

Defence Reform Act 2014

2014 CHAPTER 20

PART 2

SINGLE SOURCE CONTRACTS

Pricing of contracts

15 Pricing of contracts

- (1) Single source contract regulations must make provision about determining the price payable under a qualifying defence contract to the primary contractor.
- (2) The regulations must provide for the price payable under the contract to be determined in accordance with the formula in subsection (4).
- (3) The regulations must provide that where the Secretary of State and the primary contractor propose to amend the contract in a way that would affect the price determined by virtue of subsection (2) or this subsection—
 - (a) the price payable under the amended contract must be re-determined in accordance with the formula in subsection (4), or
 - (b) the price payable in respect of the amendment must be determined in accordance with that formula.
- (4) The formula is—

$$(CPR \times AC) + AC$$

where—

- (a) "CPR" is the contract profit rate for the contract (see section 17), and
- (b) "AC" means the primary contractor's allowable costs under the contract (see section 20).
- (5) The regulations may provide for a determination by virtue of subsection (2) or (3) to be made at such times as may be specified in the regulations (and different times may be specified for different kinds of contract).

16 Pricing of contracts: supplementary

- (1) Single source contract regulations may specify circumstances in which, if the Secretary of State and the primary contractor so agree—
 - (a) the price determined in accordance with section 15 is to be taken as a target price, and
 - (b) the total price payable under the contract is subject to adjustment by reference to any difference between—
 - (i) the amount of the primary contractor's actual allowable costs under the contract, and
 - (ii) the amount of the estimated allowable costs used for the purpose of determining the target price.
- (2) The amount of any adjustment by virtue of subsection (1)(b) must be determined—
 - (a) by agreement between the Secretary of State, or an authorised person, and the primary contractor, or
 - (b) by the SSRO, where the matter is referred to it by the Secretary of State, an authorised person or the primary contractor.
- (3) Section 21 (final price adjustment) does not apply to a contract in a case where an agreement of a kind mentioned in subsection (1) has effect.

17 Contract profit rate

- (1) Single source contract regulations must make provision for determining the contract profit rate for a qualifying defence contract.
- (2) The regulations must provide for the determination to be made by taking the following sequence of steps, subject to section 18(2)—

Step 1

Take the baseline profit rate (see section 19) which is in force at the relevant time.

"The relevant time" means—

- (a) in a case within section 15(2)—
 - (i) when the contract is entered into, if the contract is a qualifying defence contract by virtue of section 14(3), or
 - (ii) when the contract is amended, if the contract is a qualifying defence contract by virtue of section 14(4) or (5);
- (b) in a case within section 15(3), when the contract is amended.

Step 2

Adjust that rate by an agreed amount, being an amount falling within specified parameters above or below the baseline profit rate, so as to reflect the risk of the primary contractor's actual allowable costs under the contract differing from its estimated allowable costs.

"Specified" means specified in the regulations.

Step 3

Deduct an agreed amount from the amount resulting from step 2, so as to ensure that profit arises only once in relation to those allowable costs under the contract in respect of which the regulations provide that a deduction may be made (and see section 20 as to allowable costs).

Step 4

Deduct the SSRO funding adjustment (see section 19) which is in force at the time mentioned in step 1 from the amount resulting from step 3.

Step 5

Where the Secretary of State determines that the amount resulting from step 4 should be increased so as to give the primary contractor a particular financial incentive as regards the performance of provisions of the contract specified by the Secretary of State, increase that amount by an amount specified by the Secretary of State.

Any increase must not exceed the maximum increase permitted by the regulations.

Step 6

Take the amount resulting from step 5 and add to or subtract from it an agreed amount, so as to ensure that the primary contractor receives an appropriate and reasonable return on the fixed and working capital employed by the primary contractor for the purposes of enabling the primary contractor to perform the contract.

This adjustment—

- (a) is to be made having regard to the capital servicing rates determined under section 19, but
- (b) does not apply to the extent that the costs of the fixed and working capital employed by the primary contractor are allowable costs under the contract.
- (3) The contract profit rate is—
 - (a) the amount found at the end of step 6 in subsection (2), or
 - (b) in a case where step 6 is disapplied under section 18(2)(a), the amount found at the end of the last of the steps in subsection (2) that apply in that case.
- (4) For the purposes of subsection (2)—
 - (a) "agreed" means agreed by the Secretary of State, or an authorised person, and the primary contractor;
 - (b) the adjustment agreed under step 2, 3 or 6 may be zero.

18 Contract profit rate: supplementary

- (1) The Secretary of State or an authorised person, and the primary contractor, must have regard to guidance issued by the SSRO in relation to any of the steps set out in section 17(2).
- (2) Single source contract regulations may—
 - (a) disapply the requirement to take any or all of steps 2 to 6 in section 17(2) in relation to a qualifying defence contract the value of which is less than the amount specified for the purposes of this paragraph;
 - (b) provide for any or all of those steps to apply in relation to such a contract with modifications set out in the regulations;
 - (c) where the Secretary of State is a party to a group of qualifying defence contracts with the same primary contractor, provide for section 17(2) to apply in relation to those contracts—
 - (i) taken together or individually, and

- (ii) with such modifications as may be set out in the regulations.
- (3) Single source contract regulations may provide that the SSRO—
 - (a) may, on an application by a person within subsection (4), determine whether the amount of an adjustment agreed under step 2, 3 or 6 in section 17(2) is appropriate;
 - (b) may, in consequence of a determination by virtue of paragraph (a) that the amount of such an adjustment is not appropriate, determine that the price payable under the contract is to be adjusted by an amount specified by the SSRO.
- (4) The following persons are within this subsection—
 - (a) the Secretary of State,
 - (b) an authorised person, and
 - (c) the primary contractor.

19 Rates etc relevant to determining contract profit rate

(1) The Secretary of State must, for each financial year, determine—

the baseline profit rate,

the SSRO funding adjustment,

the capital servicing rate for fixed capital, and

the capital servicing rate for working capital.

- (2) For the purpose of assisting the Secretary of State in determining for a financial year each of the rates mentioned in subsection (1) and the SSRO funding adjustment, the SSRO must provide the Secretary of State with its assessment of what is the appropriate rate or funding adjustment for that year.
- (3) The SSRO—
 - (a) must provide its assessment to the Secretary of State no later than 31 January in the preceding financial year, and
 - (b) must, in preparing its assessment, have regard to such matters as may be specified in guidance issued by the Secretary of State (as well as other matters that appear to the SSRO to be relevant).
- (4) The Secretary of State must publish each of the rates mentioned in subsection (1) for a financial year, and the SSRO funding adjustment for that year, in the London Gazette no later than 15 March in the preceding financial year.
- (5) Subsection (6) applies if, in the case of a particular rate or the SSRO funding adjustment, there is a difference between the rate or funding adjustment determined under subsection (1) and the SSRO's assessment of the appropriate rate or funding adjustment for the financial year in question.
- (6) The Secretary of State must, when publishing the relevant rate or the funding adjustment, also publish reasons for the difference.

20 Allowable costs

(1) The SSRO must issue guidance about determining whether costs are allowable costs under qualifying defence contracts.

- (2) In determining whether a particular cost is an allowable cost under a qualifying defence contract, the Secretary of State or an authorised person, and the primary contractor, must be satisfied that the cost is—
 - (a) appropriate,
 - (b) attributable to the contract, and
 - (c) reasonable in the circumstances.
- (3) In determining whether the requirements set out in subsection (2)(a) to (c) are met in relation to a particular cost, the Secretary of State or an authorised person, and the primary contractor, must have regard to guidance issued under subsection (1).
- (4) The Secretary of State or an authorised person may at any time require a primary contractor to show (whether by reference to guidance issued under subsection (1) or otherwise) that the requirements set out in subsection (2)(a) to (c) are met in relation to a particular cost claimed by the primary contractor as an allowable cost under a qualifying defence contract.
- (5) The SSRO may determine the extent to which a particular cost is an allowable cost under a qualifying defence contract where the Secretary of State, an authorised person or the primary contractor applies to the SSRO for such a determination.
- (6) The SSRO may determine that the price payable under the contract is to be adjusted by an amount specified by the SSRO in consequence of a determination under subsection (5), having regard to the extent to which the cost in question was treated as an allowable cost when the price payable under the contract was determined (or last determined) in accordance with section 15.

21 Final price adjustment

- (1) Single source contract regulations may provide for adjustments to be made to the total price payable by the Secretary of State under a qualifying defence contract.
- (2) The regulations must specify the procedure to be followed in determining the amount of any adjustment.
- (3) Provision made under subsection (2) must include provision for the amount of any adjustment to be determined—
 - (a) by agreement between the Secretary of State, or an authorised person, and the primary contractor, or
 - (b) by the SSRO, where the matter is referred to it by the Secretary of State, an authorised person or the primary contractor.
- (4) Provision under this section may be expressed so as to apply—
 - (a) to particular kinds of qualifying defence contracts;
 - (b) to qualifying defence contracts the value of which is of or above the amount specified for the purposes of this paragraph.
- (5) The Secretary of State may direct that provision under this section does not apply in relation to a qualifying defence contract the value of which is—
 - (a) of or above the amount specified for the purposes of subsection (4)(b), but
 - (b) less than the amount specified for the purposes of this paragraph in the regulations.

(6) The regulations may specify matters to which the Secretary of State must have regard in deciding whether to make a direction under subsection (5).

22 Recovery of unpaid amounts

- (1) This section applies where—
 - (a) the SSRO determines by virtue of section 18(3)(b), 20(6) or 21(3)(b) that the price payable under a qualifying defence contract is to be adjusted, and
 - (b) as a result of the adjustment—
 - (i) the Secretary of State is required to pay an amount to the primary contractor, or
 - (ii) the primary contractor is required to repay an amount to the Secretary of State.
- (2) If all or part of the amount mentioned in subsection (1)(b)(i) or (ii) is not paid or repaid before the payment date, the unpaid balance carries interest from that date at the rate for the time being specified in section 17 of the Judgments Act 1838.
- (3) The "payment date" is the date determined by the SSRO, in making the determination in question, as the date by which the amount must be paid or repaid.
- (4) The person to whom the amount is required to be paid or repaid ("the creditor") may recover from the other person as a debt due to the creditor the unpaid balance and any unpaid interest.