

# SSRO

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Regulations Office

*Assuring value, building confidence*

## Profit rate consultation – chart pack

29 September 2016

## Key terms and definitions

**Comparability principle** - The aim of the baseline profit rate is to provide the starting point in the determination of the contract profit rate (totalling steps one to six). It is set with reference to the returns of comparable companies whose economic activities are included in whole or in part in the activity types that contribute to the delivery of QDCs and QSCs.

**Activity type** – A group of economic activities, defined by the SSRO, which correspond to types of activity that contribute to the delivery of QDCs and QSCs. For example ‘Develop and Make’, ‘Provide and Maintain’, ‘Ancillary Services’ or ‘Construction’. In practice, activity types are defined as distinct groups of NACE codes and text search terms.

**Comparable company** – A company whose economic activities are included, in whole or in part, within an activity type.

**Comparator group** – A group of comparable companies undertaking one or more of the economic activities which make up an activity type.

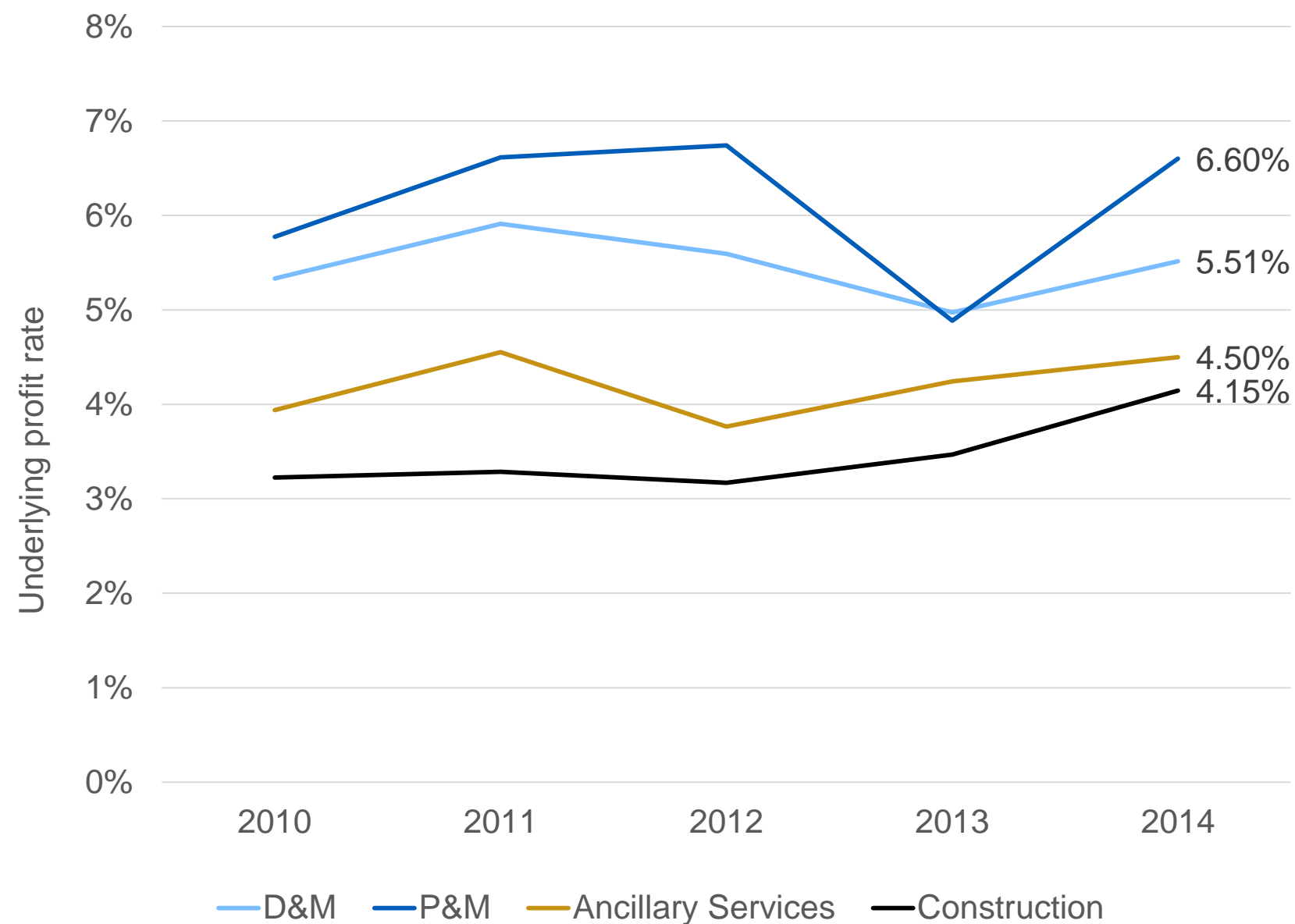
**Economic activity** – An activity that involves the production, distribution and consumption of goods and services.

**NACE code** – The European Union system of classifying economic activities for the purpose of statistical and other analysis. The SSRO uses NACE codes in conjunction with text search terms to identify comparable companies within the Orbis database.

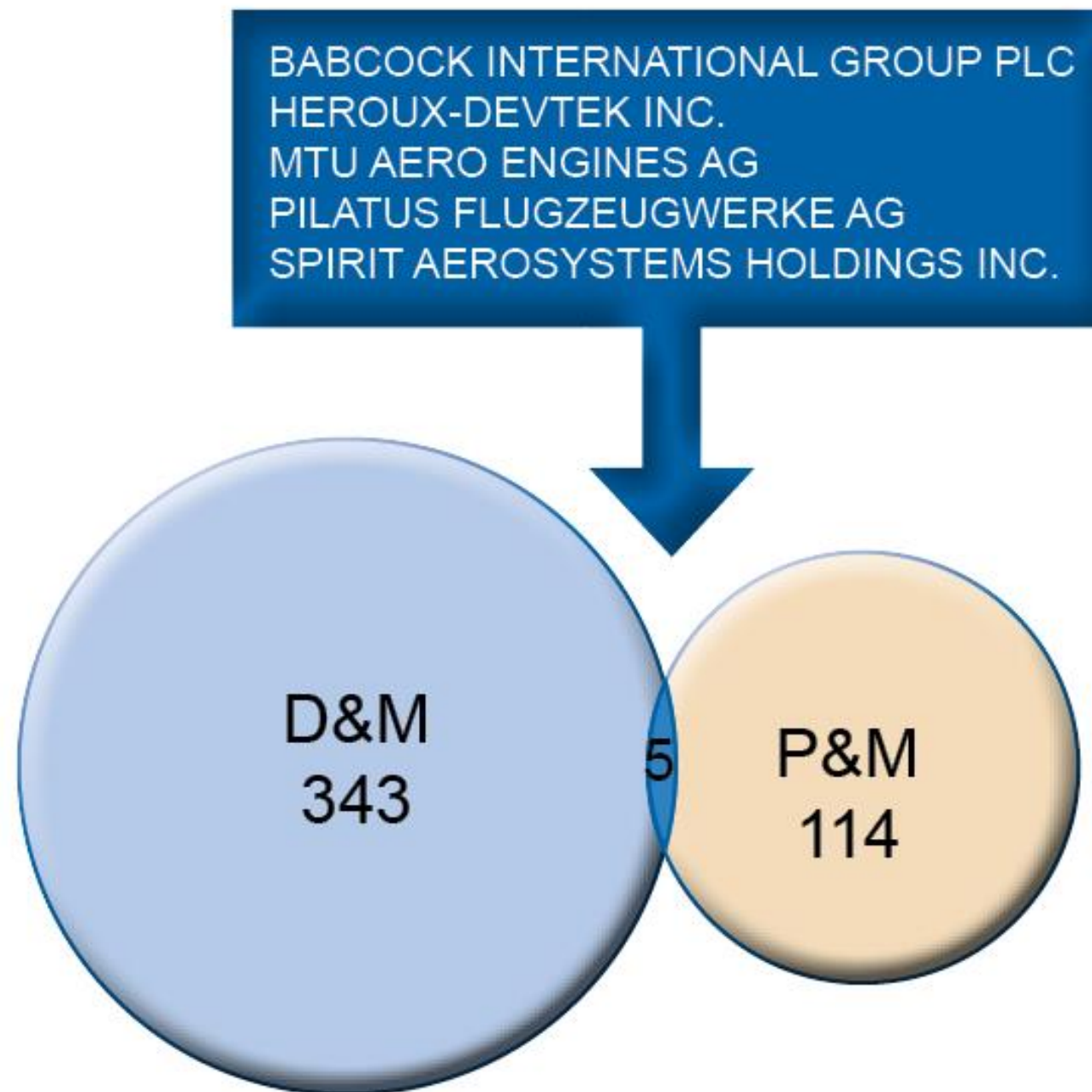
**Orbis** – The database of company-specific information and data supplied by Bureau van Dijk. The SSRO uses this to identify comparable companies and as a source of financial data on those comparable companies for use in the calculation of the baseline profit rate.

**Text search term** – A word or group of words relating to economic activities used to identify comparable companies. For example ‘manufacture’ or ‘production’. The SSRO uses text search terms in conjunction with NACE codes to identify comparable companies within the Orbis database.

## Underlying profit rate for activity type comparator groups 2010 to 2014

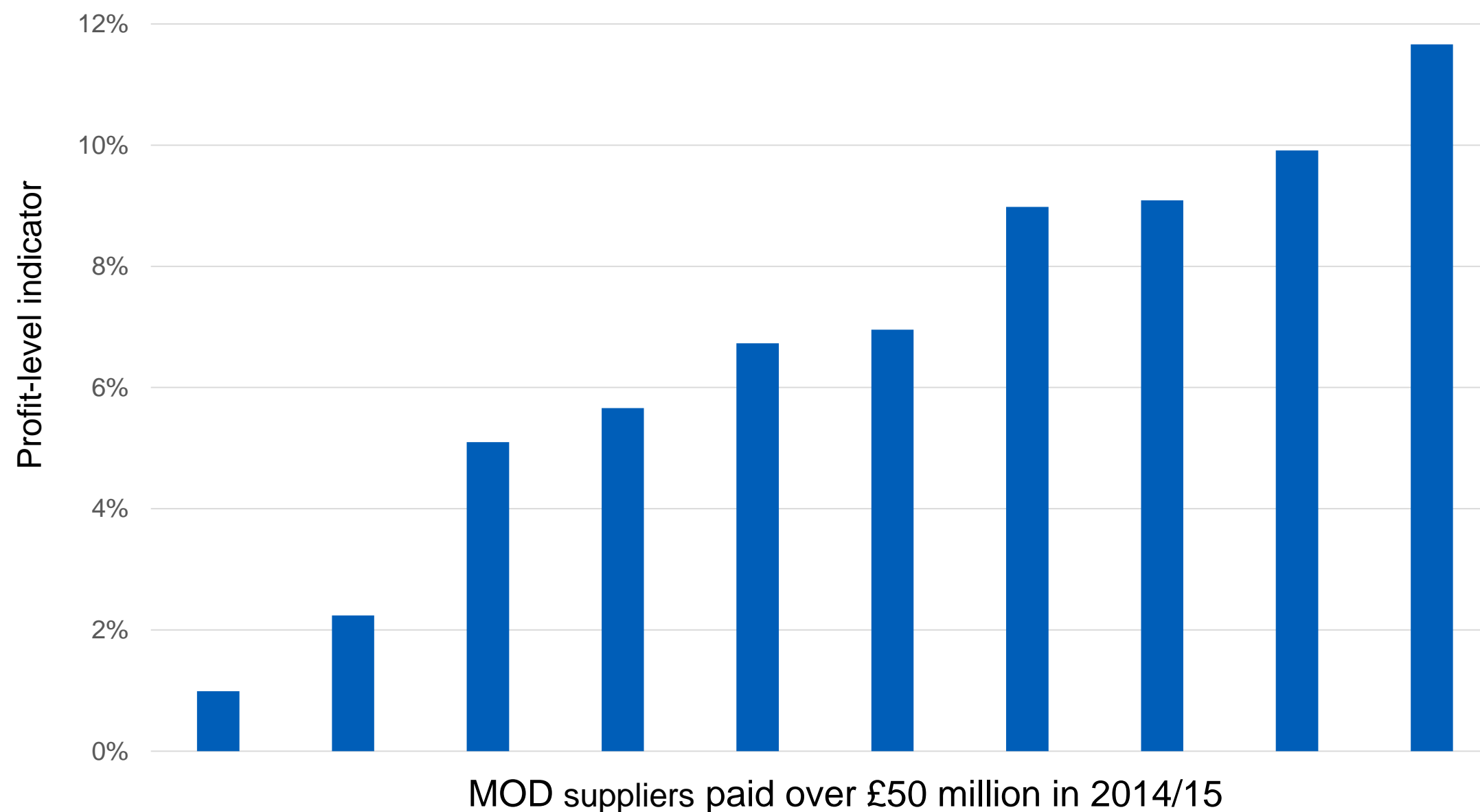


## The comparator groups



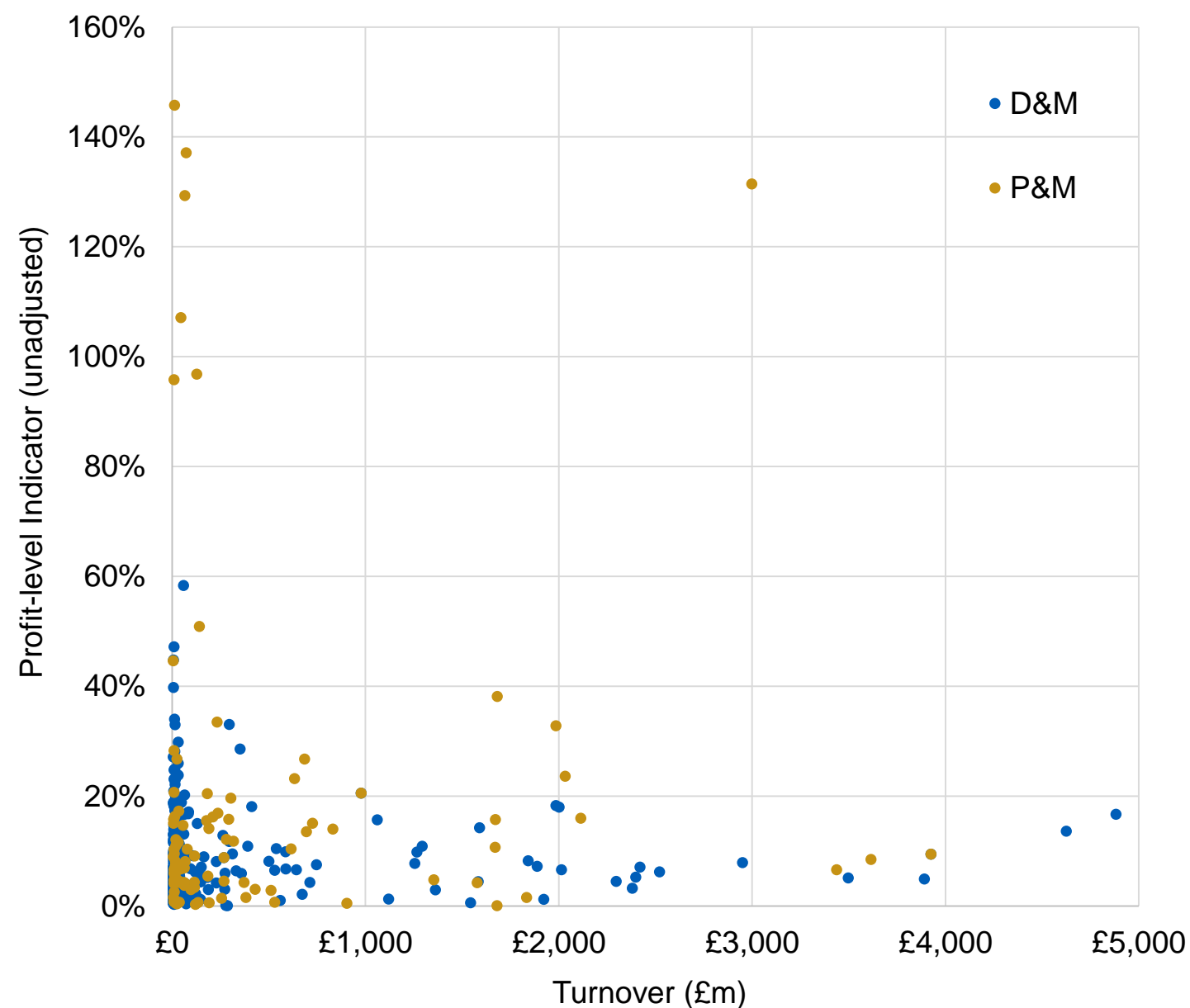
[Numbers before the exclusion of most-recent-year loss-makers]

## The range of profit-level indicator for the main MOD suppliers in the 2016/17 BPR comparator groups



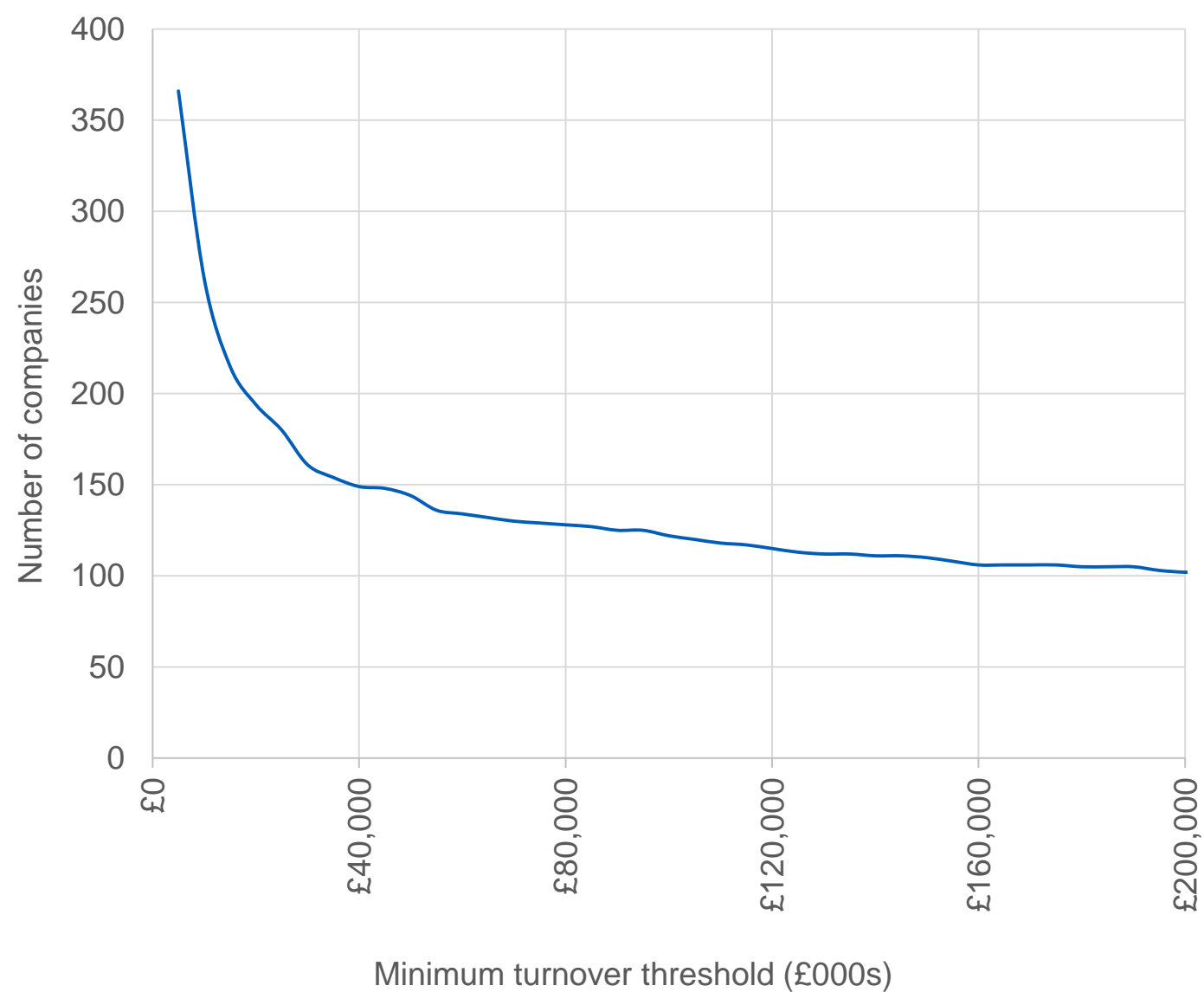
## Turnover and profit: 2015/16

Comparing company turnover with profit (return on cost) for companies included in the D&M and P&M comparator groups for the 2016/17 BPR calculation

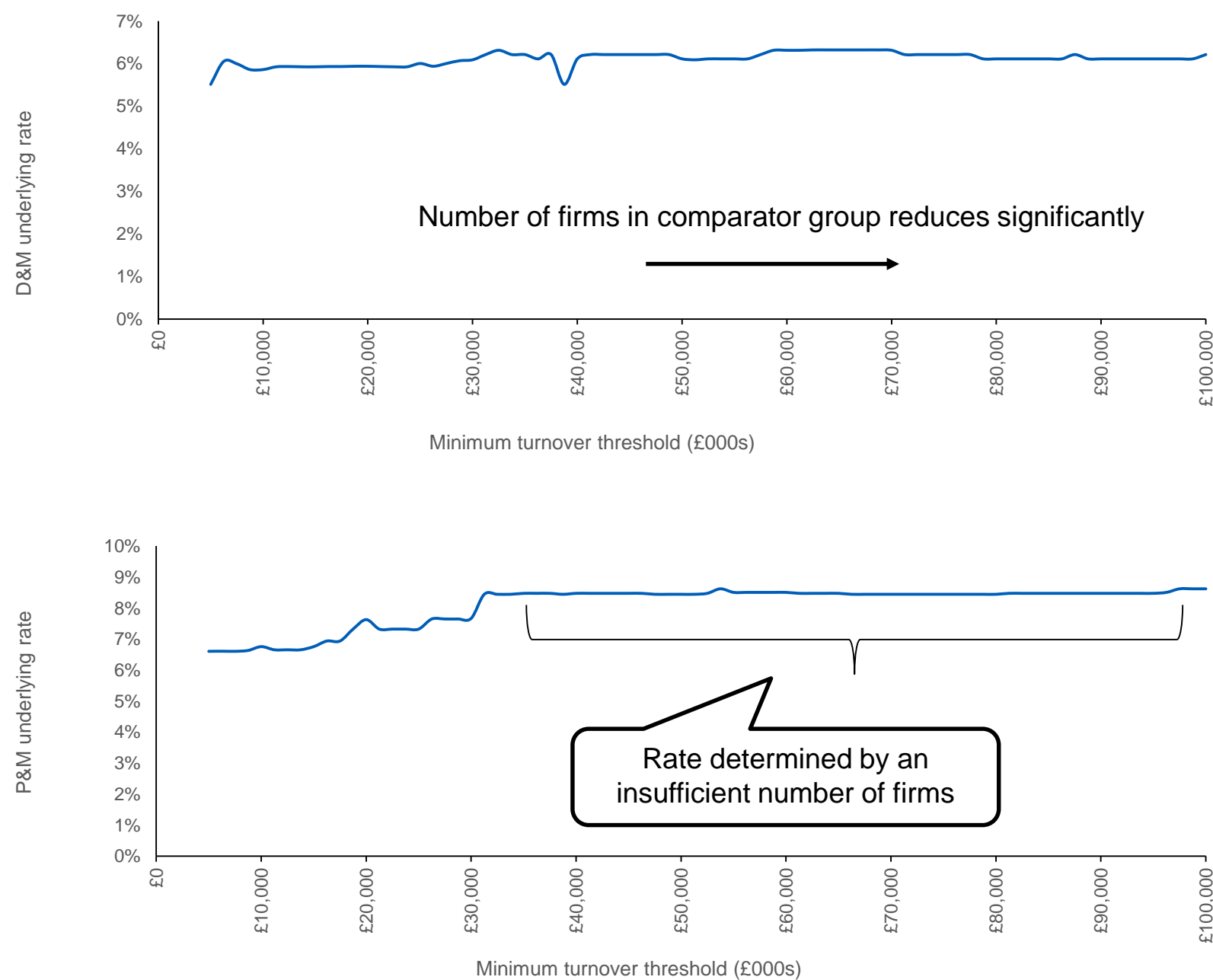


## Turnover threshold and comparator basket size

Number of companies in 2016/17 D&M and P&M comparator groups that pass a given minimum turnover threshold



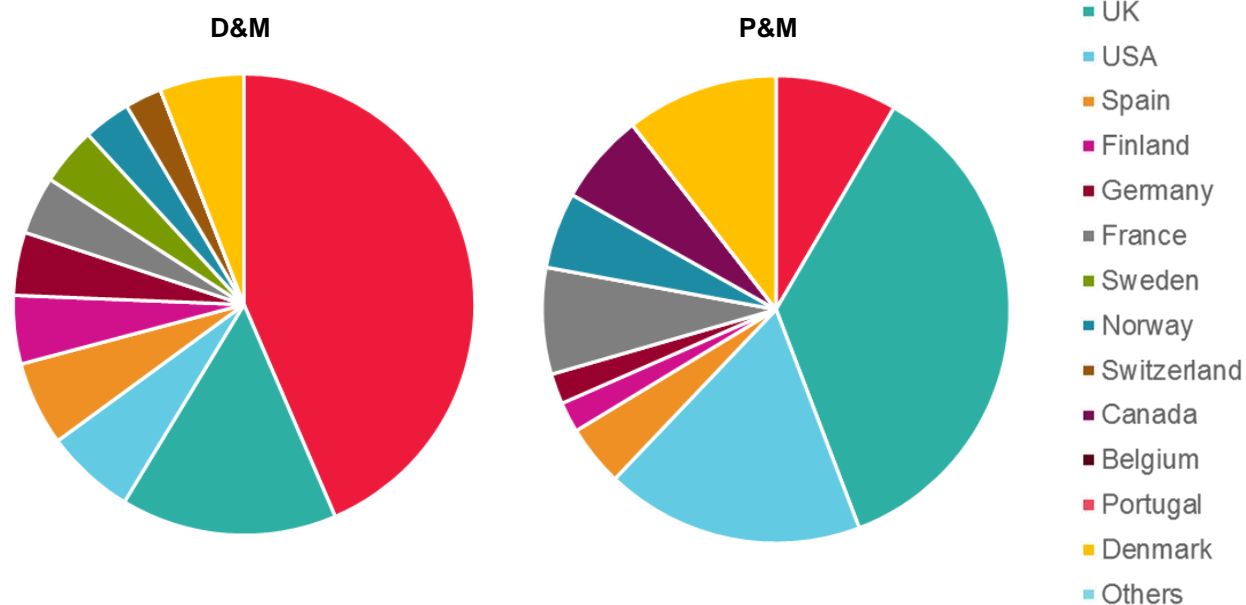
## Profit rates and the turnover threshold



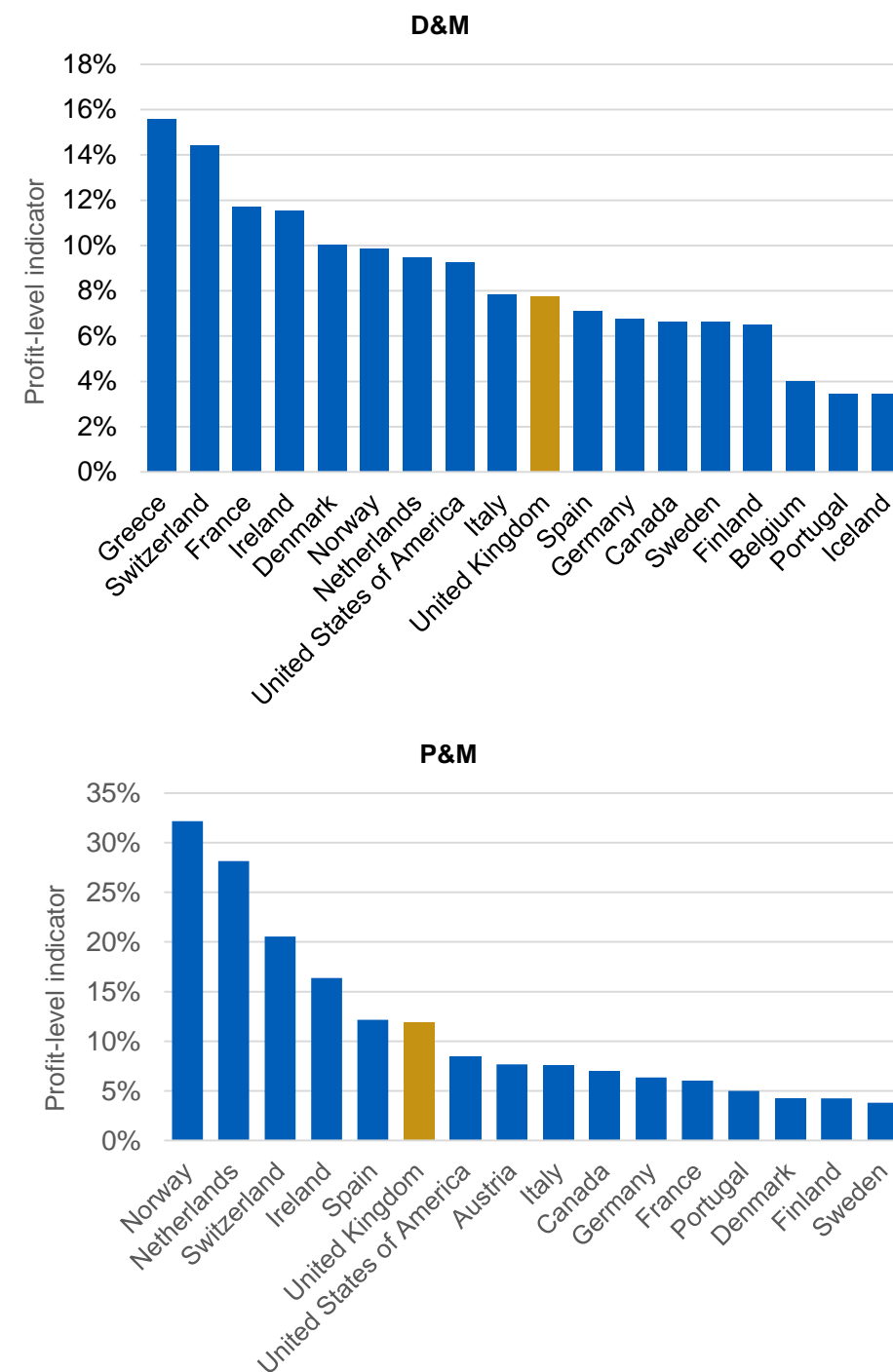


## Geographic analysis

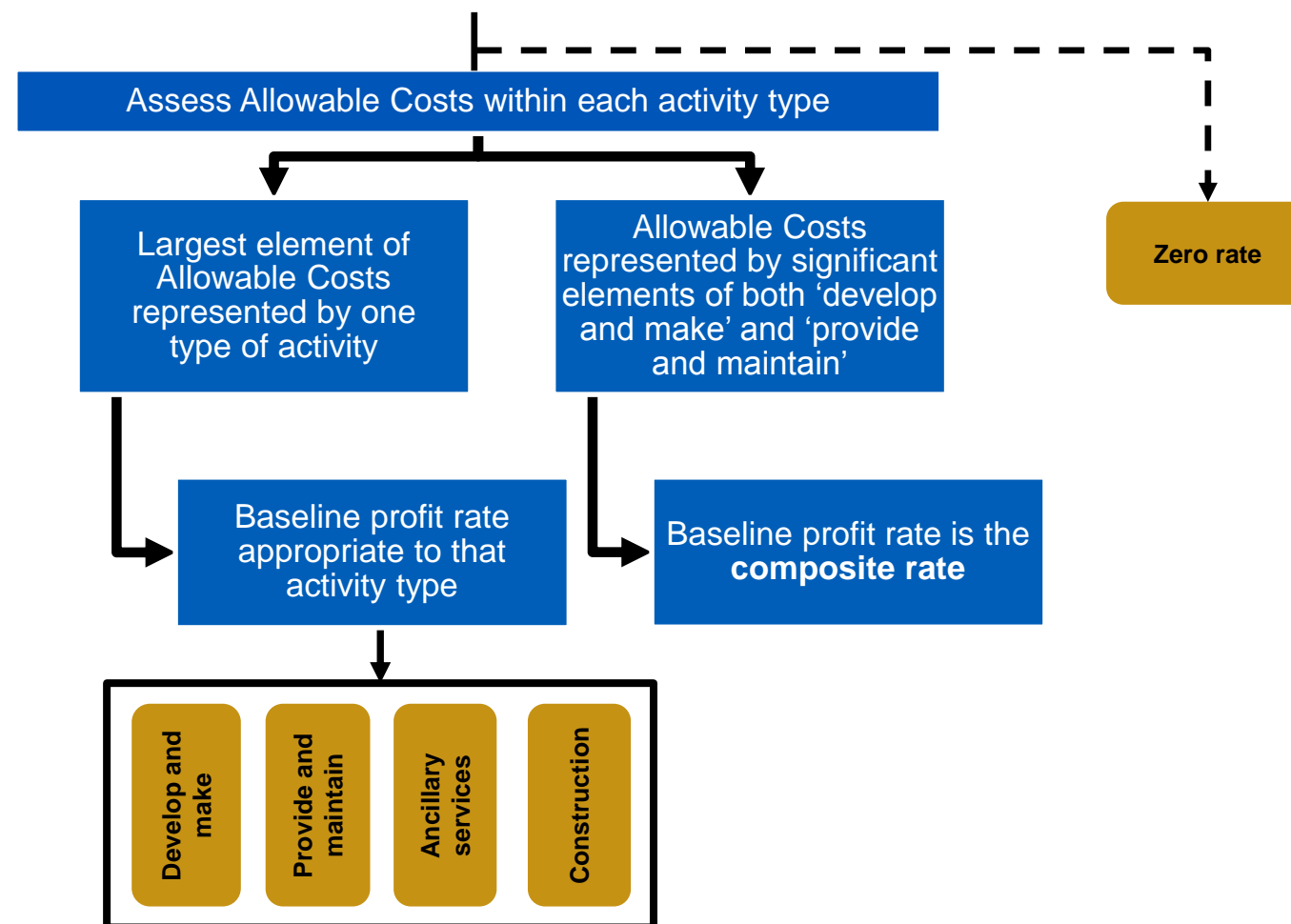
Number of firms included in 2016/17 BPR analysis by country



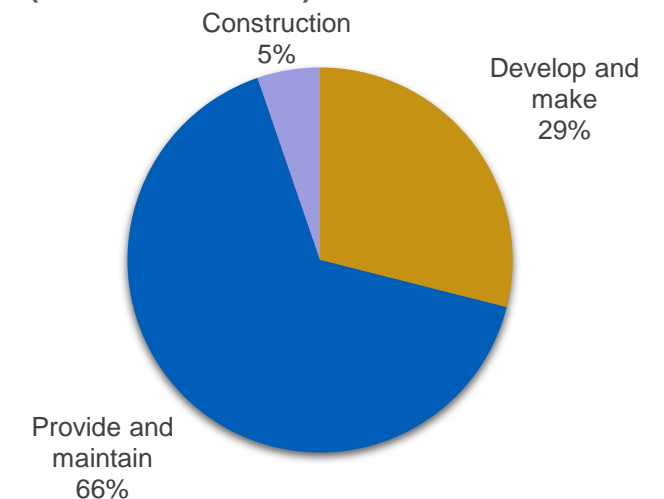
Average net cost plus margin for comparable companies by country



# Choosing the appropriate baseline profit rate



**First 38 QDCs/QSCs by activity type category  
(as at 1 June 2016) - contract numbers**

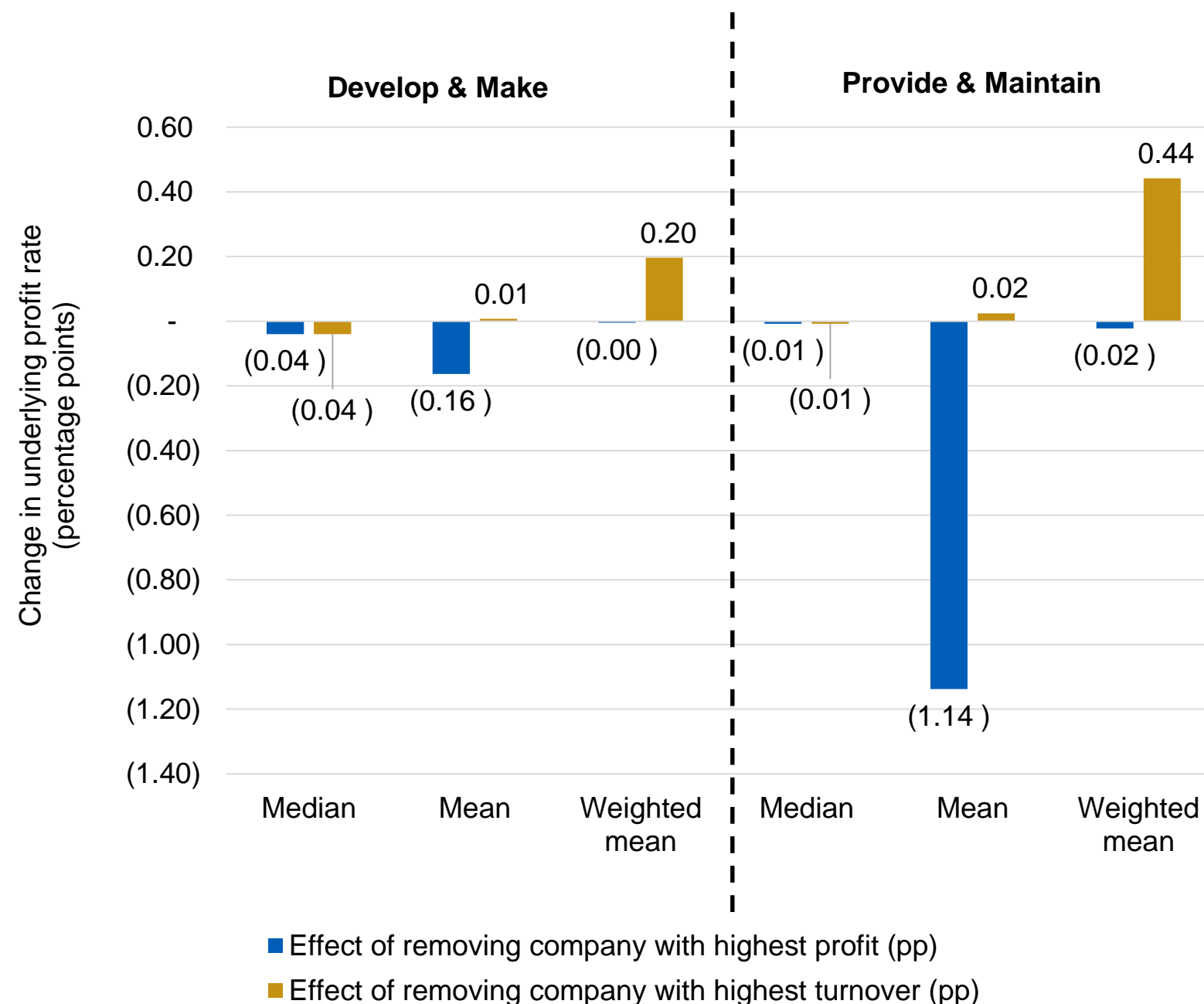


## The CADMID cycle and the BPR

CADMID – The basic activities of each phase (MOD acquisition framework)	Profit rate description	Develop and make	Provide and maintain	
		<p>This category includes manufacturing or assembly of goods or equipment to order based on designs or specifications provided. It also covers the disposal of equipment, the purchase of long-lead items for manufacture, prime contracting and systems integration and upgrade activities.</p>	<p>It also includes research, design and development of technical intellectual property for goods, equipment, engineering or software performed to order, typically in line with any agreed design brief or specification.</p>	<p>This category includes any work undertaken that either provides the MOD with a capability where the contractor owns the assets, or where the contract covers work on in-service equipment.</p> <p>It includes servicing and upkeep for the MOD owned equipment, including ongoing engineering and maintenance and includes training related to the introduction and operation of equipment.</p>
		<p><b>Assessment</b></p> <ul style="list-style-type: none"><li>• Reduce risk to a level consistent with delivering an acceptable level of system performance to tightly controlled time and cost parameters.</li></ul> <p><b>Manufacture</b></p> <ul style="list-style-type: none"><li>• Deliver the solution to the military requirement within the time and cost limits.</li><li>• Conduct System Acceptance to confirm that the system satisfies the SRD and the URD, as agreed at Main Gate.</li><li>• Transfer the lead customer function to the User, for equipment.</li></ul> <p><b>Disposal</b></p> <ul style="list-style-type: none"><li>• Carry out plans for efficient, effective and safe disposal of the equipment.</li></ul>	<p><b>Concept</b></p> <ul style="list-style-type: none"><li>• Produce a statement of the outputs that users require from the system, framed as a User Requirements Document (URD).</li><li>• Form the delivery team.</li><li>• Involve industry.</li><li>• Identify technology and procurement options for meeting the requirement that merit further investigation.</li><li>• Obtain funding and agree plan for the Assessment (in detail) and subsequent stages (in outline), identifying performance, cost and time boundaries within which it is to be conducted.</li><li>• Initiate the Through Life Management Plan (TLMP).</li></ul> <p><b>Assessment</b></p> <ul style="list-style-type: none"><li>• Produce the System Requirements Document (SRD), defining what the system must do to meet user needs as stated in the URD.</li><li>• Establish and maintain the linkage between user and system requirements.</li><li>• Identify the most cost-effective technological and procurement solution.</li><li>• Develop the SRD, trading time, cost and performance to identify the technological solution.</li><li>• Reduce risk to a level consistent with delivering an acceptable level of system performance to tightly controlled time and cost parameters.</li><li>• Refine the TLMP, including detailed plans for the Demonstration phase.</li><li>• Continuously monitor project maturity and, when appropriate, construct and submit a Main Gate Business Case seeking approval for the project within tightly defined performance, time and cost boundaries.</li></ul> <p><b>Demonstration</b></p> <ul style="list-style-type: none"><li>• Eliminate progressively the development risk and fix performance targets for manufacture, ensuring there is consistency between the final selected solution and the SRD and URD.</li><li>• Place contract(s) to meet the SRD.</li><li>• Demonstrate the ability to produce integrated capability.</li></ul>	<p><b>In-Service</b></p> <ul style="list-style-type: none"><li>• Confirm the Defence capability provided by the system is available for operational use, to the extent defined at Main Gate, and declare the In-Service Date (ISD) in service date.</li><li>• Provide effective support to the front line.</li><li>• Maintain levels of performance within agreed parameters, whilst driving down the annual cost of ownership.</li><li>• Carry out any agreed upgrades or improvements, refits or acquisition increments.</li></ul>

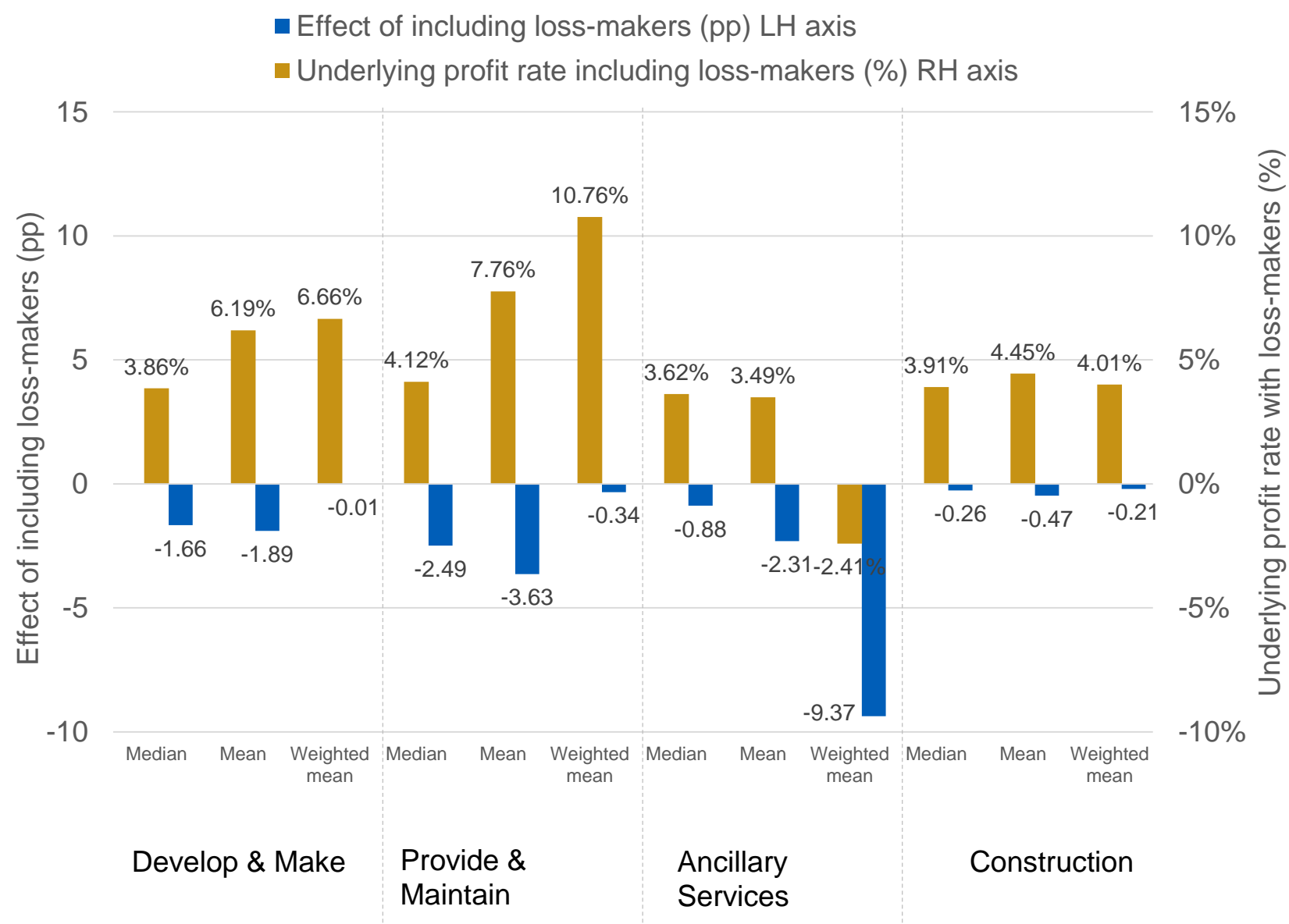
# The robustness of the median

The influence of untypical cases on measures of central tendency in the 2016/17 comparator groups



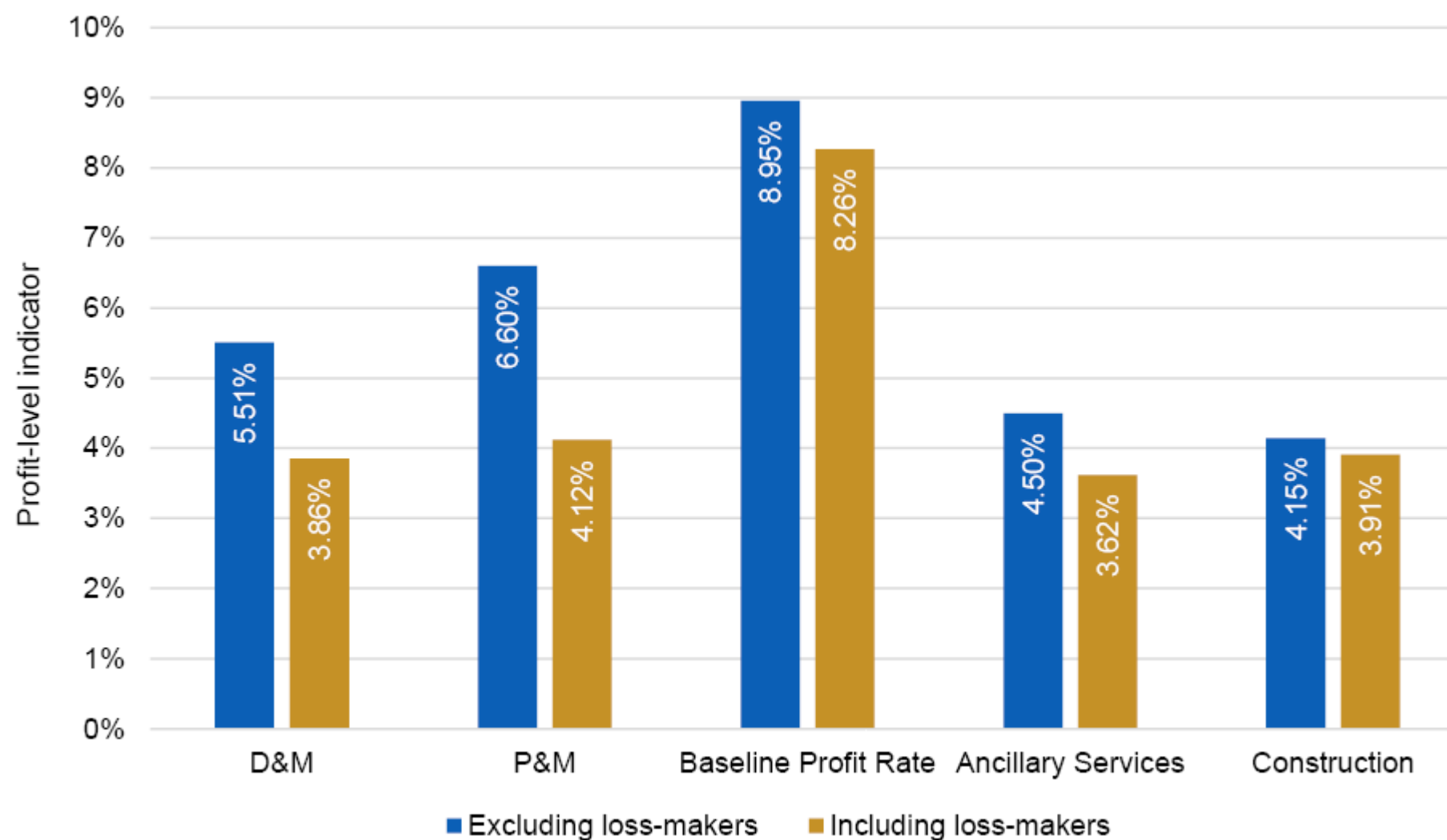
# The robustness of the median

Effect on different average measures of including loss makers in the analysis of underlying profit rates



## The impact of loss makers

Median profit rate for each comparator group when including/excluding loss-makers



## The capital servicing adjustment

Distribution of comparable company profit-level indicators with and without the capital servicing adjustment

