

# SSRO

Single Source  
Regulations Office



## 2019 Annual Compliance Report

The SSRO is an executive non-departmental public body, sponsored by the Ministry of Defence.



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# Executive Summary

The regulatory framework introduced by Part 2 of the Defence Reform Act 2014 (the Act) requires transparency by contractors, establishing a statutory set of standardised reports. The data accumulated in the statutory reports may be used by the MOD to support procurement and contract management. It is intended to improve independent estimating for budgeting and challenges to contractor costs. The data should also inform discharge of the SSRO's functions in a way that delivers value for money and fair and reasonable prices. To achieve this, reports must contain the required data and that data must be good quality.

The SSRO must keep under review the extent to which persons subject to reporting requirements under the Act are complying with them. The [SSRO Data Strategy](#) identifies the link between this function and the use of data in support of the regulatory framework. The 2019 Annual Compliance Report presents our review of report submissions made for QDCs and QSCs entered into between 1 April 2015 and 31 March 2019. It includes all contract and supplier reports that were due for submission by 30 April 2019. The monitoring of report submissions was undertaken in line with our published [compliance methodology](#).

The SSRO had been notified of 214 qualifying defence contracts and qualifying sub-contracts as at 31 March 2019, 201 of which had made contract report submissions. These contracts were placed with a relatively small number of contracting companies, across a total of 69 Global Ultimate Owners (GUOs).

Our compliance approach includes consideration of the extent to which contractors are complying with their reporting obligations as well as using the submissions to understand what the reports disclose about how the Act and the Single Source Contract Regulations 2014 (the Regulations) are operating. In line with our methodology, we measure contractor compliance against statutory reporting requirements through two key performance indicators which consider the timeliness and the quality of report submissions.

The report finds that 72 per cent of contract report submissions and 71 per cent of supplier report submissions expected during 2018/19 were submitted in accordance with the reporting timeframes set out in the Regulations, which is below the SSRO's target of 75 per cent. The more frequent update reports were generally made on time while initial reports were more often delayed, although overall most contract report submissions were subsequently made within two months of the reporting deadline.

The strategic reports were, in general, less timely than other supplier reports. There have been several instances where expected Strategic Industry Capacity Reports (SICRs) have not been submitted, or have been provided by a group company rather than the Global Ultimate Owner. The MOD is working to change how relationships with these key suppliers are managed and intends the SICR to support this work.

There continue to be a minority of reports that have either not been submitted or have been submitted well beyond the timescales set out in the legislation. The MOD is able to take enforcement action in such cases and has reported to us that it issued four compliance notices in 2018/19. We continue to support contractors to submit reports, including through our help desk, guidance, on-boarding meetings and other compliance meetings. These arrangements have helped contractors to improve compliance. Our on-boarding meetings for new contractors and teams have had a positive impact on the timeliness of submissions. We have also improved the way data is collected through the Defence Contracts Analysis and Reporting System (DefCARS) by introducing a 'potential QDC/QSC' facility in DefCARS to help contractors commence their reporting obligations before a contract is entered into and by developing a training environment to support internal DefCARS training by contractors.

72% of contract report submissions and 71% of supplier report submissions expected during 2018/19 were submitted on time

The timeliness of contract report submissions is generally lower for companies based outside the UK

We will continue to offer this support and to make improvements to DefCARS in the future, but there is more action that can be taken to improve the timeliness of report submissions. It would assist if the MOD and contractors discuss and clarify reporting requirements at the contract negotiation stage. Emphasis should be placed on ensuring that non-UK based companies, where the timeliness of contract report submissions is generally lower, are aware of the reporting requirements before entering into a QDC or QSC and any perceived barriers to compliance should be addressed. The SSRO will seek to discuss performance with GUOs whose timeliness across all contracts is below average to better understand the causes behind the delays.

In 2018/19 we identified one or more potential issues in 69 per cent of the initial contract submissions made. As at July 2019, the SSRO had raised 758 issues about 2018/19 contract report submissions with contractors, of which 608 have subsequently been resolved. We have identified that the most common issues on contract reports relate to:

- reporting of contract prices (inconsistent prices reported in the same report and between reports for the same contract);
- output metrics (missing information or metrics not being linked to contract deliverables); and
- report submission administration (for example due dates of reports being reported incorrectly).

For supplier reports the most common issue relates to changes between actuals and future estimates and the average number of issues being raised per report is consistent with the prior year.

Overall, however, the number of issues raised on contract reports has reduced, with the average number of issues on initial contract reports halving since 2017/18. This is partly a result of the SSRO's updated approach to monitoring compliance where we now place greater reliance on automated validation checks

in DefCARS and on the MOD's reviews of submitted reports. The introduction of a greater range of validation warnings in DefCARS means that contractors are able to address issues before making a report submission and we hope the introduction of a third set of validation rules in May 2019 will continue this downward trend.

The SSRO has commenced a review of reporting requirements to consider the purpose behind the existing requirements, the use of the data and whether the requirements are proportionate. Initial topics include the reporting of contract amendments and variances, the defined pricing structure used in contract reports and the overhead reports. This work may help to improve the quality of report submissions in due course.

We carried out targeted reviews of two initial report submissions between December 2018 and March 2019 and issued a report to the MOD on this in May 2019. The report concluded that there is a clear place for the MOD's own checking of reports alongside the SSRO's compliance monitoring, given the MOD's knowledge of the subject contracts. This work provided insight into how the regulatory framework and the MOD's internal procedures were being applied and identified some issues with inconsistent reporting of contract prices, incorrect recording of reporting dates and incomplete cost recovery rates. We intend to continue with a programme of targeted reviews during 2019/20.

In July 2019 we published a working paper to commence a formal review of our compliance methodology. The review seeks to update the methodology to reflect developments that have taken place since it was published in early 2017, including changes in technology and approach. We are also considering how our approach to compliance monitoring may be improved, taking into account feedback from stakeholders. Any update to the methodology will be subject to public consultation in the Autumn. The current timetable is for publication of any revised methodology by 31 January 2020, with implementation from 1 April 2020.

The SSRO raised 758 issues with contractors, 608 of which have now been resolved.

The number of issues raised on contract reports has reduced overall and the average number of issues on initial contract reports has halved since 2017/18.

# Introduction

The SSRO must keep under review the extent to which persons subject to requirements under the Act are complying with them.

The SSRO's compliance methodology directly supports two of our statutory functions:

1. The requirement under section 36(2) of the Act to keep under review the extent to which persons subject to reporting requirements are complying with them.
2. The requirement under section 39(1) of the Act to keep under review the provision of the regulatory framework established by the Act and the Regulations.

In carrying out these functions, the SSRO must aim to ensure that:

- good value for money is obtained in government expenditure on qualifying defence contracts (value for money); and
- that persons who are parties to qualifying defence contracts are paid a fair and reasonable price under those contracts (fair pricing).

Single source contractors are required to submit statutory reports on each of their qualifying defence contracts (QDCs) and qualifying sub-contracts (QSCs). The SSRO has developed the Defence Contracts Analysis and Reporting System (DefCARS), with input from the defence industry and MOD users, to provide an easy to use, secure means of submitting the reports. The collection of data moved from an excel based submission process to the on-line version of DefCARS in March 2017. The majority of analysis presented in this report is drawn from the data submitted into the online version of DefCARS, as it focuses on 2018/19.

The reporting obligations apply to defence contractors, so their compliance is a significant focus of this report. The report considers the timeliness of report submissions, the issues identified from our review of submissions, associated themes, and actions that have been, or need to be, taken.

The SSRO also relies on the MOD's reviews of report submissions to inform its understanding of the extent to which

The 2019 Annual Compliance Report presents our review of report submissions made for 201 QDCs and QSCs entered into between 1 April 2015 and 31 March 2019. It includes all contract and supplier reports that were due for submission by 30 April 2019. The monitoring of report submissions was undertaken in line with our published compliance methodology (the methodology). Our approach includes consideration of the extent to which contractors are complying with their reporting obligations as well as using the submissions to understand what the reports disclose about how the Act and the Regulations are operating.

We measure contractor compliance against statutory reporting requirements through two key performance indicators:

1a) "All required reports have been submitted within the relevant deadlines".

1b) "Reporting obligations have been met for all reports submitted in accordance with the Regulations and relevant statutory guidance".

contractors are complying with the requirements of the regime. The report considers the nature and extent of issues identified by the MOD during the year. It describes the 'targeted reviews' that were piloted in 2018/19, which gave detailed consideration to a small number of reports and reviewed how the MOD had reviewed those reports.

As part of its compliance methodology, the SSRO typically raises queries arising from report submissions directly with contractors and, if these are not resolved, refers issues to the MOD. Issues raised with the MOD may involve both compliance with reporting requirements and the way in which the system of pricing contracts is being applied. The report includes analysis of issues referred to the MOD and a summary of the MOD's responses.

The SSRO has developed the Defence Contracts Analysis and Reporting System (DefCARS), with input from the defence industry and MOD users, to provide an easy to use, secure means of submitting reports.

# Reporting requirements

Defence contractors are required to submit two types of reports, contract reports and supplier reports, as summarised in Figure 1.

Our analysis refers to two types of contract reports, initial reports and update reports:

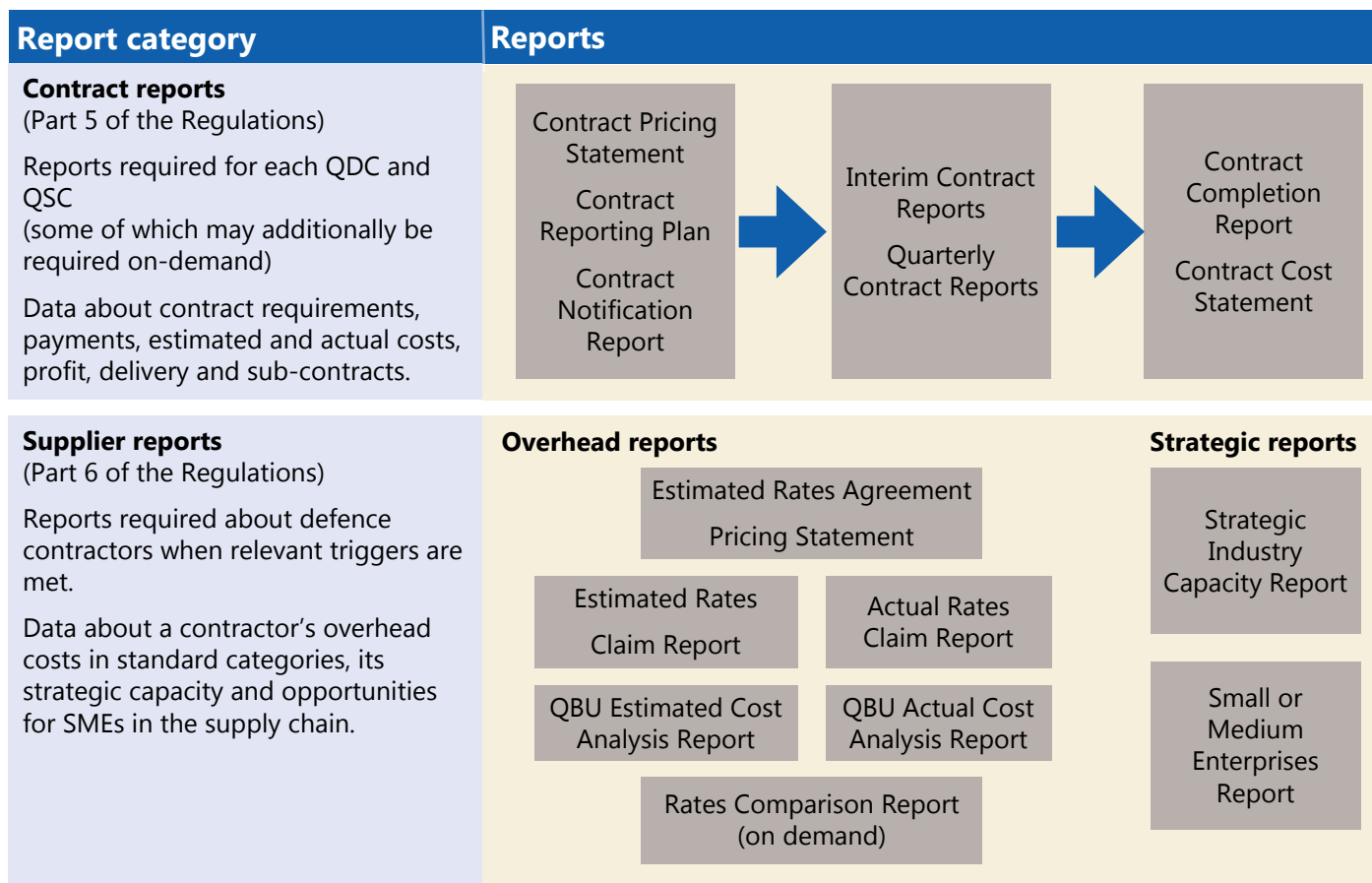
- 'initial reports' being the Contract Pricing Statement (CPS), the Contract Reporting Plan (CRP) and the Contract Notification Report (CNR), known collectively as the Contract Initiation Report (CIR); and
- the 'update reports' being the Interim Contract Report (ICR), the Quarterly Contract Report (QCR), the Contract Completion Report (CCR) and the Contract Costs Statement (CCS).

We also refer to two types of supplier report:

- 'overheads reports' being the Qualifying Business Unit Estimated Cost Analysis Report (QBUECAR), the Qualifying Business Unit Actual Cost Analysis Report (QBUACAR), the Estimated Rates Agreement Pricing Statement (ERAPS), the Estimated Rates Claim Report (ERCR), the Actual Rates Claim Report (ARCR) and the Rates Comparison Report (RCR) which is only triggered by a written notice from the Secretary of State; and
- 'strategic reports' being the Strategic Industry Capacity Report (SICR), and the Small or Medium Enterprises (SME) Report.

The reporting requirements are set out in Parts 5 and 6 of the Regulations. The SSRO supplements those requirements with reporting guidance, which contractors must have regard to when completing the reports.

**Figure 1: reports required under the regulatory framework**



\*In this table, and in the Regulations, "QBU" refers to a qualifying business unit.

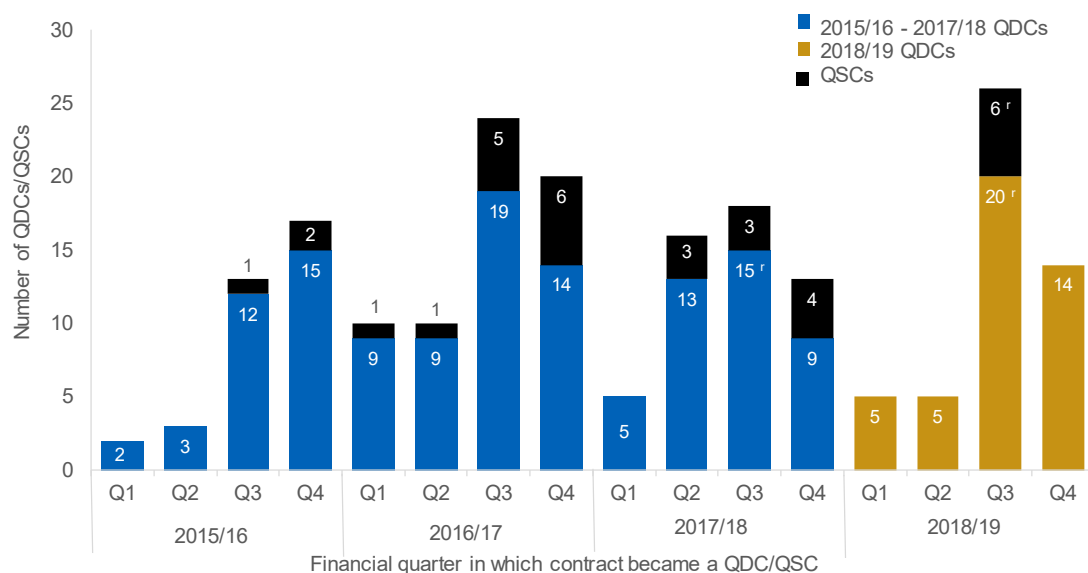
# Analysis included in the report

This report analyses reports submitted before the cut-off date of 30 April 2019. It includes analysis of:

- QDCs and QSCs entered into between 1 April 2015 and 31 March 2019 and notified to the SSRO by 30 April 2019; and
- associated contract and supplier reports due for submission by 30 April 2019.

As of the cut-off date, the SSRO had been notified of 214 QDCs and QSCs that had been entered into between 1 April 2015 and 31 March 2019. Of these, reports had been received by the SSRO for a total of 201 contracts. The key statistics relating to these contracts have been reported in the SSRO's [Annual qualifying defence contract statistics: 2018/19](#) and the detailed messages from that publication are not repeated here.

**Figure 2: Breakdown of QDCs and QSCs, where reports have been received, by quarter in which the contract became a qualifying contract**



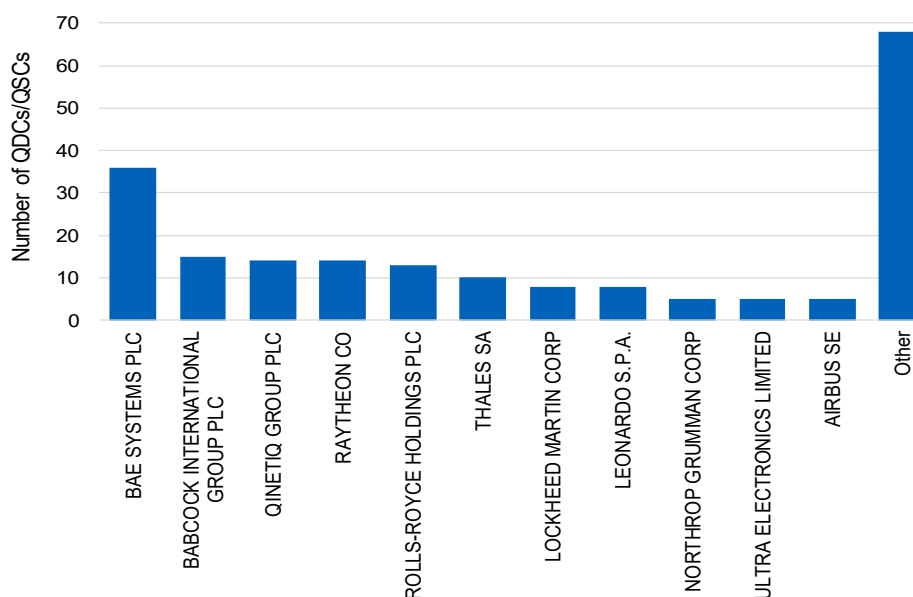
The number of contracts entering the regime has remained relatively consistent across the last two years, as shown in Figure 2. 50 qualifying contracts were entered into in 2018/19, in respect of which the SSRO has received reports, and 52 in 2017/18.

The 201 QDCs and QSCs for which reports had been received were placed with 98 individual contracting companies, across a total of 69 GUOs.<sup>1</sup> The MOD placed 66 per cent of qualifying contracts (equating to 133 contracts) placed with the top eleven GUOs or companies subsidiary to them. Figure 3 sets out the distribution of the 201 QDCs and QSCs placed by the MOD, showing the numbers of contracts awarded to the top eleven GUOs.

50 qualifying contracts were entered into in 2018/19

<sup>1</sup> The legislation refers to the 'Ultimate Parent Undertaking' to be consistent with the Companies Act 2006 which defines 'parent undertaking' and 'subsidiary undertaking', however contract reports do not identify the Ultimate Parent Undertaking. The SSRO uses the Global Ultimate Owner (GUO) definition from the Orbis database, provided by Bureau van Dijk.

**Figure 3: Number of QDCs / QSCs, where reports have been received, by Global Ultimate Owners**



The SSRO has grouped contracting companies into their respective GUO by considering whether the GUO controls a majority (greater than 50.01 per cent) of the voting rights of the company in question. Where a company has no single entity with a controlling majority, the company itself is considered the GUO of the corporate group.

The SSRO reviews the reports submitted by contractors and seeks to understand the information provided. Increasingly, the SSRO relies on automated validation checking in its DefCARS system and focuses more detailed, manual investigations around validation warnings that have not been addressed by the contractor. We recognise that ensuring the accuracy of reported information depends on the MOD also checking reported information and taking action where appropriate. We have enabled the MOD to raise queries with contractors in DefCARS and for contractors to respond, and this information is reviewed by the SSRO as part of the implementation of its compliance methodology.

We consider the extent to which persons subject to reporting requirements have complied with their obligations and what this tells us about how the regime is operating. To deliver our statutory aims and functions, we seek to achieve the following:

- good quality data from contractors, that is relevant, comparable and reliable;
- identification of issues related to meeting reporting requirements (reporting issues), to data quality and to the application of the regulatory framework, for example pricing control;
- a shared understanding with the MOD and contractors about identified issues; and
- appropriate action by the SSRO, the MOD and contractors to address issues. Action by the SSRO to address issues may include revised support to contractors, updated guidance, development of DefCARS and recommendations for legislative change.

Further detail on the data sources and methodology for inclusion of information in this report is detailed in Appendix 1.

We recognise that ensuring the accuracy of reported information depends on the MOD also checking reported information and taking action where appropriate



# Timeliness

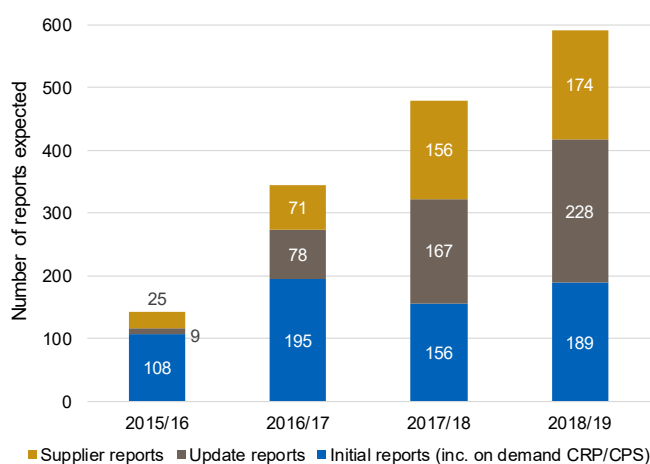
The first key indicator in the SSRO's compliance and review methodology relates to timeliness:

**1a) "all required reports have been submitted within the relevant deadlines" (SSRO KPI 75% of submissions by relevant deadlines)**

It is important that report submissions are made on time, firstly because this is a statutory requirement and secondly because the benefits to the regime can only be realised when there is a complete body of timely information available to benchmark and analyse.

## Contract reports

**Figure 4: Breakdown of the number of expected reports, by financial year the report was due**



For the 214 QDCs and QSCs reported as being entered into between the period 1 April 2015 and 31 March 2019, 1,130<sup>2</sup>, <sup>3</sup> contract reports, and 426 supplier reports<sup>4</sup> were due in accordance with statutory deadlines by the end of April 2019. During 2018/19, a total of 417 contract reports and 174 supplier reports were expected. Figure 4 details the breakdown of expected report by year.

**Table 1: Number of contract reports expected and submitted by report type, 1 May 2018 to 30 April 2019**

Report type	Number submitted	Number expected	Number submitted on time	% submitted on time
CIR	156	189	112	59
QCR*	159	168	144	86
ICR*	44	45	37	82
CCR*	4	5	1	20
CCS*	9	10	5	50
<b>Total</b>	<b>372</b>	<b>417</b>	<b>299</b>	<b>72</b>

\*update reports for where a CIR submission has not been made are not considered.

A total of 372 contract reports had been received by 30 April, as detailed in Table 1. Table 1 of Appendix 2 details the information requirements of the contract reports. 72 per cent of the total contract reports expected during 2018/19, based on the information reported by contractors, were submitted in accordance with the reporting timeframes set out in the Regulations.

<sup>2</sup> As required in line with Part 5 of the Single Source Contract Regulations

<sup>3</sup> Any references to initial reports include on-demand submissions

<sup>4</sup> As required in line with Part 6 of the Single Source Contract Regulations

## Supplier reports

Overheads reports may be required for a QBU in some years and not others, depending on whether the ongoing contract condition<sup>5</sup> and QBU threshold<sup>6</sup> are met. The SSRO does not have independent access to the information required to assess whether these requirements are met for a QBU and is dependent on notifications from the MOD and the contractor. The analysis therefore considers the timeliness of those submissions which have been received.

A total of 134 supplier reports had been received by 30 April, as detailed in Table 2. Table 2 of Appendix 2 details the information requirements of the supplier reports. 71 per cent of the total supplier reports expected during 2018/19, based on the information reported by contractors, were submitted in accordance with the reporting timeframes set out in the Regulations.

**Table 2: Number of supplier reports expected and submitted by report type, 1 May 2018 to 30 April 2019**

Report type	Number submitted	Number expected**	Number submitted on time	% submitted on time
QBU Estimated Cost Analysis Report and QBU Actual Cost Analysis Report (QBUCAR)	52	54	48	89
Estimated Rates Claim Report (ERCR)	21	25	20	80
Actual Rates Claim Report (ARCR)	22	25	21	84
Estimated Rates Agreement Pricing Statement (ERAPS)	19	25	18	72
Rates Comparison Report (RCR)	2	2	2	100
Strategic Industry Capacity Report (SICR)	10	21	7	33
Small or Medium Enterprises Report (SME)	8	22	7	32
<b>Total</b>	<b>134</b>	<b>174</b>	<b>123</b>	<b>71</b>

\*one additional SME report was submitted below UPU level

\*\*analysis is based on those supplier report submissions which have been received and consideration of their timeliness.

Table 2 shows that it is the two strategic supplier reports required by Part 6 of the Regulations, the SICR and the SME, which are most significantly delayed. The SSRO can more accurately assess whether the SICR and SME reports are required, as these depend on the ongoing contract condition alone and not the QBU threshold.

5 The "ongoing contract condition" is met in relation to a financial year if, at any time in that year, obligations relating to the supply of goods, works or services under one or more of the qualifying defence contracts referred to in subsection (4)(a) or (b) (as the case may be) are outstanding (s25(5) of the Act). Regulation 31(2) notes that this is subject to a minimum value of qualifying defence contract for reporting requirement to be imposed, and the amount specified for the purposes of that subsection is:

(a) for the financial years ending on 31 March 2016 and 31 March 2017, £20,000,000;  
 (b) for subsequent financial years, £50,000,000.

6 the total value of what it provides for those purposes in that period is at least £10,000,000.

## Analysis of timeliness

Figure 5 details submission timeliness on a 12-month rolling basis. It splits the contract reports into the initial reports and all subsequent update reports. This shows that the update reports, which are primarily made up of the QCR and ICR submissions, are generally made on time. By contrast, the CIR submissions have been delayed in more cases, which brings down the overall contract report submission timeliness. Figure 5 does not split the supplier reports into overhead reports and strategic reports, given the low number of strategic reports received, but it is clear from Table 2 that the SICR and SME reports are significantly less timely than the overall average for supplier reports.

**Figure 5: 12 month rolling average of report submission timeliness, by report type**

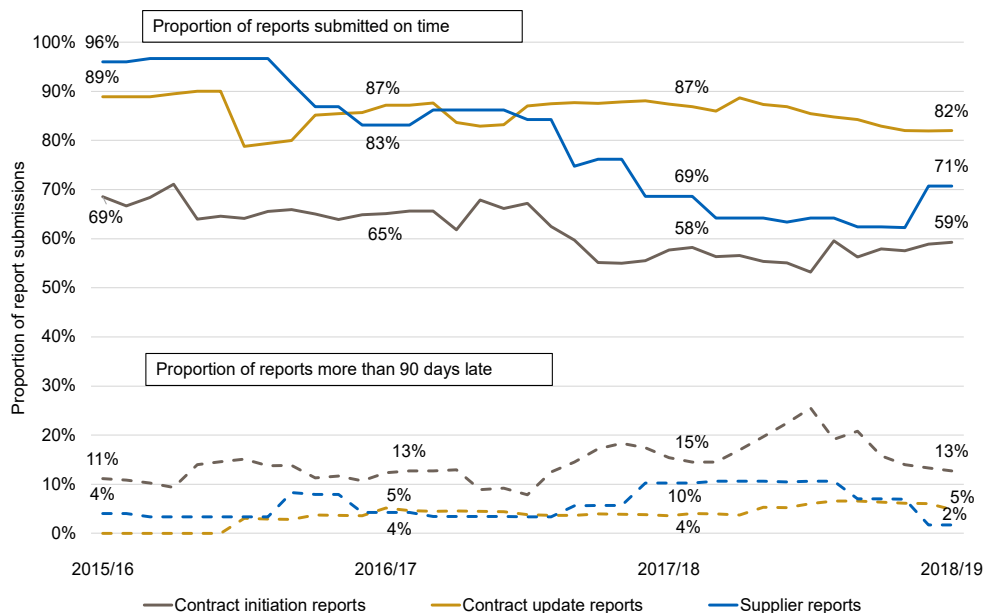
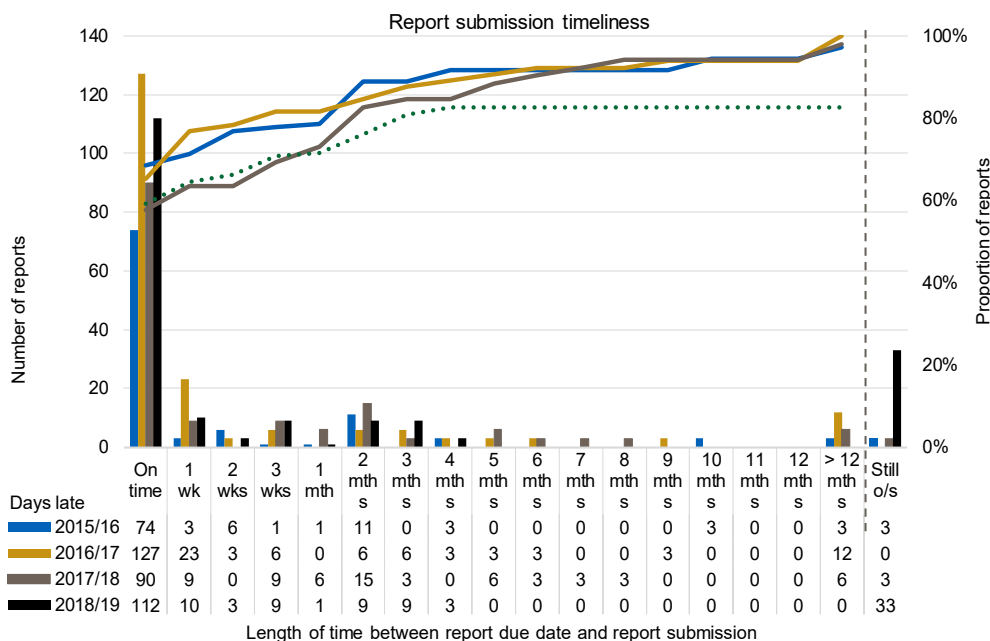


Figure 5 also shows the percentage of reports which are submitted over 90 days late. The proportion of contract reports submitted over 90 days late is consistent with prior years for each of the respective report types. Analysis on the length of delays by different report types is considered further below.

Most late submissions were made within two months of the reporting timeframes set out in the Regulations and only a few were delayed beyond this. When considering the delayed submissions, it is the initial reports that stand out as being submissions that consistently take longer to submit over the update reports, this can be seen

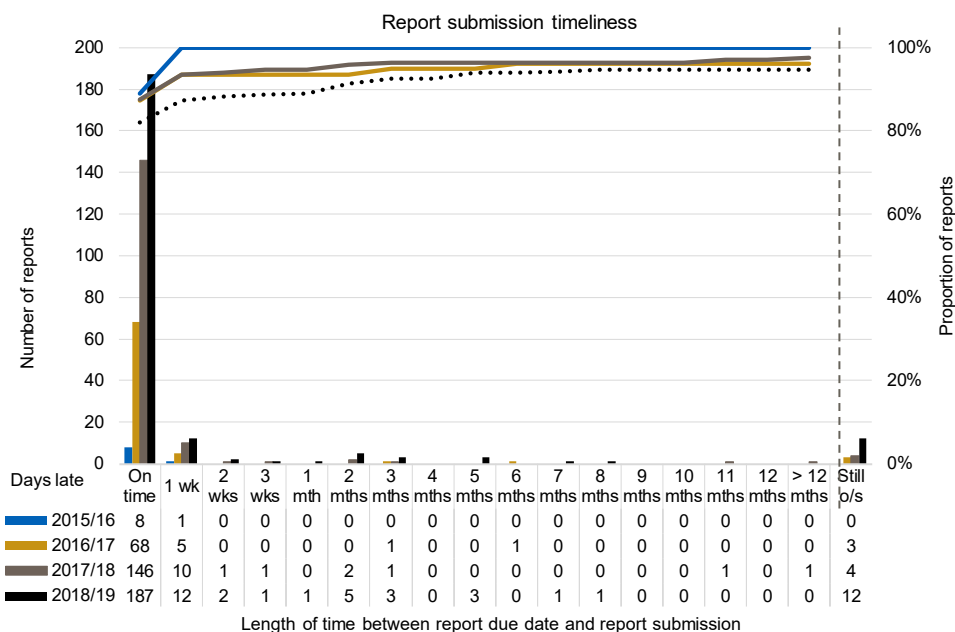
by analysing the timeliness of submissions for the different years that the reports were due. With respect to the supplier report submissions, it is the non-submission of SICR and SME reports that has caused the downward trend of supplier report timeliness over the last few years.

**Figure 6: Analysis of the timeliness of initial report submissions, by financial year report due**

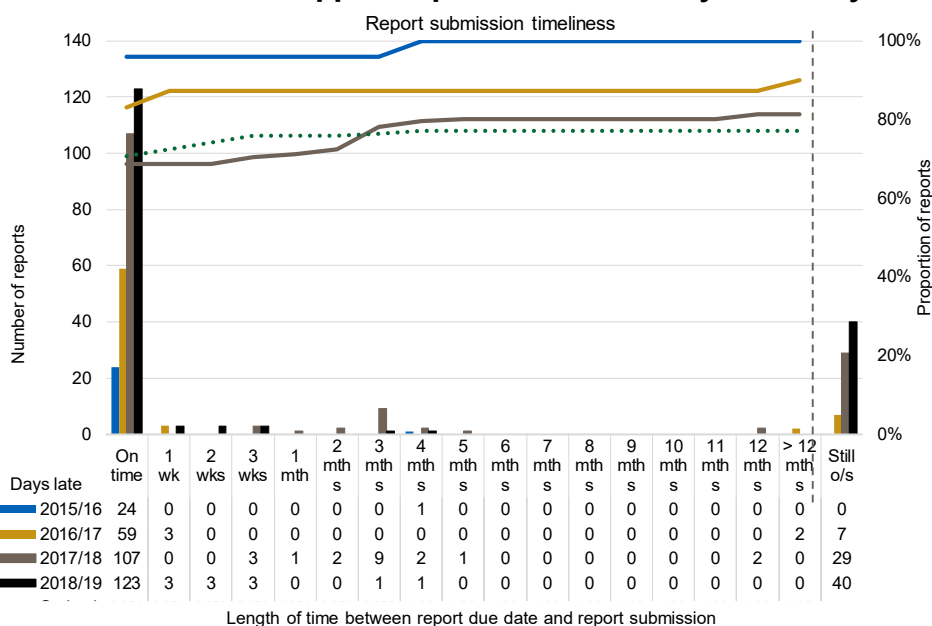


Figures 6 to 8 detail the analysis of timeliness of report submissions by the year the report was due, although the data for 2018/19 is subject to change as 12 months have not yet passed since the end of the financial year.

**Figure 7: Analysis of the timeliness of update report submissions, by financial year report due**



**Figure 8: Analysis of the timeliness of supplier report submissions, by financial year report due**



The timeliness of contract report submissions is generally lower for companies based outside the UK. Table 3 compares the percentages of reports submitted on time for UK and non-UK based contracting companies.

**Table 3: Timeliness of all initial and update contract report submissions by geographical location**

Company type	Number of reports due	Initial reports on time	Update reports on time	Overall on time	Overall submitted late	Overall outstanding
UK based contracting company	976	69%	87%	77%	22%	1%
Non-UK based contracting company	154	29%	67%	40%	27%	32%

The number of reports due for non-UK based companies is lower than for UK based companies, but still represents a significant proportion of the total (17 per cent overall).

**Figure 9: Timeliness of contract report submissions by GUO (only for GUOs with a minimum of 10 report submissions)**

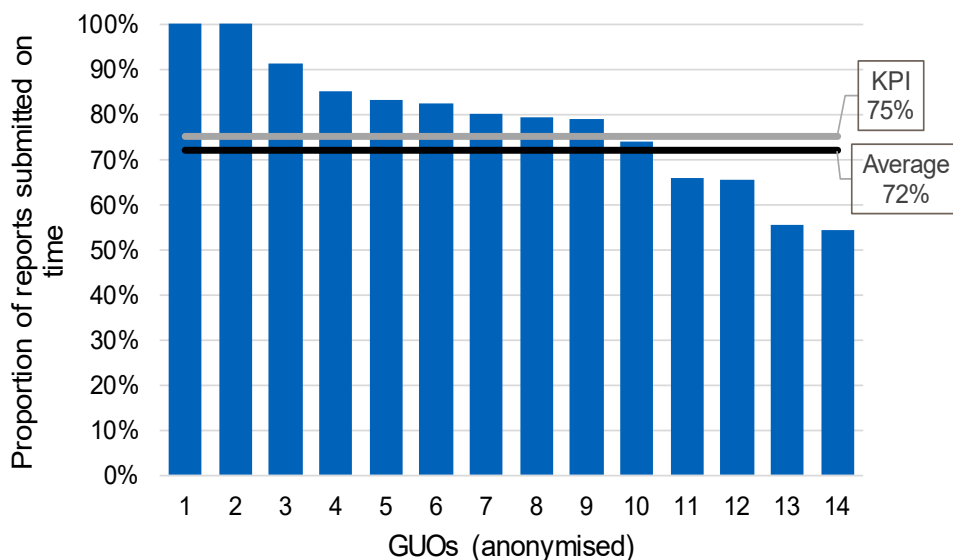


Figure 9 details the timeliness of contract report submissions for all GUOs with a minimum of 10 report submissions, comparing them against the average timeliness across all GUOs. There is a mixed level of timeliness of report submissions and even amongst the GUOs with the greatest number of contracts there are those where submission timeliness is below the average. The SSRO will seek to discuss performance with the four GUOs whose timeliness is below the average to better understand the causes behind the delays.

### Improving submission timeliness

The SSRO is committed to making the reporting process as easy and clear as possible. We held numerous bilateral meetings with contractors during 2018/19 to discuss reporting issues. This has included SME and non-UK based contractors. We have delivered an annual programme of four MOD and four industry training sessions to improve stakeholders’ understanding of DefCARS and of the reporting requirements and have recently issued reporting guidance on when supplier reports become due. We will continue to work with contractors and with the MOD in this way to assist contractors in making timely report submissions.

The support that the SSRO provides to contractors includes on-boarding meetings. Our on-boarding process for contractors has been standardised since December 2017 and we now offer such meetings whenever a contract notification is received that involves a new contractor or team with their first qualifying contract. We undertook 17 on-boarding sessions between December 2017 and April 2019. A total of 16 of the 17 on-boarding sessions were for contractors with only a single QDC or QSC. In each case the on-boarding meeting was held before the initial set of contract reports were due, using the standardised format.

The SSRO is committed to making the reporting process as easy and clear as possible

**Table 4: Timeliness of initial contract report submissions, for all initial reports submitted since December 2017, by on-boarding status**

On-boarding status	Number of reports due	Initial reports on time
On-boarded	45	67%
Not on-boarded	222	57%

Table 4 compares the timeliness of initial report submissions for contracts where an on-boarding session was held. The timeliness of submissions of the initial reports for on-boarded contracts, at 67 per cent, compares well against the 57 per cent for those contracts that were not on-boarded.

The SSRO has continued to improve the way data is collected via DefCARS, for which the user feedback has been positive. Two key developments that went live in the system in July 2018 were:

- the introduction of a 'potential QDC/QSC' facility to allow contractors to see and make a start on their reporting obligations in advance of entering into a qualifying contract;
- the development of a 'training environment' within the system to assist contractors with training personnel who will be involved in data entry in the future.

As of 30 April 2019, we provided access to the 'potential QDC/QSC' facility for 20 contracts. We have been informed that 11 of these contracts were entered into in the 2018/19 financial year. All of the submissions in relation to these 11 contracts were made in accordance with statutory deadlines, as shown in Table 5.

**Table 5: Timeliness of initial contract report submissions, for all initial reports submitted since July 2018, by 'potential QDC/QSC' status**

Contractor 'Potential QDC/QSC' facility used/not used	Number of reports due	Initial reports on time
Used	33	100%
Not Used	138	51%

### Late reports and reports not received

It is clear that the majority of report submissions are made and made on time. However, there continue to be a minority of reports that have either not been submitted or have been submitted well beyond the timescales set out in the legislation. There are three key reasons for submissions being delayed:

- the contractor is unclear about the reporting requirements;
- the contractor needs additional time to gather the relevant information; and
- the contractor is unable or unwilling to make the submissions required by the regime.

One reason that contractors have given for refusing to provide reports is that they are subject to restrictions applying in other jurisdictions.

If the SSRO is notified that reports are due from a contractor, it engages with the contractor and supports them to comply. In cases where this is unsuccessful and reports remain overdue, the SSRO will refer the matter to the MOD to consider enforcement action.

The Secretary of State is able under sections 31 and 32 of the Defence Reform Act to issue compliance or penalty notices where contractors fail to meet reporting requirements. In line with regulation 49(2) (b), the time limit for issuing a compliance or penalty notice is six months after the date the report is due.

Table 6 details the number of report submissions that were due by 30 April 2019 but had not been received. It categorises the overdue reports by reference to the period for which they have been outstanding.

**Table 6: Report non-submissions as at 30 April 2019, by length of delay**

Length of delay to submission (months)	Number of outstanding initial report submissions	Number of outstanding update report submissions	Number of outstanding supplier report submissions
0-3	12	6	21
4-6	6	3	17
7-9	12	3	2
10-12	3	0	0
12+	6	7	36
<b>Total</b>	<b>39</b>	<b>19</b>	<b>76</b>

In the 2018 Annual Compliance Report, the SSRO reported that there were a total of 33 outstanding initial reports as at 30 April 2018. These 33 reports could have been provided by submitting 11 CIRs in DefCARS. The following can be reported in relation to the 33 reports:

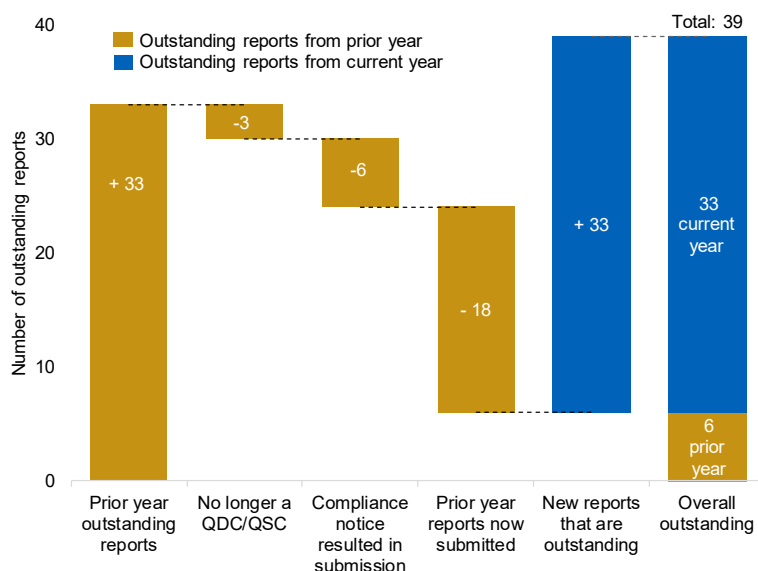
- 6 reports (2 CIRs) were submitted after the MOD issued compliance notices;
- 3 reports (1 CIR) were removed from the list after the MOD advised that the contract to which they relate should not have been notified to the SSRO as a QDC;
- 18 reports (6 CIRs) were submitted by contractors without the need for a compliance notice;
- 6 reports (2 CIRs) that were outstanding as at 30 April 2018 remained outstanding as at 30 April 2019.

The MOD advised the SSRO that it issued four compliance notices in 2018/19. Two of these compliance notices related to overdue report submissions and resulted in 6 overdue initial reports (2 CIRs) being submitted. One of the compliance notices was, in effect, a duplicate and one notice related to the contract that the MOD later advised was not a QDC.

Figure 10 shows the outstanding initial reports at 30 April 2019 and how the number outstanding (39) was derived from the number outstanding at 30 April 2018.

The MOD issued four compliance notices in 2018/19

**Figure 10: comparison of change to outstanding initial reports between 30 April 2018 and 30 April 2019**



For contract reports, the outstanding 39 initial and 19 update reports represent a total of 6 and 4 per cent respectively of the expected reports. The 76 supplier reports that were not submitted represent 18 per cent of the total expected. As at May 2019, the MOD has not advised of any compliance or penalty notices being issued in respect of the overdue reports referred to in Table 6.

### Future action

There is more action that can be taken to improve the timeliness of report submissions. It would assist if the MOD and contractors discuss and clarify reporting requirements at the contract negotiation stage. Emphasis should be placed on ensuring that non-UK based companies are aware of the reporting requirements before entering into a QDC or QSC, as 32 per cent of non-UK based company contract report submissions remained outstanding at 30 April 2019. Any perceived barriers to compliance should be addressed.

There have been several instances where expected SICR and SME submissions have not been made, or where the submission has been made below the GUO level. This is consistent with findings we reported in the 2018 Annual Compliance Report. The SICR is concerned with forward planning, informing the MOD of key strategic level company information.

Without these submissions being made, and made

at the relevant company level, key information that may be used for ongoing procurement decisions may not be available for the MOD's consideration. The MOD is working to change how relationships with key suppliers, who are required to make SICR submissions, are managed. The MOD should, where appropriate, consider increased use of the enforcement provisions of the legislation. In the limited cases where compliance notices have been issued, the required report submissions have been forthcoming.

The SSRO will consider providing on-boarding style meetings to contractors or GUOs who have performed below average with their report. We may target use of the 'potential QDC/QSC' facility at those contractors. In addition, the SSRO may seek to better understand any restrictions claimed to arise in other jurisdictions which prevent contractors making submissions. Depending on the findings, we may need to consider action to reduce the impact of such claims, for example through developments to the reporting guidance or recommendations for legislative change. Such action will likely require working closely with the MOD.

# Quality of submissions

The second key indicator in the SSRO's compliance and review methodology relates to the quality of report submissions:

**1b) "reporting obligations have been met for all reports submitted in accordance with the Regulations and relevant statutory guidance" (SSRO KPI 25% of contract report submissions made 'right first time')**

The performance indicator applied by the SSRO allows for only a 'pass or fail' of an entire submission once made, regardless of the number of errors that may be apparent in the initial submission. This is considered further as part of Figure 12 below.

The SSRO's review process starts after a contract submission has been made and, depending on the timeliness of contractor responses to issues, can continue over a period of several months. The SSRO's assessment of the quality of submissions is based on the financial year the report was submitted. The SSRO queries potential errors with report submissions that impact data quality, such as:

- internal inconsistencies;
- arithmetical errors; and
- matters that appear to be erroneous, for example incomplete information.

To keep the provisions of the framework under review, the SSRO may also raise issues with contractors in order to understand relevant explanations relating to the pricing of contracts. In line with the Act and Regulations, contractors are obliged to report the facts, assumptions, and calculations relevant to each element of the Allowable Costs and to describe the calculation used to determine the contract profit rate, including all adjustments to the baseline profit rate.

The SSRO has updated its approach since June 2018, placing greater reliance on:

- automated validation checks in DefCARS; and
- MOD reviews of submitted reports.

DefCARS automatically checks reports against a set of validation warnings, which flag potential errors within a field or report by reference to the reporting requirements. For example, an incomplete field will result in an automatic validation warning. Validation checks are run at the point of submission and the contractor has the option to rectify any issues before submitting the report. Further validation warnings were incorporated within DefCARS in June 2018 (validation rule set two). The SSRO published the full set of contract report [validation warnings](#) in May 2019, alongside its latest update to the statutory [reporting guidance](#). The benefits of the functionality include:

- assisting contractors to provide complete submissions on the first attempt;
- identifying potential reporting issues which may merit further investigation; and
- enabling the collation of validation warnings that consistently occur.

The SSRO focuses its manual reviews on issues that can be linked to validation warnings. It may base future targeted or thematic reviews on issues identified from validation warnings.

Queries are raised directly with contractors and if an issue arises on a CIR submission and is applicable to each of the three initial submissions, it is counted as three individual issues raised. If the contractor does not respond to issues, or provides a response that does not address the issues raised, the SSRO passes these matters to the MOD.

In July 2018, the SSRO introduced functionality in DefCARS that enables queries about reports to be raised and responded to in the system. The MOD has access to DefCARS and can raise its own queries with contractors. The SSRO is able to review those queries to keep under review the extent to which reporting requirements are being complied with and inform its understanding of how the provision of the Act and the Regulations is being applied.



## Issues raised

In 2018/19, the SSRO identified one or more potential issues in 69 per cent of the initial contract submissions made. As at July 2019, for reports submitted in 2018/19, the SSRO had reviewed a total of 398 contract report submissions. A total of 758 issues were raised with contractors with respect to these submissions, as set out in Table 7, of which 608 have been resolved.

**Table 7: Total number of issues raised with contractors on contract and supplier report submissions, by year the report was submitted<sup>7</sup> (as at July 2019)**

Year	Contract reports			Supplier reports		
	Number of issues raised	Number of issues resolved*	Number of issues in progress	Number of issues raised	Number of issues resolved*	Number of issues in progress
2015/16	424	421	3	48	29	19
2016/17	1,294	1,259	35	130	50	80
2017/18	1,265	1,237	28	173	84	89
<b>2018/19</b>	<b>758</b>	<b>608</b>	<b>150</b>	<b>326</b>	<b>91</b>	<b>235</b>
<b>Total</b>	<b>3,741</b>	<b>3,525</b>	<b>216</b>	<b>677</b>	<b>254</b>	<b>423</b>

\*Either through contractor or MOD response.

**Figure 11: 12 month rolling average number of issues per report type, by submission date**

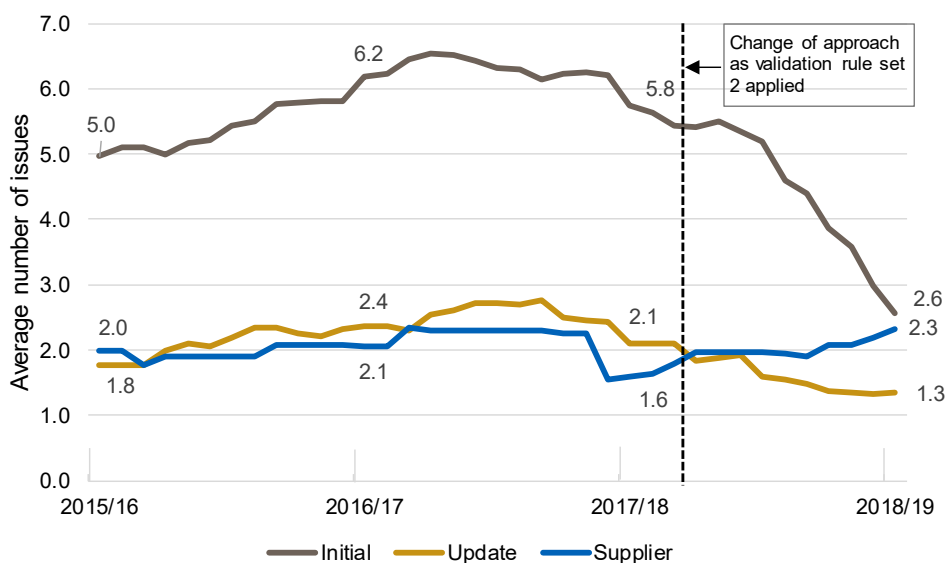


Figure 11 shows that the numbers of issues raised on contract reports is reducing. This is particularly apparent in relation to the initial contract reports, where the average number of issues raised has halved since the prior year. The reduction in issues raised has been due to a combination of factors linked to our change in approach in reviewing submissions, including increased reliance on automatic validation warnings, more focused manual reviews and reliance on the MOD to review submissions.

The CPS, one of the three initial contract reports, generally has the most issues raised against it. The CPS relates primarily to the facts, assumptions and calculations used to determine allowable costs and the description of the six-step calculation used to determine the contract profit rate.

For the update reports, QCR and ICR submissions have fewer issues raised against them. The information requirements for the QCR and ICR reports include the reporting of deliverables, costs, profits and adjustments, payments, material events and circumstances, and sub-contracts. The better performance in respect of the QCR and ICR may relate to the fact that these reports are completed on a more routine basis.

<sup>7</sup> Previous analysis has reported issues by the year the contract became a QDC or QSC. This presentation of analysis has been updated to focus on the year the report was submitted to align with other analysis within this report.

It is important to note that each submission has multiple data points and the SSRO has built more than 150 validation rules into DefCARS. The numbers of issues raised are relatively low by comparison. An analysis of the key themes arising from the identified issues is considered later in this report.

As at July 2019, for reports submitted in 2018/19, the SSRO had reviewed a total of 141 supplier report submissions. We have raised a total of 326 issues on

supplier report submissions for reports submitted in 2018/19, with issues relating primarily to the completeness of information provided and the need to explain year on year variances. A total of 91 of these issues have been resolved by contractor action to date. As some of the supplier report submissions are made on a freeform basis, it is not possible to focus on validation warnings arising only and the SSRO's review process continues to include a more detailed assessment against the requirements of Part 6 of the regulations.

**Figure 12: 12 month rolling average proportion of report submissions correct first time, by submission date**

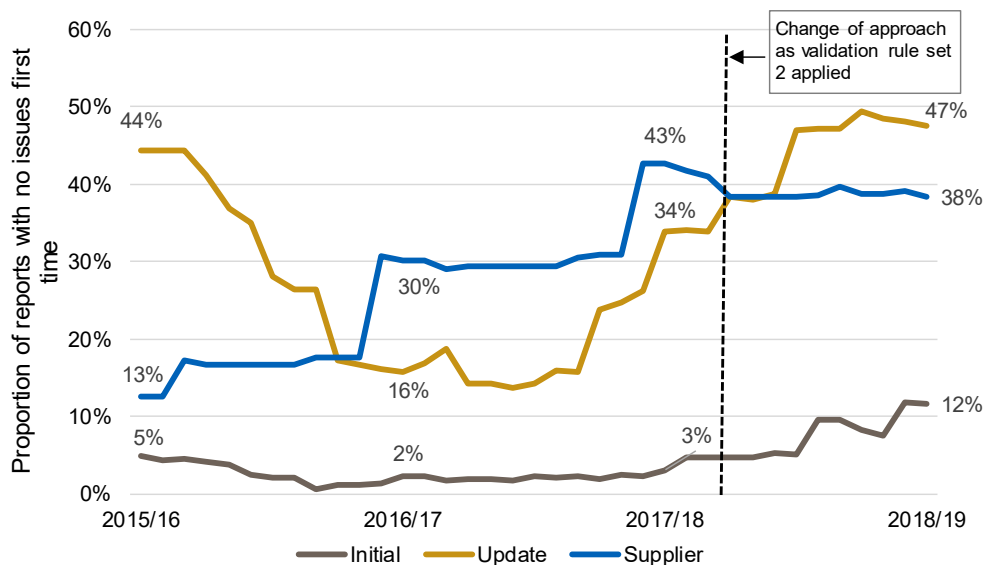


Figure 12 shows that issues continue to be raised year on year with initial report submissions. There has been a small increase in the number of submissions made 'right first time' over the past year, but this is still only in the minority of cases for the initial report submissions.

With respect to the update reports, Figure 12 shows the percentage of reports submitted with no issues was initially higher than for other contract reports or the supplier reports. The performance in 2015/16 is based, however, on only nine report submissions. The percentage of reports with no issues then dropped in 2016/17, as more submissions were made, before improving in 2017/18 and 2018/19. The increase in update reports submitted without issues in the past two years may relate to introduction of the online version of DefCARS in March 2017, which included an auto-population facility from one report to the next, and the fact that some of these reports are submitted more frequently, raising levels of familiarity with the reports.

The number of supplier report submissions is gradually increasing over the years as more qualifying contracts enter the regime and more of the associated number of business units become subject to the regulations. The proportion of submissions made with no issues has increased since 2015/16, but has dropped slightly in comparison with the prior year. The overall increase may be explained by increasing familiarity with the reporting requirements in relation to supplier reports.

**Figure 13: Proportion of contract report submissions with no issues raised, by GUO (only for GUOs with a minimum of 10 report submissions)**

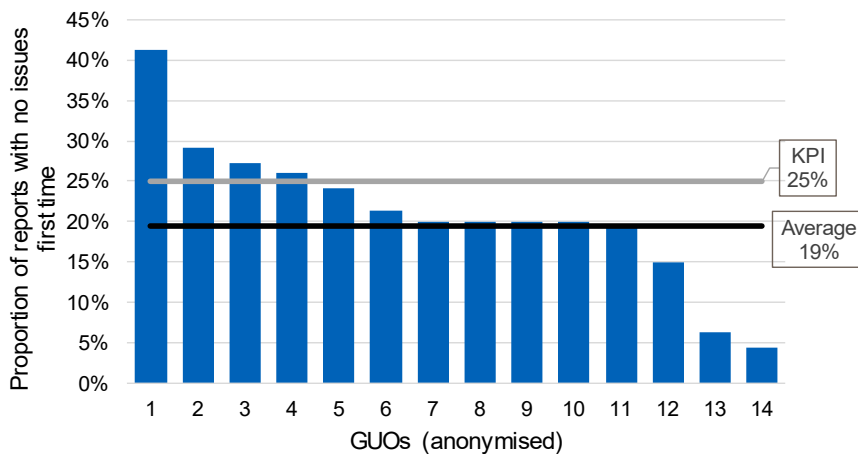


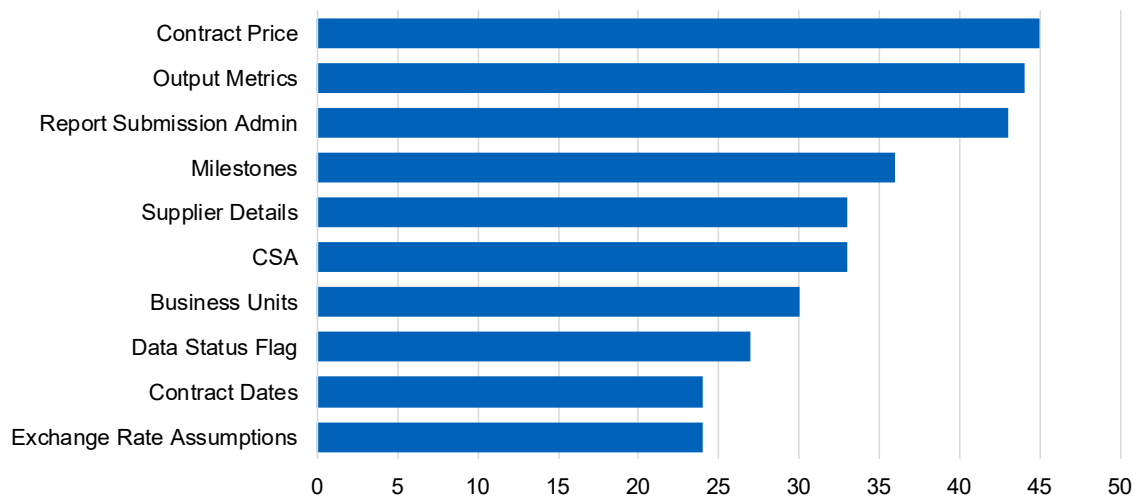
Figure 13 details the proportion of contract reports submitted with no issues raised for all GUOs with a minimum of 10 report submissions. As with the consideration of timeliness, there is a mixed level of quality of report submissions.

Amongst the GUOs with the greatest number of contracts there are those who perform below either the SSRO’s performance indicator or the average level achieved by all contractors. The SSRO will investigate the performance of the GUOs whose proportion of reports submitted with no issues is below the average to better understand the causes behind the issues arising.

**Themes arising from identified issues**

The queries raised by the SSRO and the MOD on the statutory reports cover a wide range of issues. Figures 14 and 15 detail the top themes that have arisen from the SSRO’s review of contract and supplier report submissions, respectively, in 2018/19. Figure 16 details the top 2018/19 themes that have arisen from the MOD’s review of contract report submissions.

**Figure 14: Analysis of the top ten themes from contract report issues raised by the SSRO in 2018/19**



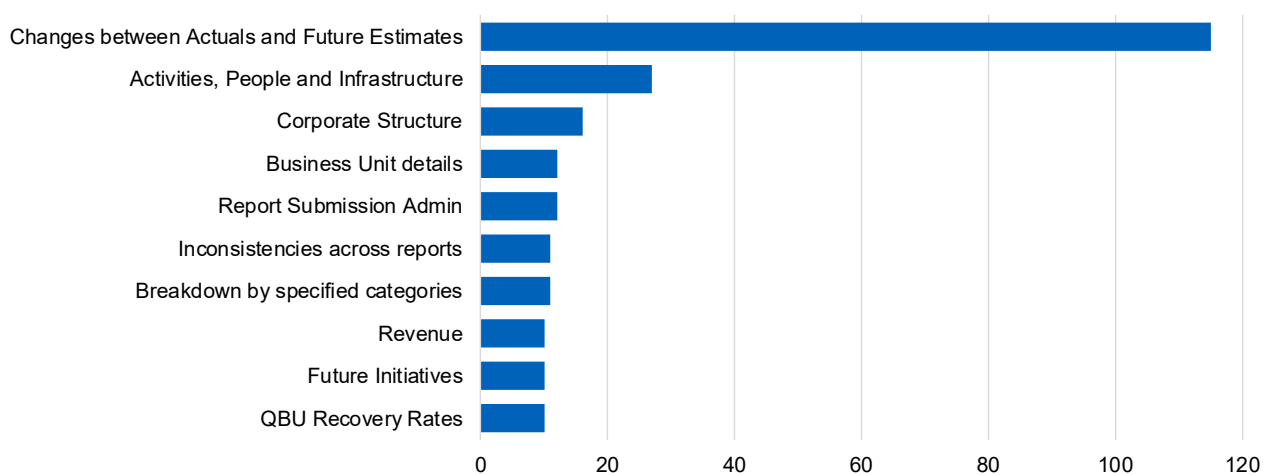
The SSRO raised 758 issues on contract report submissions. The top ten themes noted in Figure 14 account for 45 per cent of the total issues raised. Table 8 describes the types of issues arising within each of the top ten themes.

**Table 8: Common contract report issues identified by the SSRO in 2018/19**

Theme	Common issues arising
Contract price	Inconsistent prices reported in the same report and between reports for the same contract. Exclusion of 'sunk' elements.
Output metrics	Missing metrics or metrics not linked to contract deliverables.
Report submission admin	Due dates of reports reported incorrectly.
Milestones	Unexplained variances between expected and actual delivery.
Supplier details	Missing data.
Capital servicing adjustment	Calculation incomplete or not based on capital servicing rates in force at the time of the agreement.
Business units	Missing data.
Data Status Flags	Incorrect selection of cost status, for example costs noted as being final when they are still provisional.
Contract dates	Unexplained changes to the contract completion date or date of latest pricing amendment.
Exchange rate assumptions	Missing confirmation of whether exchange rate assumptions apply

Some of the themes relate to basic administrative data which is either incomplete or inconsistent between reports. This includes supplier details, business units, exchange rate assumptions and data status flags. The absence of such information will likely impede analysis and use of the data. DefCARS picks up most of such issues automatically and flags them for attention at the point of submission. The ongoing identification of these issues indicates that contractors need to take more care before making a submission.

**Figure 15: Analysis of the top themes from supplier report issues raised by the SSRO in 2018/19**



Overall, there are fewer issues arising with supplier reports than there are with contract reports. This is primarily due to two reasons. First, there are fewer supplier report submissions than contract report submissions. Secondly, there is less standardisation in DefCARS of the supplier reports, with the consequence that there are fewer standardised data points in supplier reports compared to contract reports. The key theme arising from the issues raised on supplier reports concerns variance analysis. Table 9 describes the types of issues arising within each of the top themes.

**Table 9: Common supplier report issues identified by the SSRO in 2018/19**

Theme	Common issues arising
Changes between actuals and future estimates	Variance analysis between prior year actuals and prior year estimates and prior year actuals and current year estimates missing.
Activities, people and infrastructure	Descriptions of forecast costs, anticipated changes, labour requirements, policies to employ graduates or apprentices, to provide staff bonuses or for training and development of personnel not presented in the required categories of (i) QDCs and QSCs; (ii) any other defence contract; and (iii) all other contracts.
Corporate structure	SICR submissions detailing corporate structure missing the level of granularity required.
Business unit details	Dates of the most recent completed year for business units missing or incorrectly reported.
Report submission admin	Dates of required submission incorrectly reported.
Breakdown by specified categories	Categories used in the legislation not followed.
Revenue	Missing description showing the proportion of revenue from QDCs, QSCs and any other defence contract.
Future Initiatives	Information on material future initiatives missing.
QBU Recovery Rates	Recovery rates information incomplete.

**Figure 16: Analysis of the top themes from contract report issues raised by the MOD in 2018/19**



The SSRO introduced a facility in DefCARS for the MOD to raise issues against report submissions, with effect from the start of August 2018, which has given us sight of the MOD’s reviews of report submissions. The MOD’s reviews were stimulated by development of the MOD’s commercial toolkit detailing its policies with respect to the collection and review of data on qualifying contracts in DefCARS. MOD reviewers raised 301 issues across 18 contracts which had reports submitted in 2018/19. In line with the approach agreed with the MOD, the SSRO does not raise any duplicate issues as part of its own review of submissions.

The SSRO has undertaken some analysis of the issues raised by the MOD. Only 31 of the issues raised by the MOD were linked to validation warnings in DefCARS that remained following submission of reports. A significant number of the remaining issues were raised in areas where the MOD has been able to check information against contractual agreements. The MOD queried differences between reported information and its understanding of the contract in relation to:

- contract values;
- elements of the six-step calculation of the contract profit rate;
- sub-contract details;
- contract amendments;
- explanations for variances; and
- agreed reporting plans.

There are instances where the MOD has raised duplicate issues within report submissions. Some of the issues raised by the MOD have not been allocated to categories in DefCARS in the same way that the SSRO would have categorised them. There is some room for the MOD to increase the number of reports that it reviews and also to improve the way that it raises and categorises issues raised.

The SSRO has worked with the MOD, by attending MOD training sessions aimed at Delivery Teams, to ensure that the practical use of the issues logging functionality is better understood by teams. We will continue to provide such support where we can.

The issues raised by the SSRO or the MOD in DefCARS may be linked to validation warnings that remain in the submissions or entirely separate from those warnings. Figure 17 considers the extent to which the automatic validation checking in DefCARS is driving the issues that are being raised with report submissions.

**Figure 17: Proportion of issues raised by the SSRO in 2018/19 linked to validation warnings**

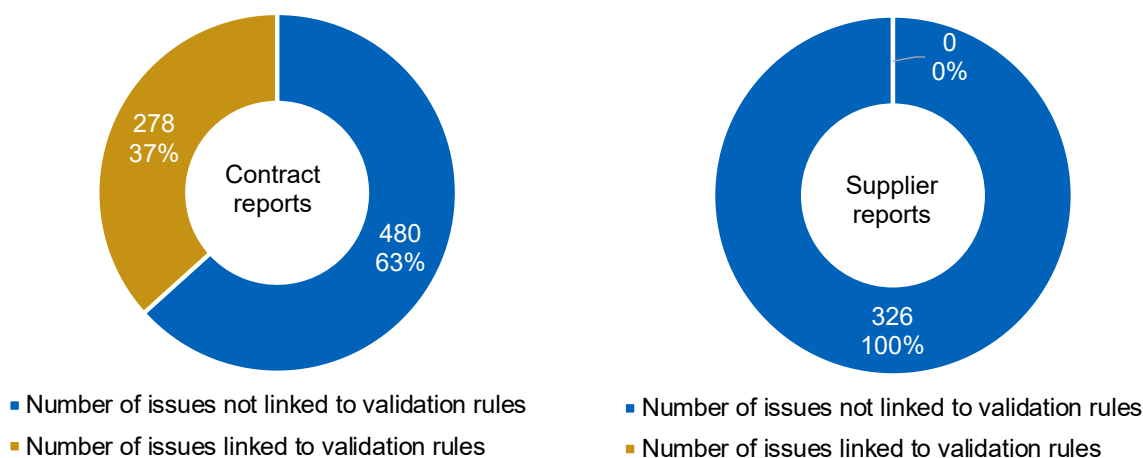


Figure 17 shows that there continue to be issues raised that are not linked to validation warnings. The SSRO has developed the validation rules in the system, particularly for contract reports, with a second set of validation rules introduced in July 2018 and a third set in May 2019. If issues continue to be raised that are not linked to validation rules, then there may be potential to extend the validation rules in DefCARS. This may increase compliance by flagging issues at the point of submission and decrease the level manual review. If issues related to validation rules continue to arise, this may indicate a wider problem that needs to be addressed. It is expected that in future years the SSRO will be able to collate information on validation warnings that consistently occur and have not been rectified. We expect that the number of issues arising that are not linked to validation warnings will decrease over time but we will continue to monitor the balance between issues that are linked to validation warnings and those that are not.

To date, none of the issues raised on supplier reports have been linked to validation warnings. This is primarily because there are a very limited number of rules that have been developed for supplier reports. In future, the SSRO may investigate whether any additional functionality could be developed in DefCARS to further automate the checking of supplier reports.

## Improving the quality of submissions

The regulatory framework introduced by Part 2 of the Defence Reform Act 2014 (the Act) requires transparency by contractors, establishing a statutory set of standardised reports. The data accumulated in the statutory reports may be used by the MOD to support procurement and contract management. It is intended to improve independent estimating for budgeting and challenges to contractor costs. The data should also inform discharge of the SSRO's functions in a way that delivers value for money and fair and reasonable prices. To achieve this, reports must contain the required data and that data must be good quality.

The introduction of a greater range of validation warnings in DefCARS has helped to reduce the number of such issues compared to previous years. It is hoped that introduction of the third set of validation rules in May 2019 will continue this downward trend. The third validation rule set indicates if:

- the status of some costs appear erroneous (such as costs profiled in future years being labelled as 'final');
- the contractor hasn't indicated whether exchange rate assumptions are applicable or not;
- the total contract price has changed from the last submitted contract report (of any type) and, if so, data relating to the latest pricing amendment should be completed.

We have been able to identify the validation warnings raised automatically by DefCARS which have not resulted in contractors amending their reports. This information has provided the SSRO with a better understanding of the difficulties faced by contractors in completing reports, and insight into how the provisions of the legislation have been applied in practice.

In order to assist with improvements to data quality, we have also:

- improved the way data is collected via DefCARS;
- held on-boarding sessions with contractors;
- made ongoing improvements to

reporting guidance;

- raised more focused issues directly on DefCARS; and
- initiated a programme of reviews of reporting requirements.

During 2018/19, the SSRO has issued new or updated guidance on:

- the 'date a contract is entered into', which will help identify when contract reports become due, as part of its DefCARS reporting guidance;
- when supplier reports are due, with potential scenarios, which will help contractors who are subject to reporting obligations to identify which reports are due, for which period and when they need to be submitted;
- the capital servicing adjustment, making clear that regardless of which financial periods are described in the records from which data is drawn to determine the capital employed and cost of production, the capital servicing rates to which the relevant parties must have regard are those in force at the time of the agreement; and
- the QCR and ICR sections of the guidance.

We provided functionality that allows contractors to work within a 'training environment' in DefCARS. We enabled contractors to start populating their initial report submissions before a qualifying contract has been entered into, using the 'potential QDC/QSC' option. We have also made it possible for both the SSRO and the MOD to raise issues directly in the system against individual submissions.

There are some themes arising from issues identified with reports that can be addressed through guidance updates.

Following a prioritisation exercise, we have consulted on the next iteration of reporting guidance, including updates in relation to on-demand reporting and the CCR section of the guidance.

The introduction of a greater range of validation warnings in DefCARS has helped to reduce the number of issues

We have made it possible for both the SSRO and the MOD to raise issues directly in the system against individual submissions

As part of our work to improve the operation and reporting of our compliance work, we are considering the current 'pass or fail' approach to determine whether additional reporting would improve the transparency over the quality of submissions made. This is something we will consider as part of our work to review the methodology.

The SSRO has started to undertake work on a review of reporting requirements. This review aims to consider the purpose behind the reporting requirements, the use of the data, and whether requirements are proportionate. It will involve consideration of the data submitted in reports. Initial topics include the reporting of contract amendments and variances, the defined pricing structure used in contract reports, and the overhead reports. This work may help to improve the quality of report submissions in due course.

There are areas in which contractors continue to find difficulty in applying the regulatory requirements:

- some contractors have reported that they are unable to provide metrics information, even though this is a legislative requirement, as either no metrics are applicable to the contract type, or the contract has not stipulated appropriate metrics; and
- the requirement and ability to report 'sunk' costs when a contract is brought within the regime following an amendment has proved to be problematic for some contractors.

Further consideration may need to be given to the operation of these regulatory requirements and they have been identified as areas for future work by the SSRO.

The highest number of issues raised on supplier reports relate to the explanation of variances. These issues have arisen due to suppliers either not providing, or inadequately explaining, the differences between prior year actual costs and prior year estimated costs, or between prior year actual costs and current year estimated costs. The MOD is considering legislative change that would only require material variances to be explained. The SSRO will keep this under review as a potential focus of future work.

The consideration of supplier reports overall would be improved by feedback from the MOD on the intended purpose and use of the reports. This will aid understanding of the value of the data and how best it can be captured. The SSRO has commenced work in this area by including overhead report submissions in its review of reporting requirements in 2019/20.

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The highest number of issues raised on supplier reports relate to the explanation of variances



# Targeted reviews

Between December 2018 and March 2019, the SSRO carried out targeted reviews of two initial report submissions and issued a report to the MOD on this work in May 2019.

The aim and scope of the review, which was agreed with the MOD in advance, was to undertake detailed monitoring of compliance with reporting requirements by contractors and to see how Delivery Teams had dealt with the reports. The reviews did not extend to providing assurance that individual contracts have been priced according to statutory requirements, nor that all the costs included in the contracts were Allowable.

The targeted reviews provided insight into how the regulatory framework and the MOD's internal procedures were being applied. It was recognised throughout that the insight provided from the reviews could not be generalised, as the two reports selected for review were not representative of the population of reports on qualifying contracts.

The reviews identified issues with inconsistent reporting of contract prices, incorrect recording of reporting dates and incomplete cost recovery rates. Questions were raised as to whether the deliverables, metrics and milestones recorded in submissions actually described what was intended under the legislation.

In both cases, there were issues with how the MOD's review processes were working in practice and with the timeliness of the MOD's reviews. There were two key reasons, cited by both of the Delivery Teams, for the lack of timely review of contractor submissions:

- the MOD has experienced significant difficulties in accessing DefCARS, due to bandwidth limitations on the MOD's Enterprise Gateway Service; and
- Delivery Teams felt that other pressures, particularly competing work priorities and changes in personnel, affected their ability to complete report reviews within the MOD's target timescale.

The report concluded that there is a clear place for the MOD's own checking of reports alongside the SSRO's compliance monitoring, given the MOD's knowledge of the subject contracts. Increased alignment between the SSRO and the MOD and consistent delivery of checking and monitoring promotes greater benefits, such as quality data to support contract and supplier management and more efficient defence procurement.

Findings from the reviews indicated that follow-up action may be required to address the identified issues. Separate proposals have been prepared for consideration between the SSRO and the MOD and we will be undertaking further targeted reviews during 2019/20.

The SSRO will be undertaking further targeted reviews during 2019/20.

# Issues referred to the MOD

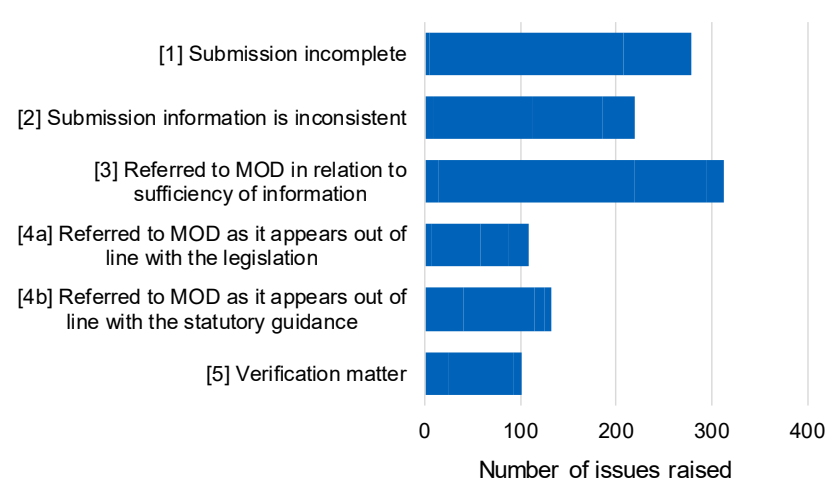
During 2018/19, the SSRO referred issues to the MOD for attention if no response was provided by the contractor to the SSRO's initial queries, or a response was provided that appeared out of line with the legislation or statutory guidance.

**Table 10: Number of issues referred to the MOD on contract report submissions, by year the report was submitted**

Year	Number of issues referred	Number of issues resolved	Number of issues in progress
2015/16	100	97	3
2016/17	576	541	35
2017/18	327	299	28
2018/19	148	65	83
<b>Total</b>	<b>1,151</b>	<b>1,002</b>	<b>149</b>

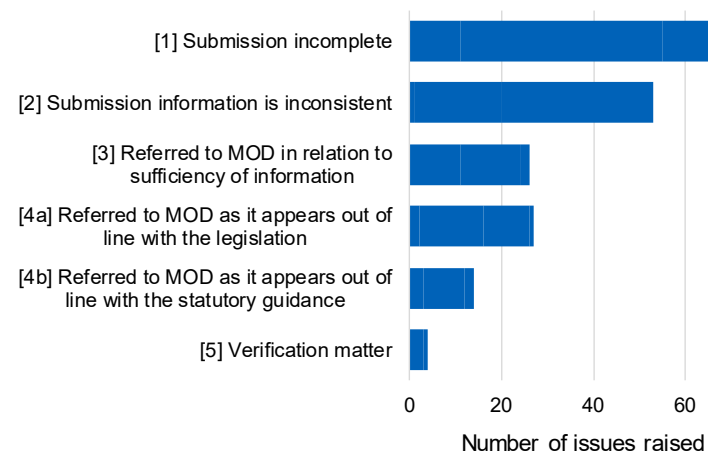
Figure 18 provides a breakdown of the categories used by the SSRO when referring issues to the MOD.

**Figure 18: Analysis of the categories of issues referred to the MOD, 2015/16 to 2018/19**



In the 2018 Annual Compliance Report, the SSRO reported that the MOD had categorised 134 contract report issues brought to its attention by the SSRO as potential breaches of the legislation. Since publication, but before the compliance logging functionality went live on DefCARS, the MOD confirmed that an additional 55 contract report issues brought to its attention by the SSRO were potential breaches of the legislation. Figure 19 provides a breakdown of the categories used by the SSRO for these 189 issues when they were referred to the MOD.

**Figure 19: SSRO categorisation of 189 contract report issues noted by the MOD as potential breaches of the legislation**



The following updates can be provided regarding the 189 issues characterised by the MOD as potential breaches of legislation:

- 133 of the issues have been resolved, mainly through contractor amendments and resubmissions. Of these, there were 29 issues that the MOD decided to take no further action on, the vast majority of which relate to incomplete or inconsistent submissions.
- 56 issues are still being considered by the MOD to decide whether they involve breaches of the legislation and what enforcement action will be taken.

Of the 56 issues that are still being considered by the MOD, 21 were categorised by the SSRO as issues that appeared to be out of line with the legislation or out of line with the statutory guidance.

The SSRO has received feedback from the MOD on how it has categorised the issues raised with it by the SSRO, however the reasons for why the 189 potential breaches of legislation may have occurred are not clear. It is also unclear whether any action has been taken by the MOD, or can be taken by the SSRO to prevent reoccurrence of such issues.

The SSRO has referred 210 issues to the MOD with respect to overhead report submissions and 141 of these relate to SICR report submissions. There has been no response from the MOD on the individual issues raised, however the MOD is working to change how relationships with the key suppliers are managed and intends to use SICRs to inform this work. While the SICRs reviewed meet the requirements of the legislation in terms of the key outline information required, the depth of the information provided varies significantly between submissions. Without the requested feedback from the MOD, it is unclear how useful the submissions made have been for the MOD's purposes or whether the depth or quality of submissions are meeting the MOD's expectations.

Some of the issues that the SSRO has raised with the MOD outside of DefCARS which remain outstanding are now more than two years old and many of them relate to reports submitted prior to 2018/19. It is not clear whether these remaining issues are likely to be, or can now be resolved. If not, there may continue to be some data quality issues with the information in DefCARS.

There remain issues that the SSRO has raised with the MOD within DefCARS which the MOD has not yet responded to. These issues have been raised in the period after July 2018 and the SSRO intends to continue to seek responses to these in 2019/20. Further issues will continue to be raised with the MOD in cases where they are not resolved with contractors.

Our expectation is that the timeliness of responses to issues referred to the MOD by the SSRO will improve going forward. There have been advances in the MOD's processes and procedures for the review of submissions, and the MOD has advised that its difficulties in accessing DefCARS have been alleviated.

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Our expectation is that the timeliness of responses to issues referred to the MOD by the SSRO will improve going forward

# Development of the methodology

The SSRO's approach to date has supported contractors to meet reporting requirements and set expectations on the quality of data submitted. The findings from our compliance monitoring have informed our other statutory functions, allowing for the identification of areas for improvement in our methodologies, guidance and systems, and provided evidence for our review of legislation.

The SSRO has sought to adopt a more efficient, risk based and proportionate approach to the application of our methodology. We have developed further automatic validation in DefCARS and provided for all correspondence and issues to be fully logged and communicated via DefCARS. This has provided for a more secure, transparent and efficient way of raising and resolving issues. In addition, we have introduced 'targeted reviews' of submissions which have involved detailed discussion with MOD Delivery Teams.

Alongside developments in our compliance monitoring, we have supported contractors in other ways to improve the quality of submissions. We have:

- updated our standard on-boarding process for contractors with new qualifying contracts;
- implemented a training environment on DefCARS;
- enabled contractors to gain early access to DefCARS via the 'potential QDC / QSC' functionality; and
- held calls and meetings with contractors to discuss any issues arising from submissions.

The SSRO has worked with the MOD to develop the MOD's processes and procedures for reviewing report submissions and to ensure that there has been a greater shared understanding of the issues encountered in contractor submissions. As reported in its commercial toolkit, updated in February 2019, the MOD has adopted a consistent policy with respect to the collection and review of data on qualifying contracts.

We published a working paper in July 2019 to commence a formal review of our compliance methodology. The review seeks to update the methodology to reflect more clearly the SSRO's role, as well as developments in technology, approach and consideration of stakeholder feedback received since the existing methodology was published in early 2017. We are also considering how our approach to compliance monitoring may be improved. Any update to the methodology will be subject to public consultation in the Autumn.

The current timetable is for publication of any revised methodology by 31 January 2020, with implementation from 1 April 2020.

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The SSRO has sought to adopt a more efficient, risk based and proportionate approach to the application of our methodology

# Appendix 1: Data sources and Methodology

The contract data in this report is sourced from the latest of the Contract Pricing Statement, Contract Notification Report, Quarterly Contract Report, Interim Contract Report, or Contract Completion Report. Data related to quality and timeliness of submissions are sourced from DefCARS, and the SSRO's internal compliance monitoring logs.

## Adjustments to data

All data is as reported to the SSRO, except in some circumstances where there are known, and significant, data quality issues. In these cases, some adjustments have been made so the analysis is not misleading.

## Definitions and clarifications

A QDC is a non-competitively procured defence contract with a value of £5 million or more. If a sub-contract of a QDC is also awarded without competition, and has a value of more than £25 million, it becomes a QSC.

References to 'initial reports' includes any on-demand CPS and CRP submissions.

The analysis in this report is based on when the report submission is due or submitted and is based on the period 1 May to 30 April each year. Contractors have one month after the contract becomes a qualifying contract to submit their reports. For example, a contract entered into on 30 March 2019 will have an initial report due date of 30 April 2019 and therefore the initial report would be included in the analysis for the 2018/19 financial year. The analysis aims to be consistent with the Annual Qualifying Defence Contract Statistics 2018/19<sup>8</sup>, which reports on contracts by the government financial year in which they became QDCs/QSCs.

Analysis looking at the timeliness of report submissions uses the report due date to group the analysis by financial year, whilst analysis looking at the quality of report submissions uses the report submission date to group the analysis into the relevant financial year.

A contracting company is defined as a UK or non-UK company based on the registered address of the contracting company, sourced from the contract report submissions.

Totals are calculated on unrounded figures, before being rounded for presentational purposes.

## Reporting on compliance issues

The SSRO has monitored whether contractors are meeting their reporting obligations under section 36(2) of the Act by considering if the required submissions:

- were delivered on time; and
- contained the information prescribed in the Regulations and any relevant statutory guidance issued by the SSRO.

The compliance approach included querying obvious errors (for example internal reporting inconsistencies) as well as raising any issues if completed reports seemed to be erroneous (for example reports containing incomplete or limited information). Where specific issues were raised with a contractor but not resolved satisfactorily, the SSRO informed the MOD asking that it considered its responsibilities with respect to the issue of compliance and penalty notices.

Additionally, the SSRO has reviewed the reports submitted by contractors to understand the operation of the provision of the Act and Regulations with respect to the pricing of contracts. While the SSRO has sought to understand the operation of the pricing provisions of the regulatory framework by reference to information reported on individual contracts, it has not audited reported costs or profit rates on a contract by contract basis, nor provided any assurances that individual contracts have been priced in accordance with statutory requirements.

<sup>8</sup> <https://www.gov.uk/government/publications/annual-qualifying-defence-contract-statistics-201819>

The SSRO raised concerns with the MOD on pricing issues, particularly as to how the price control provisions of the Act and the Regulations were being applied. Concerns were raised for the following circumstances:

- the facts, assumptions and calculations relevant to an element of the Allowable Costs suggested a breach of the Act and the Regulations or deviation from the statutory guidance which was neither reported nor explained;
  - the calculation made under Regulation 11 of the Regulations, including any adjustment under the six steps, to determine the contract price of a QDC appeared to be a breach of the Act, the Regulations or a deviation from the statutory guidance but was neither reported nor explained;
- an unsatisfactory explanation was provided for a contravention of the Act or the Regulations;
  - a deviation from the statutory guidance was reported by a contractor; and other information material to the pricing of the contract was reported and this appeared to suggest a failure to comply with the Act, the Regulations or a deviation from the statutory guidance.

# Appendix 2: Information requirements of the statutory reports

The Act and Regulations set out the statutory reports that defence contractors must submit to provide transparency about their costs with respect to QDCs and QSCs.

There are 15 different types of reports that are collected via DefCARS which relate to either specific contracts (contract reports) or defence suppliers (supplier reports). Contract reports are provided by the contracting company (the named party responsible for delivering the contract) on a minimum of three occasions during the lifecycle of a QDC or QSC.

**Table 1: contract reports**

Report	Key information captured
Contract Notification Report (CNR)	Captured in DefCARS as part of the Contract Initiation Report (CIR) template. <ul style="list-style-type: none"> <li>• Annual breakdown of costs and profits estimated under contract;</li> <li>• Annual cost profiles split by defined pricing structure;</li> <li>• Sub-contract details;</li> <li>• Payment schedule; and</li> <li>• Contract deliverables, metrics and milestones.</li> </ul>
Contract Pricing Statement (CPS)	Captured in DefCARS as part of the Contract Initiation Report (CIR) template. <ul style="list-style-type: none"> <li>• Calculation of Total Contract Price;</li> <li>• Calculation of the Contract Profit Rate; and</li> <li>• Facts, assumptions and calculations relating to each element of the Allowable Costs.</li> </ul>
Contract Reporting Plan (CRP)	Captured in DefCARS as part of the Contract Initiation Report (CIR) template. <ul style="list-style-type: none"> <li>• Reporting dates for all contract reports;</li> <li>• The defined pricing structure to be used in reporting;</li> <li>• Output metrics; and</li> <li>• Cost recovery bases.</li> </ul>
Quarterly Contract Report [if >£50m] (QCR)	<ul style="list-style-type: none"> <li>• Annual breakdown of costs and profits, both at time of latest agreement and by incurred and forecast costs at reporting date;</li> <li>• Cost breakdown by contractor's own reporting structure;</li> <li>• Costs profiled by calendar quarter;</li> <li>• Details of any material variances between estimated costs and current forecasts;</li> <li>• Sub-contract details;</li> <li>• Forecasts of any post-contract price adjustments; and</li> <li>• Information on contract milestones.</li> </ul>

Report	Key information captured
Interim contract report [lower value - <£50m] (ICRL)	<p>The Interim Contract Report (ICR) is split into two templates in DefCARS to reflect the differing reporting requirements for contracts above and below £50m. For contracts below £50m, the following information is captured:</p> <ul style="list-style-type: none"> <li>• Annual breakdown of costs and profits, both at time of latest agreement and by incurred and forecast costs at reporting date;</li> <li>• Cost breakdown by defined pricing structure;</li> <li>• Annual breakdown of recovery base volumes, both at the time of latest agreement and by incurred and forecast volumes at reporting date</li> <li>• Details of any material variances between estimated costs and current forecasts;</li> <li>• Sub-contract details;</li> <li>• Forecasts of any post-contract price adjustments; and</li> <li>• Payment schedule; metrics; and milestones.</li> </ul>
Interim contract report [higher value - >£50m] (ICRH)	<p>The Interim Contract Report (ICR) is split into two templates in DefCARS to reflect the differing reporting requirements for contracts above and below £50m. For contracts above £50m, the following information is captured:</p> <ul style="list-style-type: none"> <li>• Annual breakdown of costs and profits, both at time of latest agreement and by incurred and forecast costs at reporting date;</li> <li>• Cost breakdown by defined pricing structure;</li> <li>• Annual breakdown of recovery base volumes, both at the time of latest agreement and by incurred and forecast volumes at reporting date; and</li> <li>• Details of any material variances between estimated costs and current forecasts.</li> </ul>
Contract completion report (CCR) [6 months after contract end]	<ul style="list-style-type: none"> <li>• Annual breakdown of costs and profits, both at time of latest agreement and by incurred and forecast costs at reporting date;</li> <li>• Cost breakdown by defined pricing structure;</li> <li>• Annual breakdown of cost recovery rates, both at the time of latest agreement and by incurred and forecast volumes at reporting date;</li> <li>• Details of any material variances between estimated costs and current forecasts;</li> <li>• Sub-contract details;</li> <li>• Forecast or actual values of any post-contract price adjustments; and</li> <li>• Payment schedule; metrics; and milestones.</li> </ul>
Contract costs statement (CCS) [12 months after contract end]	<p>There is a short structured report form to collect basic details, but the main content of the report is unstructured and is submitted by the contractor in a supporting file.</p> <ul style="list-style-type: none"> <li>• Contractor's accounting period;</li> <li>• The cost allocation and apportionment methodology;</li> <li>• Annual profile of Allowable Costs;</li> <li>• Explanation between the total actual Allowable Costs and the breakdown of purchases, other direct costs and indirect costs; and</li> <li>• Explanation of any variance between reported information and the most recent on-demand report.</li> </ul>
On demand contract reports	<p>The Secretary of State can require contractors to submit a Contract Reporting Plan, Contract Pricing Statement or Contract Costs Statement.</p>



Supplier reports are reports required by the Regulations that are provided on a supplier rather than contract level. These are provided on an annual basis where the relevant threshold has been met. The effect of the threshold is that not all suppliers with QDCs/QSCs will be required to submit supplier reports. There is an additional supplier report, the Strategic Industry Capacity Report, which is submitted outside of DefCARS.

**Table 2: supplier reports**

Report	Key information captured
Actual Rates Claim Report (ARCR)	For these reports there is a short-structured report form to collect some basic details but the main content of the report is unstructured and is submitted by the contractor in a supporting file.
Estimated Rates Claim Report (ERCR)	<ul style="list-style-type: none"> <li>Provides the actual and estimated cost recovery rates and cost recovery bases for the Qualifying Business Unit.</li> </ul> Supporting information and analysis looking at how their rates were calculated from the financial statements or budget estimates.
Estimated Rates Agreement Pricing Statement (ERAPS)	Provides descriptions, facts and assumptions used in the estimated rates claim report. No numeric fields or calculations.
QBU Actual Cost Analysis Report (QBUACAR) QBU Estimated Cost Analysis Report (QBUECAR)	These reports are combined into a single template in DefCARS to reduce duplication called the Qualifying Business Unit Cost Analysis Report (QBUCAR). <ul style="list-style-type: none"> <li>Provides actual and estimated operating costs, staffing costs and revenue information in a structured format, with breakdowns of items by defined business function (e.g. manufacturing, engineering).</li> </ul> Estimate and actual cost recovery rate and cost recovery base information is provided as well as actual and estimated business unit costs applicable to defined activity types (e.g. research and development).
Rates Comparison Report (RCR)	<ul style="list-style-type: none"> <li>Details of all QDCs of the QBU which have cost recovery rates used as the basis for contract pricing.</li> <li>Details of the rates used within the QBU.</li> <li>Compares actuals and estimates for cost recovery rates and recovery base volumes.</li> </ul>
SME Report	Provides quantitative information in relation to the use of small and medium sized enterprises in the supply chain.
Strategic Industry Capacity Report (SICR)	The SICR provides a long term view of key suppliers' capacity and overheads relevant to the MOD's current and future requirements. The SICR provides information on suppliers' corporate structures broken down by QBU and revenue streams. The report also includes any planned changes to structure, a description of the suppliers' activities, people and infrastructure, forecast costs of maintaining industrial capacity and details on the supply chain. Forecasts are for a period of five years.

