News story: Secretary of State announces new rates for determining profit in regulated defence contracts

Following the SSRO's recommendation in January 2019, the Secretary of State for Defence has announced the baseline profit rate and other rates to be used from 1 April 2019 to determine the profit element of qualifying defence contracts and qualifying sub-contracts.

The Defence Reform Act 2014 requires the MOD and contractors in qualifying defence contracts (QDCs) and qualifying sub-contracts (QSCs) to follow a six-step process to determine the profit rate to be applied in those contracts. Three of the six steps are determined with reference to rates set by the Secretary of State, informed by recommendations from the SSRO. The rates and associated steps are:

- the baseline profit rate (step 1);
- the SSRO funding adjustment (step 4); and
- the capital servicing rates used in the capital servicing adjustment (step 6).

The rates announced by the Secretary of State for use from 1 April 2019 are shown below:

Table 1: Recommended rates agreed by the Secretary of State for Defence

Element	2018 Rates	2019 Rates
Baseline Profit Rate (BPR) (% on contract cost)	6.81%	7.63%
Fixed Capital Servicing Rate (% on Fixed Capital employed)	4.38%	3.98%
Working Capital Servicing Rate (% on positive Working Capital employed)	1.21%	1.18%
Working Capital Servicing Rate (% on negative Working Capital employed)	0.53%	0.53%
SSRO Funding Adjustment	-0.024%	-0.042%

To provide transparency for stakeholders, the SSRO has published its recommendation for the 2019/20 baseline profit rate, capital servicing rates and SSRO funding adjustment together with details of the methodology applied and a range of supporting analysis which was provided to the Secretary of State to inform his determination.

The SSRO has also updated its guidance on determining contract profit rates and on Allowable Costs in QDCs and QSCs, to incorporate both the new rates announced by the Secretary of State and other changes for 2019/20 that were published in January 2019 following a public consultation.