

Single Source Contract Regulations 2014 Guidance

Chapter 6 Open Book and MOD Audit Rights

Purpose

1. The guidance in this chapter relates to a Qualifying Defence Contract (QDC) and applies equally to a Qualifying Sub-contract (QSC), except where it explains the different treatment of a QDC and QSC. To assess whether you are dealing with a prospective or actual QDC or QSC you must read [Chapter 2 Qualifying Defence Contracts](#).
2. The guidance does not apply to other single source contracts (Non-qualifying contracts). If you assess that your contract is a Non-qualifying contract then you must read the [Pricing of Single Source Non-qualifying contracts](#) Commercial Policy Statement.
3. If you are dealing with a prospective or actual QDC or QSC then you must read this Chapter 6 to understand the access rights the MOD has to a contractor's information during and at the end of a contract. In particular, this chapter explains:
 - a. the records a contractor can reasonably be expected to keep and the examination rights the MOD has to these records;
 - b. the duty of the contractor to report relevant events, circumstances and information that is likely to be relevant to your contract; and
 - c. the MOD's open book rights throughout the life of a contract including Post Award Review, Performance Review, and post costing.
4. This chapter has been created as definitive guidance for MOD Commercial Officers so 'you' indicates an action on the Commercial Officer.

What is the Legal Framework?

5. The primary legislation applicable to QDCs is the [Defence Reform Act 2014 \(DRA\)](#). Sections 23 and 26 refer to records and the duty to report relevant events, circumstances and information.
6. The secondary legislation applicable to QDCs is the [Single Source Contract Regulations 2014 \(SSCR\)](#). Part 4 of the SSCR sets out the duty to keep relevant records and audit rights.

Confidentiality – Criminal Offence of Unauthorised Disclosure

7. The DRA requires contractors with QDCs to keep relevant records which the MOD may access. Contractors must also provide a range of standardised reports to the MOD and the Single Source Regulations Office (SSRO). Much of the

information received will be commercially sensitive and you must handle it accordingly.

8. The Single Source Advisory Team (SSAT) within the MOD will receive the information and reports required from the contractor under the DRA. The SSAT is responsible for protectively marking the information on receipt, before distribution to the Commercial Officer identified in the DEFFORM 111. If you receive information or reports from the SSAT that is not marked with a security classification or handling instruction, you must inform the SSAT immediately.

9. Schedule 5 of the DRA details a list of 'permitted disclosures' in relation to this information, and information derived from it. Any disclosure of Schedule 5 protected information which is not a permitted disclosure is a criminal offence. Any individual convicted of committing an offence of unauthorised disclosure is **personally liable** to a fine, to imprisonment, or both. You can find detailed guidance of your confidentiality obligations in relation to Schedule 5 protected information at [Chapter 9 Confidentiality](#).

Record Keeping

10. The DRA and SSCR place a statutory obligation on contractors¹ as detailed in paragraph 11, to keep relevant records. This is achieved through mechanisms that include providing pricing information (see [Chapter 3 Pricing a Qualifying Defence Contract: The Cost Element](#) and [Chapter 4 Pricing a Qualifying Defence Contract: The Profit Element](#)) and Contract Reports (see [Chapter 5 Contract Reporting](#)). Contractors are required to keep these relevant records and allow the MOD to examine those records for the purposes set out in the DRA, as detailed in paragraph 11.b.

11. The DRA defines relevant 'accounting' and 'other' records (in hard or electronic format) as those that:

- a. the contractor may reasonably be expected to keep; and
- b. are sufficiently up-to-date and accurate for use by the MOD for the purposes of:
 - (1) auditing reports provided by the contractor;
 - (2) verifying whether a cost is an Allowable Cost²;
 - (3) verifying the reason for any difference between an estimated and actual Allowable Cost;
 - (4) verifying any other matter relating to the price payable under a QSC;

¹ In relation to a QDC including any report provided under SSCR Part 5 the prime contractor has an obligation to keep relevant records. In relation to reports on overheads and forward planning, etc. (supplier reports) under SSCR Part 6 the 'designated person' (see Chapter 8) has an obligation to keep relevant records. In both cases, the obligation is subject to the time limits set out in paragraph 12 (start date) and paragraphs 14 – 15 (end date).

² The DRA indicates that the purposes in paragraphs 11.b.(2)–(6) only apply to QDCs.

- (5) monitoring the contractor's performance of the obligations under the QSC; and
 - (6) determining whether a contract between a contractor and another party is a Qualifying Sub-contract (QSC).
12. The obligation for the contractor to keep relevant records starts from:
- a. where a QDC has been awarded following publication of an advert in the Official Journal of the European Union (OJEU), Defence Contracts Online, Contracts Finder or elsewhere, from the date of the publication of that advert;
 - b. for all other QDCs, whichever is the earliest of:
 - (1) the date the prime contractor received written notice from the MOD that negotiations had started;
 - (2) the date the MOD published a Voluntary Transparency Notice (VTN) in relation to the proposed contract;
 - (3) the date the prime contractor was invited to provide an offer;
 - (4) the date the MOD made an offer to the prime contractor; or
 - (5) the date the QDC was entered into.
 - c. where a contract assumes QDC status by agreement between both parties, as a result of an amendment to a former non-QDC, from the earliest of:
 - (1) the date the prime contractor received written notice from the MOD that amendment negotiations had started;
 - (2) the date the prime contractor was invited to provide an offer to amend the contract;
 - (3) the date the MOD made an offer to the prime contractor to amend the contract; or
 - (4) the date of the amendment.
 - d. where a report is provided under SSCR Part 6 (reports on overheads and forward planning, etc.) the first day of the contractor's accounting period relating to the financial year for which that report is provided.
13. It is therefore essential under 12.b.(1) and 12.c.(1) that you make it clear to the contractor, in writing, when contract / contract amendment negotiations have started. A template letter is attached at Annex A. It is essential that you state that the negotiations are 'without commitment'.
14. The requirement for the contractor to keep relevant records for a contract ceases on the earlier of:
- a. two years after the contract completion date³, or for relevant records

³ Contract completion is defined in the SSCR as the date described in the contract as being the contract completion date. Where no such date exists, the date on which the contractor completes all obligations which

relating to reports on overheads and forward planning, etc. (supplier reports); or

b. six years after the end of the contractor's accounting period in which the duty to keep relevant records first arose (e.g. a contractor with a financial year end of 31 March 2017 who created a relevant record on 1 November 2016 would be required to keep it until 31 March 2023), or for relevant records relating to reports on overheads and forward planning, etc. six years after the designated person's accounting period in which the duty first arose.

15. The requirement to keep relevant records relating to reports on overheads and forward planning, etc. (supplier reports) ceases on the earlier of:

a. two years after the end of the contractor's accounting period relating to the last relevant financial year in relation to which the on-going contract condition is met; or

b. six years after the end of the contractor's accounting period in which the duty to keep relevant records first arose.

16. The effect of the limit at paragraphs 14.b and 15.b is that a contractor is not legally bound under the DRA to keep relevant records for the duration of the contract. The maximum duration that can apply is seven years (assuming creation of a relevant record on the first day of the contractor's financial year). You must therefore consider carefully the need to examine records well ahead of the end of the statutory period. The time limits in paragraphs 14 and 15 only apply to records required under the DRA and SSCR. Where you require other records to be kept in support of your contract, you must specify the retention periods in the contract conditions.

17. The exception to the time limitation on keeping relevant records is if either party has made a referral to the SSRO. In this scenario the contractor must retain any records relevant to the matter being referred until the SSRO makes its ruling.

18. You can find information about the SSRO, including a summary of all of the matters which may be referred, in [Chapter 11 The Single Source Regulations Office](#).

Examination of Contractor's Records – Open Book

19. Although not referred to as 'open book' within the DRA or the SSCR, the legislation gives the MOD rights to examine the relevant records kept by a contractor in its obligations detailed in paragraph 11 (subject to the retention periods detailed in paragraph 14). The rights extend into supplier level information that supports the Supplier Reporting obligations under the DRA and SSCR (subject to the retention periods detailed in paragraph 15). You can find further information about supplier reporting in [Chapter 8 Supplier Reporting](#). Supplier level information is more likely to be used by the Cost Assurance and

entitle it to final payment under the contract, excluding any final price adjustment. If the contract is terminated before either of these events, the date the contract is terminated.

Analysis Service (CAAS) team, in rates investigations and when undertaking Performance Reviews (see paragraph 37).

20. The MOD's right to examine relevant records applies equally to QSCs. However, under the SSCR, this right is limited to sub-contracts equal to or greater than £25M. You should include DEFCON 802 (QDC: Open Book on Sub-contracts that are not qualifying Sub-contracts (QSC)) in your contract to secure equivalent open book rights for sub-contracts equal to or greater than £1M. This DEFCON also requires those rights to be flowed down the supply chain where reasonably practicable.

21. You must give the contractor written notice of your intention to examine its relevant records⁴ and you may request the records are made available in either hard or soft format. The contractor has at least 20 working days from the date on which it receives the notice to comply. You may also request the contractor to provide further information / explanation relating to those records. You may only examine the records on a working day between 09:00 and 17:00.

Appropriate Use of the MOD's Rights to Examine a Contractor's Records

22. Although the MOD can examine a contractor's relevant records any time, for the purposes listed in paragraph 11.b, the MOD is most likely to do so:

- a. after contract award, where there are concerns regarding the pricing assumptions detailed in the Contract Pricing Statement (CPS). (see [Chapter 3 Pricing a Qualifying Defence Contract: The Cost Element](#), for more detail about the CPS);
- b. following receipt of a Contract Report (Interim (ICR) and Quarterly (QCR) detailed in [Chapter 5 Contract Reporting](#)), where there is a significant variance between expected and actual costs, or unexplained changes in any forecasts;
- c. if key pieces of information relating to the delivery of the contract are not being provided;
- d. if there is an increase in poor performance in delivery of the contract, efficiency reduction or cost growth;
- e. to review sourcing decisions which relate to the QDC such as 'make or buy', appointment of sub-contractors and the appropriate use of competition;
- f. if there are repeated fluctuations in the quality of information provided in contract reports;
- g. to obtain information relevant to pricing, in preparation for follow-on contracts or amendments; and

⁴ This also applies to relevant Supplier Records and QSCs.

h. at the end of a contract, to conduct post costing where there is significant variance in actual costs, compared to estimates at the time of pricing the contract, which you believe have not been adequately explained.

23. Having examined the contractor's relevant records, you are able to request further information or an explanation relating to those relevant records from the contractor. This should be a formal request in writing with any failure by the contractor to comply dealt with under the compliance and remedies regime in paragraph 40.

Post Award Review

24. Open book principles may be used to ensure the contract was priced as described in [Chapter 3 Pricing a Qualifying Defence Contract: The Cost Element](#) and [Chapter 4 Pricing a Qualifying Defence Contract: Profit Element](#). It is MOD policy that the contractor must supply a Contract Pricing Statement (CPS) at the time of contract placement, or in exceptional circumstances (and in accordance with the SSCR), within one month of the initial reporting date⁵. In addition to the pricing information, the CPS will contain details of the cost model, risks relevant to pricing and master assumptions.

25. If there are key documents supporting the CPS that the Contractor has not provided you should request these as relevant records.

26. You can use the MOD's rights to examine a contractor's relevant records in order to investigate whether or not the contractor has followed the pricing principles (that costs are allowable only if they are attributable, appropriate and reasonable), at the time of pricing the contract. The CPS and associated documentation will form a key part of this review, and you may wish to engage CAAS to support the review. Where you require assistance from CAAS, you must complete a [DEFFORM 122](#).

27. In the past the MOD had similar rights to verify single source contract records after pricing, through DEFCON 648 or 648A (Availability of Information) (both to be archived from December 2014). However, these rights were restricted in scope and often difficult to exercise: firstly the MOD had to negotiate the appropriate DEFCONs into contracts (not always achieved); and secondly, the review of records (called post-costing) was invariably done at or near the end of the contract. This often made it a very difficult review to undertake, particularly on longer contracts.

28. Under the new framework provided by the DRA and SSCR, the MOD will introduce a new audit approach, the Post Award Review (PAR). A PAR will not be restricted to a 'once only' limit and can be undertaken at any time up to two years after contract completion (although if it does take place after contract completion it is, in effect, post-costing - see paragraph 31). The PAR is primarily intended to be conducted early in the life of the contract, to test the pricing assumptions used in pricing the contract. However, as the contract progresses, different matters may come to your attention, any of which may lead to a

⁵ The initial reporting date is defined as the date the contract was entered into for new QDC (or QSC), or date of a contract amendment.

concern that pricing principles were not followed, and you may wish to conduct a PAR.

29. A PAR is likely to be more difficult to conduct if left until late in the contract life and any investigation / audit must take account of the time limitations on a contractor's obligation to keep relevant records, at paragraphs 14 and 15. Therefore, wherever there is any cause for concern about the contract pricing, you should complete a PAR as soon as possible.

30. Where a PAR identifies that, in your or CAAS' opinion, pricing assumptions regarding Allowable Costs were not fit for purpose, you may make a referral to the SSRO for a binding determination on the matter, as described in paragraph 39.

Post Costing

31. The contract reporting regime introduced by the DRA and SSCR should highlight variances between the estimated and actual costs as the contract progresses. For firm / fixed price contracts, the MOD will be made aware of such variances much earlier than in the past. In addition the contractor must provide a Contract Completion Report (CCR) within six months after the contract completion date; and a Contract Costs Statement (CCS) within 12 months of the contract completion date. These end of contract reports include details of the actual costs incurred in delivery of the contract against the estimate of costs when the contract price was agreed.

32. The reason for requiring both a CCR and a CCS at contract completion is timing. The contractor provides the CCR sooner after contract completion in the same format as the statutory reporting through the contract life. It is therefore directly comparable with previous reports. As it is provided early after contract completion it will be permissible to include a certain amount of costs that are not based on actual costs but are still based on estimates. The CCS is required in slower time, in a better format for CAAS to audit, and on the basis that it will not be permissible to include estimated costs above 2% of the total cost without explanation.

33. If the CCR and / or CCS show a significant variance between the cost used in pricing and the actual costs incurred by the contractor, and the contractor has not adequately explained that variance, you should conduct a post costing exercise to determine the cause of the variance. The contractor should have already explained any significant variances which appeared through the contract reporting regime before contract end and any concerns been addressed by the MOD at the time of being reported. Post costing should therefore be by exception, only required if there has been a sudden and unexpected variation at the end of the contract, as reported in the CCR and / or CCS.

34. As with the PAR, post costing allows the MOD to review and challenge the baseline assumptions made when the contract was priced to ensure the costs included in the CCR meet the pricing principles of being Allowable Costs. Where you disagree with the contractor about the Allowable Costs included in the contract price, the MOD has the right to make a referral to the SSRO for a determination, as explained in paragraph 39.

35. Another possible outcome of a post costing exercise is a final price adjustment in accordance with Protection against Excess Profits and Losses (PEPL) for a firm / fixed / volume driven priced contract or a component of a contract. The final share line adjustment for a Target Cost Incentive Fee (TCIF) contract will be dealt with in the contract terms and conditions. You can find more information about final price adjustments in [Chapter 7 End of Contract Activities and Reports](#).

Inappropriate Use

36. You must ensure you use the MOD's rights to examine relevant records proportionately. The contractor has the right to refer the matter to the SSRO if it considers that you have acted unreasonably in relation to your rights. Situations which may give the contractor the right to feel aggrieved are:

- a. continuous applications for similar information;
- b. investigation of immaterial costs or issues;
- c. requests for information not relevant to the delivery of the contract (performance / costs / time) i.e. personal information or for simple curiosity;
- d. use of the rights for purposes other than those detailed in the SSCR (outlined in paragraph 11.b);
- e. attempts to access information which is no longer required to be kept as the time periods detailed in paragraph 14 have lapsed; or
- f. repeated or unnecessary requests for an explanation, where one has already been provided.

Performance Reviews

37. You can use open book principles to investigate the performance and efficiency of a contractor in relation to the overall delivery of QDCs and the overhead rates. CAAS will undertake Performance Reviews on the MOD's major suppliers in order to stimulate performance efficiencies, drive benchmarking activities, and feed into the MOD's Key Supplier Management regime. There is no action on commercial teams in relation to Performance Reviews. However the output of the reviews may result in revisions to the MOD agreed recovery rates as described in [Chapter 3 Pricing a Qualifying Defence Contract: The Cost Element](#).

Duty to Report Relevant Events

38. A contractor must notify the MOD of relevant events. These are the occurrence (or likely occurrence) of an event, circumstances or information which is likely to have a material effect on a QDC. Events, circumstances, or information likely to have a material effect include (but are not limited to):

- a. increases in the costs of the prime contractor arising under the contract;
- b. increases in the total price payable under the contract; and

- c. the primary contractor's ability to perform a material obligation arising from the contract.

39. This is an important new statutory obligation on contractors because non-compliance may lead to the MOD making a claim against them, if you assess that the MOD has suffered loss as a result of a failure to notify (see paragraph 42). Notification by a contractor of a relevant event will allow the MOD to take appropriate action as part of the normal contract management process. You must ensure that you specify in your contract who within the project team the contractor should notify of such relevant events.

SSRO Determination for Allowable Costs

40. Where you require a determination from the SSRO about Allowable Costs, you must give at least 20 working days written notice to the contractor asking the contractor to provide evidence of how they met the pricing principles of costs being appropriate, attributable and reasonable. Where at least 20 working days has elapsed and you have not received a response or you have received a response which you consider to be unsatisfactory, you may request a determination. You can find more information about how the referrals process to the SSRO operates in [Chapter 12 The Single Source Advisory Team](#).

Compliance and Remedies

41. The DRA and SSCR provide both parties with a range of remedies to ensure compliance with the legislation. Contractor obligations outlined in this chapter include:

- a. keeping relevant records for the period described in paragraphs 14 and 15;
- b. permitting the MOD to examine relevant records, where the MOD has given notice;
- c. providing copies of relevant records which have been requested; and
- d. providing further information or explanation when requested to do so.

42. If the contractor fails to meet any of these obligations then it is considered to have committed an actionable contravention.

43. Where you believe the contractor has committed an actionable contravention, you should contact the SSAT. The SSAT will decide on a course of action which may include issuing a compliance notice and / or a penalty notice. You can find more information about the compliance regime in [Chapter 10 Compliance and Remedies](#).

44. A contravention of the duty to report relevant events, as described in paragraph 38 follows a different process. Unlike the other contraventions which are enforceable through the use of civil penalties set out in the SSCR, you must calculate the penalty amount for contravening the obligation to notify as if it were a breach of contract. In making your assessment you must consider what damages or loss the MOD has actually suffered. You can find guidance on how to do this in the Claims Against Contractors section of the [Claims topic](#).

45. There may be genuine circumstances where the contractor is unable to comply with its obligations to provide access to its records or duty to report relevant events, for instance where the contractor would contravene:

- a. a prohibition or restriction imposed by an enactment; or
- b. an obligation of confidentiality owed by the contractor, unless:
 - (1) the other party is associated with the contractor, or
 - (2) gives consent to the contractor to comply with the requirement in question.

46. Where the contractor is unable to comply because to do so would contravene a relevant restriction, the contractor must notify the MOD in writing stating the obligation(s) and explain the reasons for being unable to comply with the obligation.

47. If you reasonably suspect that the contractor has entered into an obligation of confidence for reasons other than genuine commercial reasons, then the SSCR allows you to refer the matter to the SSRO, and you must contact the SSAT for advice. The SSAT may refer the matter to the SSRO for a determination. The SSCR state the referral to the SSRO must be made within 40 working days of receipt of the notification, so where you think this course of action is appropriate, you must act promptly.

Contacts, Training and Further Information

48. The [Web Access Page](#) for the DRA and SSCR contains a summary of the legislation, details of who you can speak to for advice, and what training is available. It also contains links to other chapters in the SSCR guidance and other relevant topics and information.

What are the key points to remember?

1. The term open book is not used in the DRA but is used in this chapter to describe a range of duties and rights for the contractor and the authority.
2. Contractors have a legal duty to keep relevant records and allow the MOD access to those records, for the purposes set out in the DRA / SSCR.
3. There are time limits on the obligation of a contractor to keep relevant records which may be shorter than the duration of the contract. You need to consider carefully the implications of this when exercising your rights to examine records.
4. A contractor must notify the MOD of an occurrence, event, circumstances or information that is likely to be materially relevant to the contract.
5. The Post Award Review enabled by the DRA / SSCR gives the MOD the ability to audit and review contract pricing assumptions much earlier than has been the case, and to take action where matters of concern are revealed.
6. You should not use the new open book rights in inappropriate ways.
7. You must be aware of the serious consequences of unauthorised disclosure of information protected under Schedule 5 of the DRA. There are penalties which apply to you personally, which may include a fine or imprisonment.

Annex A

Notice of Duty to Keep Relevant Records

[Supplier's address]

Notification of the Start of Negotiations

Dear [name]

1. I am writing to you in respect of a prospective [contract / contract amendment] under the terms of the Single Source Contract Regulations 2014 (SSCR), for the supply of [insert requirement].

2. This letter represents formal notification that contract negotiations have commenced and you are obligated to keep records from the date of receipt of this notice in accordance with:

- a. SSCR Regulation 20(5)(a) Qualifying Defence Contract; and / or
- b. SSCR Regulation 20(2)(a) amendment to contract.

3. You should be aware that this notice is without commitment and does not guarantee an offer of contract.

Yours sincerely,

[MOD Commercial Officer]

[Post Title]