



SSRO

Single Source
Regulations Office



Ministry
of Defence

Demystifying the Single Source Regulatory Framework for SMEs

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13 December 2023

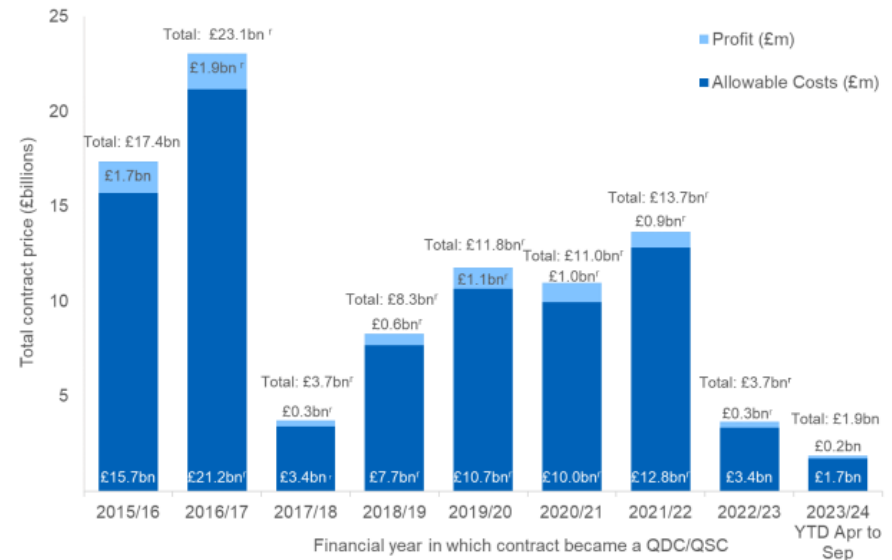
Introduction

- The Defence sector: drives innovation and employment; provides opportunities for export
- Global challenges: need to get equipment and capabilities to armed forces through speedy and efficient procurement
- Non-competitive contracts account for around half of the MOD's annual procurement spend circa £9Bn per annum.
- An area of focus that really matters to government particularly in light of the Defence Command Paper refresh
- In common with every other country that has a defence industry the UK has strict rules about how Single Source Contracts should be priced

SSRO established by the Defence Reform Act and Single Source Contract Regulations 2014

- Legislation introduced in 2014
- Regulatory framework with controls on prices of qualifying contracts and transparency
- To September 2023: 575 single source contracts, with an estimated price c.£94.5 billion
- The SSRO publishes statistical bulletins

Figure 2: Estimated stock of total contract price of QDCs/QSCs by financial year in which contract became a QDC/QSC, split by estimated cost and profit



Total estimated contract price

**£94.5
bn**

The SSRO is notified of Qualifying Defence Contracts (QDC) and Qualifying Sub-Contracts (QSC)

- What is a QDC?

A QDC is a contract made by the Secretary of State for goods, works or services for defence purposes from a 'primary contractor'. The award of the contract is not the result of a competitive process and the value of the contract is equal to or greater than £5 million*

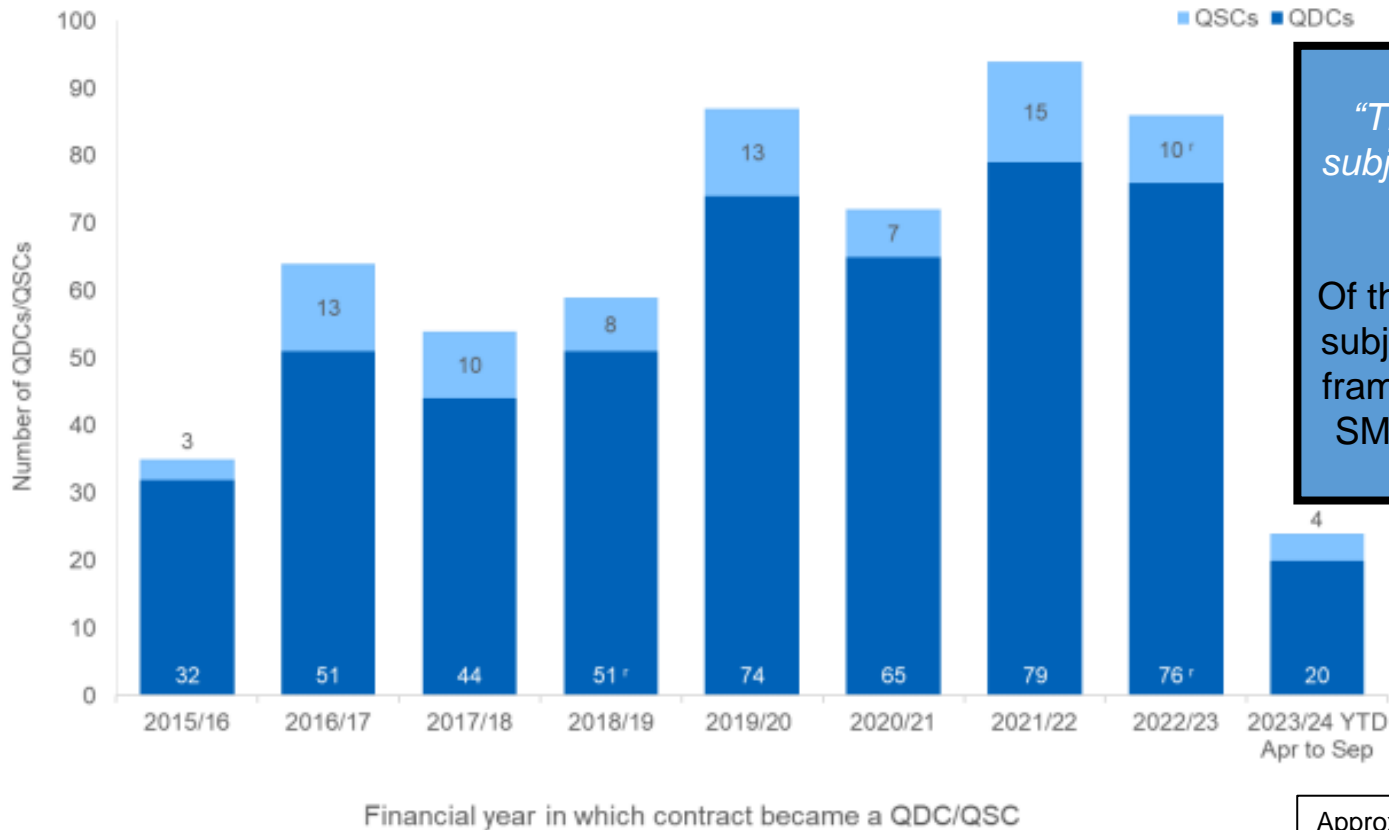
- A QSC is a non-competitive contract between a primary contractor and another contractor or between a sub-contractor and another contractor (minimum value £25 million)**
- There are exceptions which are set out in Regulation 7 (for example, contracts with foreign governments) or Secretary of State exemption.

*Section 14(2) of the DRA provides the full definition of a QDC

**Section 28(2) of the DRA provides the full definition of a QSC

As of 30 September 2023, 492 contracts became QDCs and 83 became QSCs

Figure 1: Number of QDCs/QSCs by financial year in which contract became QDC/QSC

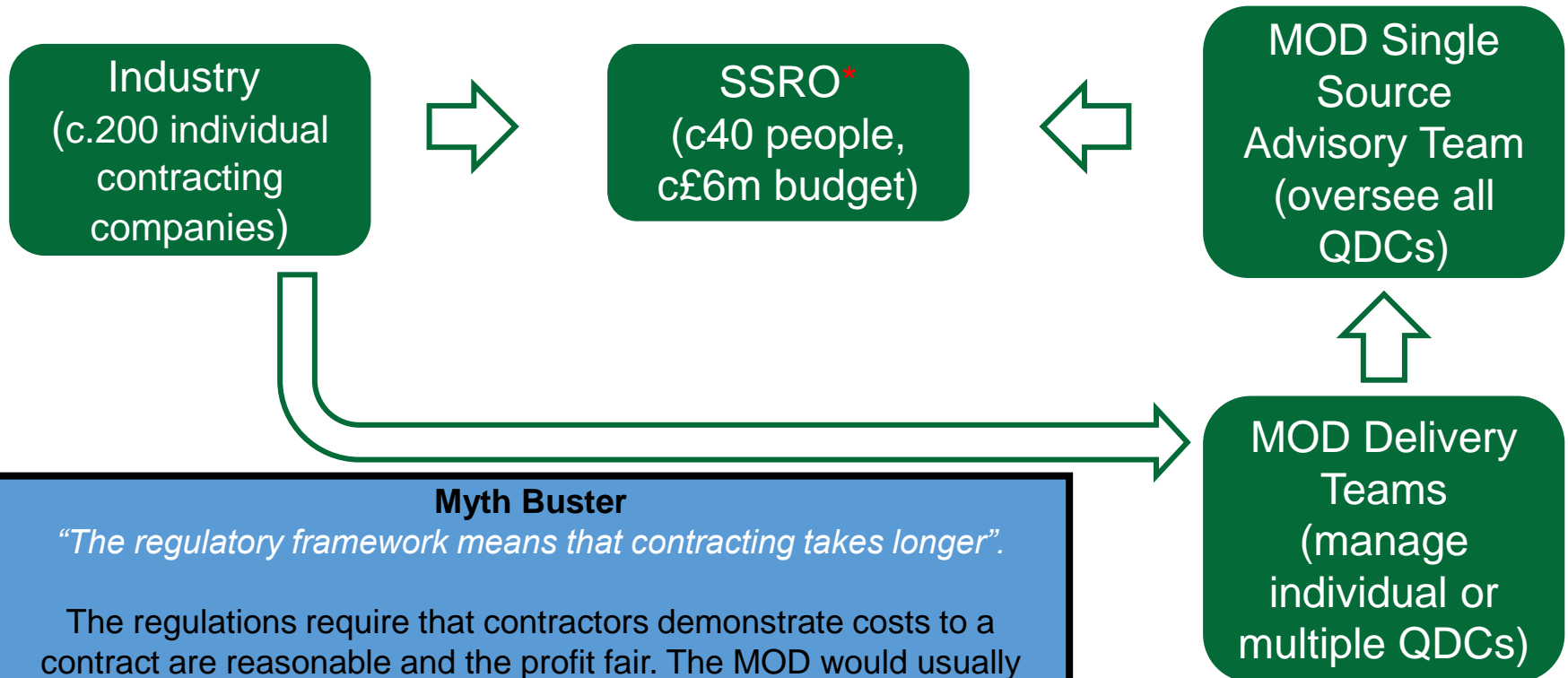


Myth Buster
“There are no SMEs subject to the regulatory framework”

Of the c. 200 companies subject to the regulatory framework, there are 26 SMEs. With a contract value \geq £100m

Approximately 8% of QDCs/QSCs are with non-UK contracting companies

The formal relationship between the SSRO and MOD is set by the Defence Reform Act and SSRO Framework Document



Myth Buster

"The regulatory framework means that contracting takes longer".

The regulations require that contractors demonstrate costs to a contract are reasonable and the profit fair. The MOD would usually require this information in any case.

The framework requires transparency on the part of defence contractors regarding prices. Larger suppliers may have to provide details about their strategic operations.

* The SSRO is sponsored by the MOD's Directorate of Sponsorship and Organisational Policy (DSOP)

MOD role in regulatory framework

The MOD sets the standards for consistent implementation of the Single Source Contract Regulations (SSCRs) across MOD and ensures MOD's obligations under the legislation are met.

The SSCR Casework team are the subject matter experts for the SSCRs and deal with approximately 200 complex queries a year with around a further 600 that are quickly resolved without needing formal tracking.

The SSCR Compliance and Data team ensure that the reporting obligations are complied with and that the MOD properly exploits the data.

The SSCR Review Team are responsible for reviewing the existing legislation and updating it where necessary

These three teams currently sit under the SSAT. As of January, the first two will sit under the Head of Performance and Scrutiny. The last one will be a separate team reporting the Director Commercial Functions

The SSRO has a range of functions to support the regulatory framework



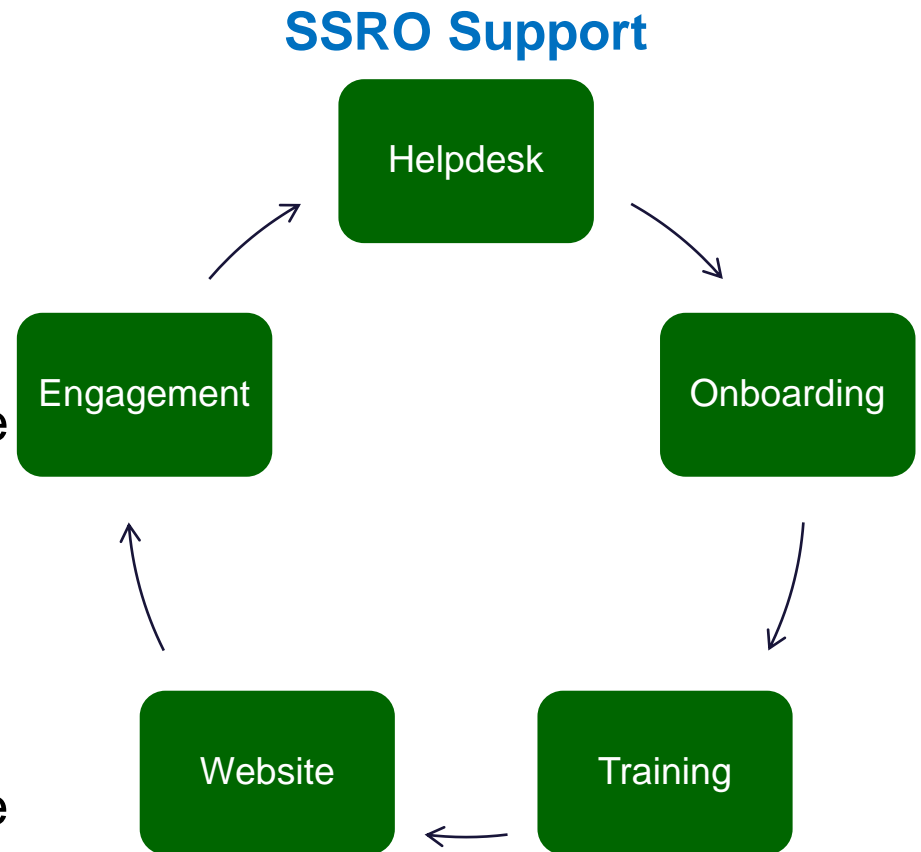
Myth Buster

“The SSRO is not impartial and sides with the MOD”

The SSRO is an arms’ length, has its own budget / Board. The MOD is not involved in SSRO day-to-day operations. The SSRO has ruled against the MOD on several occasions.

The SSRO support offering to you

- The SSRO is here to support you
- There is a comprehensive SSRO Support offering
- [Q&A document](#) receives good feedback and is a helpful source
- Encourage you to make early contact if you are to become subject to the regime
- The SSRO is looking to engage with you in your forums – please do invite



Support from the SSAT

- The SSAT provides support to delivery teams rather than suppliers.
- But if you think that your delivery teams are not applying the rules correctly, you can get in touch with the SSCR casework team.
- We will then form a view, and liaise with the delivery team. We may be involved in any subsequent discussions.
- The SSCR Casework team are also the MOD lead on referrals. They will usually attend any oral hearings, and may take overall lead from the delivery team.

Myth Buster

“The MOD can be inconsistent in the way it applies the SSCRs”

There are central bodies within the MOD who oversee use of SSCRs to ensure consistency of use.

If you think this is not the case please do let us know.

Pricing QDCs

The Defence Reform Act and the Single Source Contract Regulations require that the price payable under a qualifying contract be determined in accordance with the formula:

(Contract profit rate x Allowable Costs) + Allowable Costs



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Guidance on the baseline profit rate and its adjustment 2021/22
Version 7.1
Issued 5 August 2021
Applies from: 6 August 2021

Myth Buster

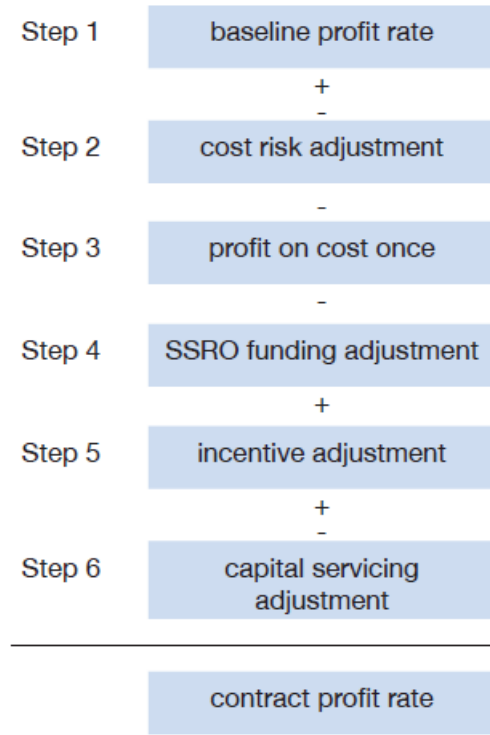
“Single sourcing and the SSCRs = difficult & laborious contracting”

Competitive contracting must also be priced – this is not single source specific.

The SSCR can be tailored: just ensure a fair price and have regard to SSRO guidance

SSRO guidance on the baseline profit rate and its adjustment can be found [here](#).

The Defence Reform Act specifies six steps used to determine the contract profit rate for qualifying defence contracts:



Myth Buster
“The profit rate is inflexible and stops contracting freedom”.

BPR is not the CPR!
 Your capital investment: Capital Servicing Adjustment
 Risk rewarded: Cost Risk Adjustment

Baseline Profit Rate

- The baseline profit rate is applied to QDCs and QSCs
- The SSRO recommends the baseline profit rate to the Secretary of State on an annual basis
- Alongside the rate, the SSRO publishes information on the methodology for calculating the rate, and provides information to aid those who may wish to scrutinise or replicate the approach taken
- The SSRO is confident that the methodology is correct and robust
- The rate for 2023/24 is 8.29 per cent

Our recommendation for 2023/24 can be found here:

<https://www.gov.uk/government/news/2023-contract-profit-rate>



Other Notices

SECRETARY OF STATE FOR DEFENCE

THE IMPLEMENTATION FROM 1 APRIL 2023 OF NEW PROFIT RATES FOR SINGLE SOURCE DEFENCE CONTRACTS

As required by Section 19(4) of the Defence Reform Act 2014, the Secretary for Defence has announced that he has set the baseline profit rate for single source defence contracts at 8.29%, based on an underlying rate of 8.44%. This is in line with the rate recommended by the Single Source Regulations Office (SSRO). It will come into effect from 1 April 2023.

In light of the profit rate used in future years the SSRO has reduced the effect of COVID by removing the year 2020/21 from the three year average.

The Secretary of State has also accepted the SSRO's recommendation on the Capital Servicing Allowance and SSRO funding adjustment to be applied to single source defence contracts. These will also come into effect from 1 April 2023.

Table 1: SSRO's Recommended Rates agreed by the Secretary of State for Defence

Element	2022 rates	2023 rates
Baseline Profit Rate (BPR) (% on contract cost)	8.31%	8.29%
Baseline Profit Rate to apply to contracts between the Secretary of State and a company wholly owned by the UK Government and where both parties agree (% on contract cost)	0.046%	0.038%
Fixed Capital Servicing Rate (% on Fixed Capital employed)	3.27%	2.9%
Working Capital Servicing Rate (% on positive Working Capital employed)	1.33%	1.67%
Working Capital Servicing Rate (% on negative Working Capital employed)	0.65%	0.51%
SSRO Funding Adjustment	0.046%	0.038%

Baseline profit rate approach and methodology



Objective

OECD: Transfer Pricing principles

Replicable



Reliable

Actual profit on actual cost

IFRS / GAAP numbers



Predictable

Stable approach

3 year rolling average



Calibrated

Stakeholder feedback (including QA of accounting data)

Completed contracts

Myth Buster
“Can’t make good level of profit through single sourcing”

The evidence does not point to companies with significant exposure to the regulatory framework performing financially poorer than their peers.
 Overheads are an Allowable Cost - if AAR

Company selection process



Allowable Costs

- Allowable Costs make up the majority of the contract price
- Costs must be **appropriate, attributable to the contract, and reasonable in the circumstances** to be an Allowable Cost
- The contract parties must have regard to the SSRO guidance in determining whether costs are Allowable Costs
- [Current guidance](#) (v6) applies from 7 November 2022

Myth Buster

“The guidance only applies to the contractor and not the MOD”.

The MOD is bound by the guidance as much as the contractor.

Myth Buster

“You can’t charge the MOD for bid costs”.

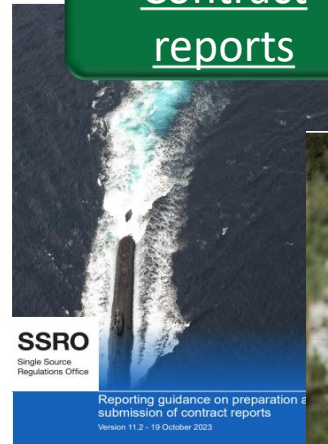
Bid costs, if AAR and agreed, are allowable.



SSRO reporting guidance is three documents

- The most recent reporting guidance update was published on 19 October 2023.
- Guidance is built in to DefCARS via use of links on each page to take users to the relevant section and is sent to new users.
- The guidance was developed in parallel with the system. Therefore, there will be elements that still need further development.
- The SSRO seeks and captures views through the Reporting and IT Sub-Group of the SSRO's Operational Working Group.

Contract reports



Supplier reports



DefCARS functionality



Myth Buster

“Nothing is done with the data that is collected under the regime”

The SSRO uses it to undertake analysis and provide the MOD with MI to inform their procurement

The SSRO is empowered to give opinions or make determinations on matters referred to it by the Secretary of State or contractors

- The legislation identifies:
 - the range of matters that may be referred
 - who may refer them
 - the circumstances in which referrals may be made
 - whether the SSRO may or must provide an opinion or determination
- Referrals can:
 - support the agreement of contract prices that are VFM and fair and reasonable
 - help to resolve contractual disagreements
 - clarify how the regulatory framework should be applied
 - generate insights that inform improvements in the regulatory framework
- Referral investigations are funded on a case-by-case basis

Myth Buster

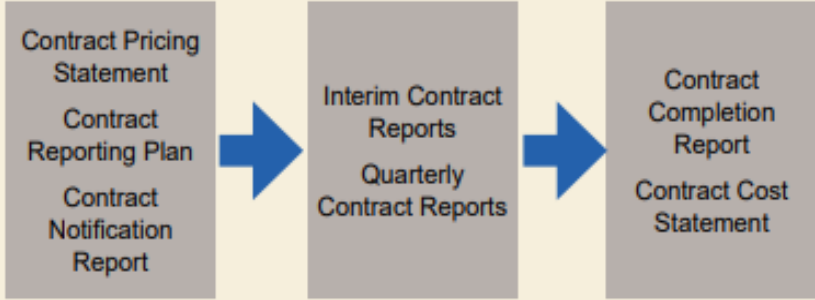
“Referrals are complex and time intensive”.

Referrals can help resolve complex contract issues.

The SSRO has worked with smaller companies in referrals.

The SSRO offers pre-referral support and is continuing to enhance it.

Contract reports relating to QDCs or QSCs and supplier reports are required by the Single Source Contract Regulations 2014

Report category	Reports
<p>Contract reports (Part 5 of the Regulations)</p> <p>Reports required for each QDC and QSC (some of which may additionally be required on-demand)</p> <p>Data about contract requirements, payments, estimated and actual costs, profit, delivery and sub-contracts.</p>	 <pre> graph LR A[Contract Pricing Statement Contract Reporting Plan Contract Notification Report] --> B[Interim Contract Reports Quarterly Contract Reports] B --> C[Contract Completion Report Contract Cost Statement] </pre>
<p>Supplier reports (Part 6 of the Regulations)</p> <p>Reports required about defence contractors when relevant triggers are met.</p> <p>Data about a contractor's overhead costs in standard categories, its strategic capacity and opportunities for SMEs in the supply chain.</p>	<p>Overhead reports</p> <ul style="list-style-type: none"> Estimated Rates Agreement Pricing Statement Estimated Rates Claim Report Actual Rates Claim Report QBU Estimated Cost Analysis Report QBU Actual Cost Analysis Report Rates Comparison Report (on demand) <p>Strategic reports</p> <ul style="list-style-type: none"> Strategic Industry Capacity Report Small or Medium Enterprises Report

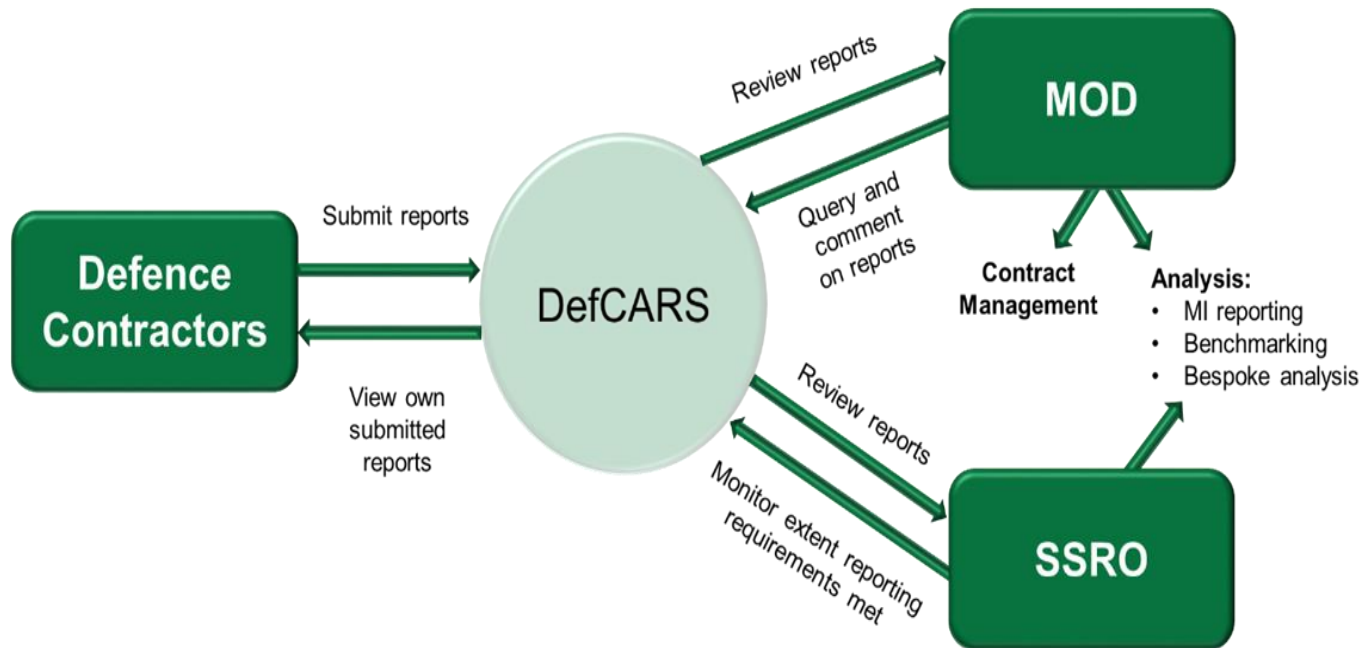
Myth Buster
“There is a reporting burden associated with being subject to the regulatory framework”.

Most SMEs won't have supplier reports. Frequency of reports can be tailored to value of the contract.

Can build in cost of reporting to contract bid, as an Allowable Cost.

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

The Defence Contracts Analysis and Reporting System (DefCARS) is the central system for the capture, storage and analysis of all data submitted in accordance with statutory reporting requirements



Myth Buster
“Using DefCARS is complicated”.

You will need training to use the system, but the SSRO provides this and its Helpdesk can assist throughout the life of the contract.

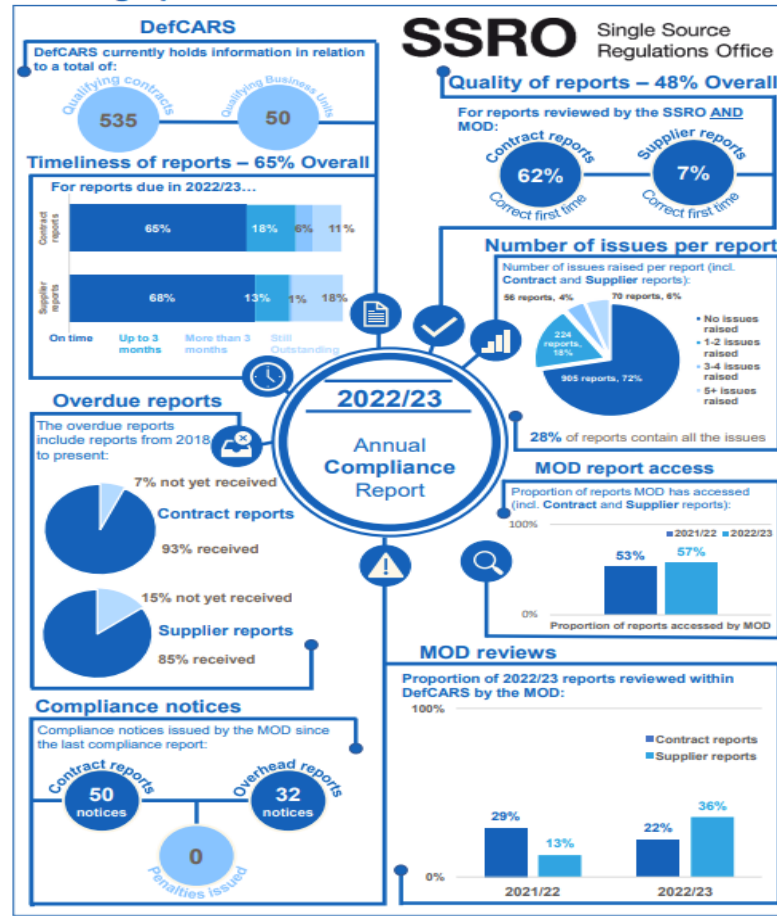
- All queries and comments on reports are within the system, rather than via email correspondence.
- As well as the live system there is a potential QDC and training environment

Annual Compliance Report 2023

[Link](#) to report

- 65 per cent of contract reports and 68 per cent of supplier reports were received on time in 2022/23.
- 62 per cent of contract reports and 7 per cent of supplier reports were submitted right first time.
- 89 per cent of contract report submissions and 82 per cent of supplier overhead report submissions are received, however often this is post the report due dates.
- The MOD issued 82 compliance notices against late reports since the last compliance report. This is a significant increase to the 12 notices issued last year and resulted in 68 (83 per cent of those with a notice) additional submissions

1. Infographic

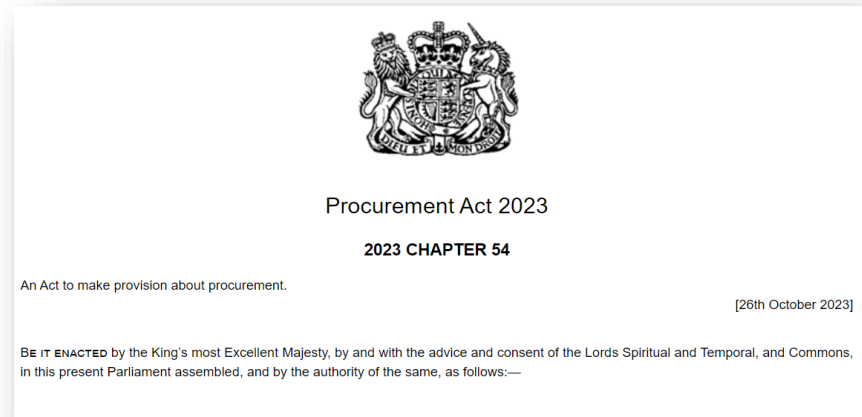


Myth Buster
“SSRO is there to catch you out”.
SSRO is there to help you comply with the regulatory framework.

Myth Buster
“SSAT is there to catch you out”.
MOD wants to get high quality data / information that is useful

Procurement Act updates the Single Source Contract Regulations

- Considerable changes to the existing regulatory framework
- Two steps removed from the contract profit rate calculation
- Flexibility introduced through use of alternative pricing methods of contracts; and componentisation
- The SSRO will support industry and the MOD through these changes: updating guidance; DefCARS and training



Myth Buster

“The legislation and Regulations have been developed in isolation”.

MOD has led development alongside stakeholder engagement.
Not looking to change legislation to stop procurement problems but to solve procurement problems that exist

SSRO Support – a variety of ways to help you

Helpdesk

Approximately
950 queries a
year

Onboarding

c. 2 or 3
sessions a
month

Training

Up to eight
sessions a year

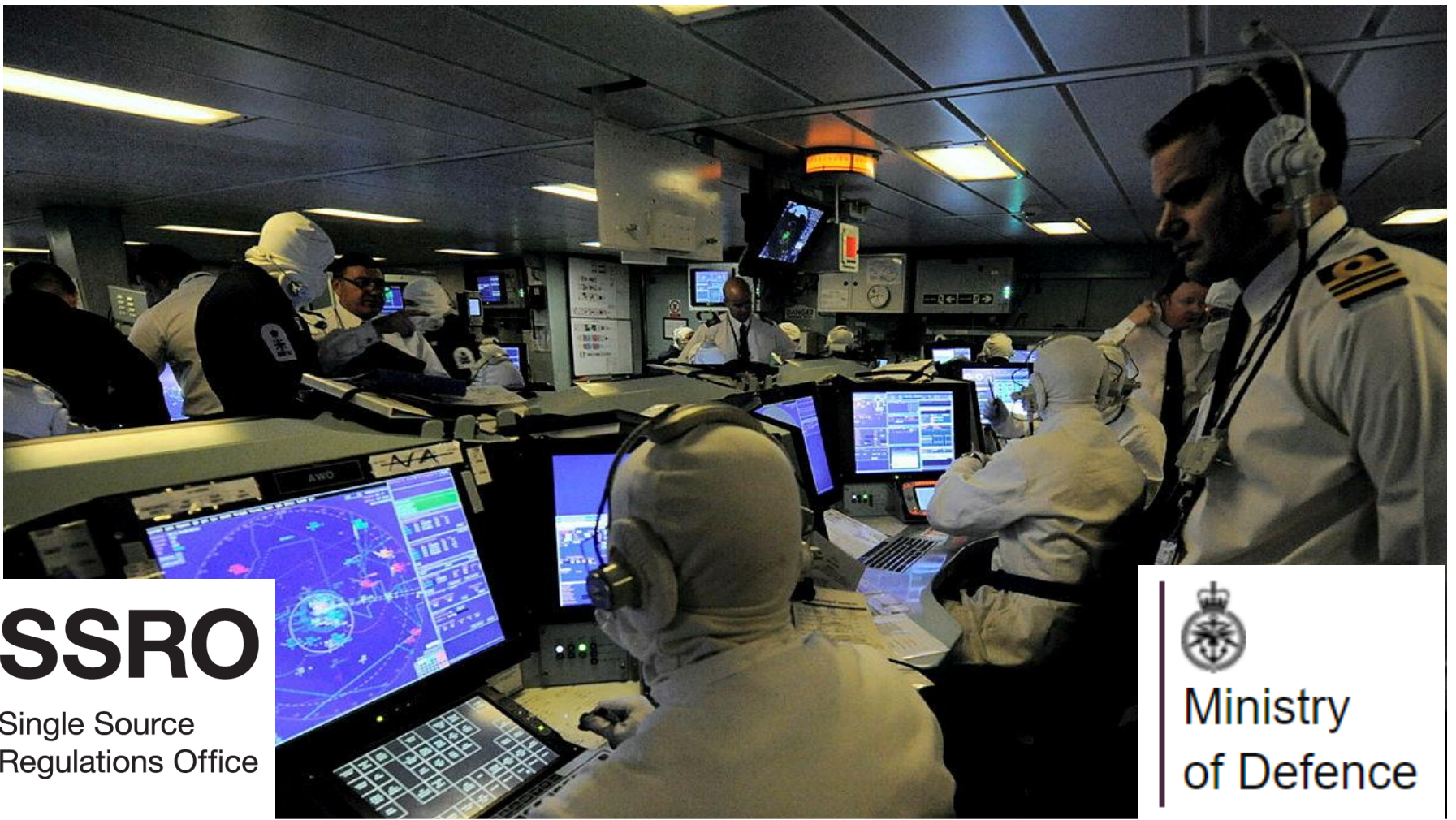
Website

Improvements
planned

OWG &
R&ITSG

Five set
meetings a year

- SSRO Support is a key engagement mechanism for the organisation
- Multiple points of contact for stakeholders
- The SSRO first looks to help the stakeholder but will also use the nature of stakeholder information / insight to improve SSRO Support
- Stakeholder satisfaction with what the SSRO offers is high



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Any questions?