of inaccuracy in the table in Appendix 3.
- 2.8. The Board approved the draft consultation document, feedback form and questions. The Board delegated to the Chair and Chief Executive authority to approve the final document for consultation.

The Board:

- a) **considered the findings of the review;**
- b) **considered the proposed new methodology;**
- c) **approved the draft consultation document (Appendix 1) and delegated to the Chair and Chief Executive authority to approve the final document; and**
- d) **approved the draft consultation feedback form and questions, and delegate to the Chair and Chief Executive authority to approve the final document (Appendix 2).**

3. Agree next steps

- 3.1. The Board resolved that the draft methodology and approach should be presented to stakeholders at the Senior Forum to be held on 17 September 2015, and that a public consultation should be launched on 25 September 2015, which would run for eight weeks.

- 3.2. The Chief Executive outlined to the Board the communication plans for launching the consultation on 25 September. The Chief Executive informed the Board that the SSRO had engaged on the proposals with the MOD and HM Treasury. It was agreed that the MOD and HM Treasury would receive an embargoed copy of the consultation document.
- 3.3. The Board would review consultation responses and finalise the methodology at its December meeting. Following this, the Board would make its assessment of appropriate profit rates in January in order to make recommendations to the Secretary of State.

4. Date of the next meeting

- 4.1. The next meeting of the Board would take place on 2 October 2015 in Finlaison House.