Department of Energy
Washington, DC 20585

July 26, 2002

The Honorable John T. Conway
Chairman
Defense Nuclear Facilities Safety Board
625 Indiana Avenue, NW
Washington, D.C. 20004-2901

Dear Mr. Chairman:

The purpose of this letter is to provide follow-up to a concern raised by the Board concerning performance incentives at the Savannah River Site (SRS). Since my earlier correspondence, there are additional actions I have initiated to address continuing concerns with the incentive structure.

Aligning contracts and contract incentive structure to drive performance is essential to be able to carryout reforms identified in the Top-to-Bottom Review. In the short term, I am reviewing and approving all contract incentive plans starting in FY03. A copy of a letter articulating my expectations is attached (Attachment 1). Longer term, I have established a project management team led by Charles Dan of Rocky Flats and Dr. Ines Triay, Manager of the Carlsbad Field Office, to review the Environmental Management acquisition process to develop a process that will allow EM to get more performance out of its performance-based contracts. A critical decision (CD) 0 is planned for mid-September 2002. Additionally, I have formed a contract review board to ensure that a corporate process is established that aligns contracts, challenges contractors, and holds individuals accountable for performance. A copy of this charter is attached (Attachment 2).

Earlier this month, I dispatched a team to Savannah River to evaluate project controls and the contract management process used at the Site. A copy of the trip report is included as Attachment 3. I have directed Savannah River to develop a corrective action plan within 60 days and have assigned the Chief Operating Officer in Environmental Management to assist Savannah River in putting together this plan as well as structure the FY03 performance incentives. I will provide a copy of both the corrective action plan and the FY03 incentive plan after they are developed.
Changing the direction of this program and improving our performance will not be easy or quick. I remain committed to fundamentally and institutionally changing this program.

Sincerely,

Jessie Hill Roberson
Assistant Secretary for
Environmental Management
MEMORANDUM FOR DISTRIBUTION

FROM:  JESSIE HILL ROBERSON
ASSISTANT SECRETARY FOR
ENVIRONMENTAL MANAGEMENT

SUBJECT: Fiscal Year (FY) 2003 Contract Performance Objectives and Incentives for Environmental Management

This memorandum conveys my expectations for future collaboration between the Office of Environmental Management (EM) and field offices in establishing performance incentives under our major site and facility contracts. We need to ensure that our contract performance objectives and incentives (including multi-year incentives) are properly aligned and linked to the EM and site-specific strategic plans. In addition, we need to aggressively and consistently challenge contractors to accelerate our clean-up and remediation objectives and provide for enhanced safety and risk reduction.

Accordingly, I expect each of you, to personally engage in both the development and negotiation of contract performance objectives and incentives and the assessment of the contractor’s performance against those objectives, consistent with Department of Energy policies on performance-based management contracting. To this end, contract performance objectives, measures and incentives for all EM major site and facility contracts will be:

- aligned with EM’s Performance Management Plans and reflect those expectations and outcomes that are truly critical to the successful accomplishment of the strategic and tactical goals of the site mission;

- contractually effective prior to the commencement of performance period,

- based on objective and measurable performance expectations and attributes to the maximum extent possible. In this regard, subjective performance expectations are to be used on an exceptional, or limited, basis. These types of subjective expectations may be desirable in ensuring that less critical performance areas receive contractor management attention. In cases where existing subjective performance expectations are in place, however, each field office will review the continued need for them, and where appropriate, work to convert these subjective expectations to objective ones; and,
structured to achieve requisite levels of quality, timeliness, and cost control and motivate the contractor to achieve or exceed expected performance.

In addition, each field office shall implement a change control process for managing the contract baseline and effect needed changes to performance objectives in a timely manner. This process must include the involvement of senior field office management and my office.

With respect to those major site and facility contracts that employ annually negotiated performance objectives and incentives (i.e., current management and operating contracts and certain “management and integration” contracts), I will review and concur in all annual performance objectives and incentives prior to commencement of negotiations with the contractor. This requirement applies regardless of whether the contract contains multi-year, “stretch,” “superstretch,” and other performance objectives and incentives that are not established on an annual or FY basis. In order to ensure that FY 2003 performance objectives and incentives reflect EM priorities and incorporated into the contract in a timely manner, I have established the following process and schedule:

- Not later than July 15, 2002, each field office shall prepare a strategy document for structuring its FY 2003 performance objectives and incentives. This document will serve as the basis for the field office’s negotiation position. I intend to review and approve this document. The strategy document shall include: the identification of key projects, performance outcomes, and expected end states that will be subject to incentivization; the proposed allocation of fee against to expectations; the identification of any subjective evaluation areas and the rationale explaining the need for the subjective evaluation areas; a discussion of the linkages and alignments of the performance objectives to ensure that critical EM and site mission objectives are achieved; and the relationship of the annual performance objectives to other objectives and incentives in the contract (i.e., multi-year, “stretch”, and “superstretch.”.

- Subsequent to the field office receiving approval of its strategy (but not later than August 1, 2002), each field site shall develop the specific performance objectives and incentives for negotiation (a “pre-negotiation plan” or similar document) for my review and approval.

- Not later than September 1, 2002, EM and the field office manager shall agree to the final set of performance objectives and incentives for the specific contract.

- Not later than September 30, 2003, the field office shall successfully conclude negotiations with the contractor for the FY 2003 performance objectives and incentives and effect the FY 2003 performance objectives and incentives into the contract.
Regarding major site and facility contracts that do not rely on annually established performance objectives, measures and incentives (e.g., cost plus incentive fee contracts for site closure), I will review and approve these contract incentives prior to award of the contract and at such time as the performance objectives, measures and incentives change during contract performance as a result of the change control process. Nevertheless, I expect each field office manager to review the existing performance objectives and incentives for these contracts under his or her cognizance to ensure that the performance objectives, measures, and incentives are properly aligned and linked to the EM and site mission.

In the near future, I will reduce the substantive instructions contained in this memorandum to a procedures document to formally effect its operation. Should you have questions or wish to discuss any aspect of this direction, please contact me or Paul Golan. Paul can be reached at 202-586-7709.
DISTRIBUTION:
Manager, Albuquerque Operations Office
Manager, Idaho Operations Office
Manager, Richland Operations Office
Manager, Office of River Protection Operations Office
Manager, Carlsbad Field Office
Manager, Savannah River Operations Office
Manager, Oak Ridge Operations Office

cc:
Gerald Boyd, Assistant Manager for Environmental Management, Oak Ridge
Roger Liddle, Assistant Manager for Environmental Management, Oakland
Carl P. Gertz, Assistant Manager for Environmental Management, Nevada
Jack P. Tillman, Assistant Manager for Environmental Management, Albuquerque
Anibal Taboas, Assistant Manager for Environmental Management, Chicago
Jerry Lyle, Assistant Manager for Environmental Management, Idaho
Barbara Male, Director, Office of Management and Information
Roger Butler, Deputy Assistant Secretary for Office of Policy, Planning and Budget
Patrice Bubar, Acting Deputy Assistant Secretary for Office of Integration and Disposition
Mark Frei, Deputy Assistant Secretary for Office of Site Closure
Mark Frei, Acting Deputy Assistant Secretary for Project Completion
James M. Owendoff, Deputy Assistant Secretary for Office of Science and Technology
PURPOSE

The purpose of this review was to assess the Savannah River Site (SRS) Performance Management Plan (PMP), focusing in the following areas:

- Project controls used to plan, estimate cost, manage, and prioritize work
- Contract incentives and contract management approaches used to drive performance

CONCLUSIONS

Little has changed from the project strategy and execution plan developed and presented in August 2001. SRS needs to resolve a number of issues (discussed below) to be able to execute a plan consistent with the EM vision and projected funding. Without significant changes, SRS has a limited probability of success in achieving the vision outlined in the PMP, and additional investment may have the potential for only marginal return.

SUMMARY OF FINDINGS

1. The Risk Prioritization process used by SRS is inadequate and an ineffective tool for planning, prioritizing, and scheduling work.

2. SRS needs to develop a cost critical path and better methodologies for managing its cost structure. SRS’s projected requirements from the Cleanup Reform Account (CRA) are excessive, peaking at $630 million in FY05.

3. Contract incentives and contract management are not clearly aligned with the mission. Incentives are not aligned with accelerated risk reduction and closure, and the contract management system in place encourages “fiefdoms” and a fragmented contract management platform.

RECOMMENDATIONS

- Transmit this report to the Manager, Savannah River Operations Office (SRO).
- Direct development of a corrective action plan.
- Conduct a follow-up review within 60 days of transmittal of this report, along with quarterly continuing project reviews.
FINDINGS

1. **SRS needs to retool or change its approach to planning, prioritizing, and scheduling work.** The Risk Prioritization process used by SRS is inadequate and ineffective. The following are examples of its shortcomings:

- The Risk Prioritization process is a complicated and subjective tool that does not properly prioritize the highest-risk or highest-cost activities. As an example, F-Area nuclear material stabilization and environmental restoration (ER) program management were given the same safeguards and security score (48), and high-level waste (HLW) vitrification activities were given a score of zero. The team noted that all ER program elements had a safeguards and security (S&S) rating of 48. SRS personnel explained that this scoring was based on the rationale that the risk of the theft of a construction crane at an ER project (probability x consequence) was similar to that of the theft of special nuclear material (SNM) at F-Area. SRS personnel stated that vitrification received a score of zero in S&S based on the rationale that there was no difference in the equipment that could be stolen during the next 5 years (the projected lasted more than 5 years).

- All ER projects were given the maximum score of 200 points in the area of “environmental insult” on the basis that there was already contamination in the environment. No weighting factor was used based on either the size or hazard of the source term. Using this approach, a small spill was given the same score as the Fourmile Branch project (a very large spill).

- This prioritization approach does not recognize the hundreds of millions of dollars in annual carrying costs of nuclear facilities or the inherent risk of unstabilized materials and aging facilities. As a result, ER work is given priority over nuclear material stabilization and nuclear facility decontamination and decommissioning (D&D) from both a risk and a business (cost) perspective. The net result is that ER work is funded ahead of both SNM stabilization and nuclear facility D&D when marginal dollars are added to the project.

- Using this approach, SRS budgeted $0 in FY02 for D&D because a risk or business benefit could not be quantified, although there are more than 4,500 structures at the site. SRS will need to demolish more than 200 facilities/year (or 1 every business day) through 2025 to meet its PMP vision, yet there is no meaningful planning or progress expected in this area during the next 5 years. This approach gives F-Area D&D planning a risk score of zero and a business score of 238, for a total score of 238. This is in contrast to the score received by the U.S. Forest Service (3,400) for work performed in support of the phyto-remediation project and other general program support. It should be noted that the $20 million purportedly funded to perform D&D in FY02 is actually
maintenance and operating (M&O) costs of facilities that have been allocated to this program.

- The highest potential maximum score for any activity is about 10,000. The approach weights business elements more heavily (by a factor of 3) than risk elements. The net result has been the development of a priority list for funding that is skewed away from high risk-reduction and high mortgage-reduction activities. This point is significant as SRS uses this approach as the basis for planning and prioritizing all work at the site.

2. **SRS needs to develop a cost critical path and better methodologies to manage its cost structure more aggressively.** SRS’s projected requirements from the CRA are excessive, peaking at $630 million in FY05 (the FY03 CRA allocation was about one-third of this value).

- From 1998 to 2002, the number of white-collar workers has grown, while the number of blue-collar workers has decreased. SRS has a suffocating cost structure that the contractor has done little to improve, and the team views this as the single largest factor driving the huge out-year costs forecast for this project. Additionally, the federal staff expressed their view that Westinghouse Savannah River Company (WSRC) has done little to address a growing skills-mix issue. The table below is based on information provided by SRO during the team’s visit.

**WSRC STAFFING**

<table>
<thead>
<tr>
<th></th>
<th>1998</th>
<th>2002</th>
<th>Net</th>
</tr>
</thead>
<tbody>
<tr>
<td>White collar</td>
<td>7,024 (57%)</td>
<td>7,135 (60%)</td>
<td>+111</td>
</tr>
<tr>
<td>Blue collar</td>
<td>5,238</td>
<td>4,725</td>
<td>-513</td>
</tr>
<tr>
<td>Total</td>
<td>12,262</td>
<td>11,860</td>
<td>-402</td>
</tr>
</tbody>
</table>

- SRS proposes funding D&D at a rate of $5–10 million year from the CRA, yet plans to fund *accelerated* transuranic (TRU) waste shipments to the Waste Isolation Pilot Plant (WIPP) at a rate of $34 million/year. SRS proposes accelerated shipments to WIPP at a rate of 2,000 drums/year or 1 shipment/week for 6 years. SRS was unable to explain the cost basis for this project. The team questions the very large $184 million proposed investment in the TRU project for a very slow rate of disposal of 12,000 drums to WIPP. The team pointed to the shipping rates of Rocky Flats (21/week) and Idaho (14/week) as benchmarks from both a process and a cost perspective.
- SRS needs to explain the cost basis and structure for the ER work in FY03–08, as it was unclear to the team what the three categories of work (shown below) represented or what the basis for the cost estimates was:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total FY03 proposed</td>
<td>$120 million</td>
</tr>
<tr>
<td>Assessments</td>
<td>$25 million</td>
</tr>
<tr>
<td>Remedial actions</td>
<td>$53 million</td>
</tr>
<tr>
<td>Continuing groundwater operations</td>
<td>$42 million</td>
</tr>
</tbody>
</table>

- SRS shows similar spending breakdowns in the FY04–08 timeframe, as well as a life-cycle cost of $2.10 billion for the ER program. The team did not understand the cost basis for this estimate. The spend rates for FY04–08 are as follows:

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
</tr>
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<tbody>
<tr>
<td>FY04</td>
<td>$130 million</td>
</tr>
<tr>
<td>FY05</td>
<td>$115 million</td>
</tr>
<tr>
<td>FY06</td>
<td>$110 million</td>
</tr>
<tr>
<td>FY07</td>
<td>$130 million</td>
</tr>
<tr>
<td>FY08</td>
<td>$140 million</td>
</tr>
</tbody>
</table>

- SRS has no motivation or interest in reducing the footprint and the supporting landlord/utility cost structure. This opinion is supported by both the Integrated Priority List and discussions held by the team with SRS personnel during the visit.

- SRS's approach to cost estimation, which involves allocating the overall cost estimates to individual work packages to establish a baseline for measuring performance, was not well described. The cost baseline, a time-phased budget that will be used to measure and monitor cost performance on the project, was not reviewed.

- SRS expressed no interest in developing a credible ER program at a level below $100 million/year or more. When the team asked what the ER program would look like at the level of the FY02 President's budget, no response was given. SRS's intent was to fully fund this program. However, it is unclear how full funding and prioritization of risk come together.

- While the HLW plan is aggressive and makes technical sense, the proposed cost from the CRA is $1.5 billion for FY03–08, capping out at $304 million in FY05. The cost estimate and planning need further refinement.

- SRS should develop a cost build-up funding profile that clearly explains how funding decisions and work prioritization are carried out.

3. **Contract incentives and contract management are not clearly aligned with the mission.** Incentives are not aligned with accelerated risk reduction and closure, and
there is a contract management system in place that encourages “fiefdoms” and a fragmented contract management platform.

- WSRC has a significantly greater focus on cost saving than on performance of work. In the ER area, “the contractor earns $1 million in fee for meeting all compliance milestones and another $5 million for performing $120 million in scope for $100 million.” WSRC admitted that there are no acceleration incentives in executives’ or employees’ performance plans, but they are incentivized to return money to the WRSC corporate management reserve. This situation drives behavior inconsistent with accelerated risk reduction and closure. Rather, it drives behavior of avoiding high-risk projects, and funding projects that involve little risk or risk reduction and provide predictable earnings to the parent company.

- WSRC has earned more than 90 percent of the available fee during the past 3 years. WSRC appears very comfortable with the contract and fee arrangement, and does not appear to be adequately challenged to drive down risks and reduce mortgage costs. WSRC is executing the work in the performance-based incentives (PBIs), but the PBIs are not aligned with accelerating reductions in risk and mortgage. The team recommends that this area be examined thoroughly.

- Contract management needs to improve. SRO still has 20+ contracting officer’s representatives providing technical direction to the contractor. Additionally, division directors have the authority to provide nontechnical direction to the contractor. WSRC stated that it was very comfortable with this arrangement. No one at SRS finds this arrangement problematic; rather, they believe it aids the free flow of work. This type of arrangement encourages a proliferation of program fiefdoms at the site.

- This contract established 20 percent of the available fee under comprehensive performance/subjective fee. WSRC is currently being paid about 95 percent in this area. Over the life of the contract, WSRC would be paid in excess of $70 million without an established standard or set of criteria against which to measure performance. SRS uses this as an “everyone can have a piece of the pie” incentive. This particular incentive needs to be reviewed.

- In a DOE-only meeting after the PMP presentation, some of the assistant managers showed a genuine interest in improving the incentive process.
TEAM COMPOSITION

- Paul Golan, DOE Headquarters
- Charles Dan, DOE Rocky Flats
- Bob Sleeman, DOE Oak Ridge
- Matt McCormick, DOE Hanford
- Barry Naft, Consultant
- Spencer Williams, Consultant
ENVIRONMENTAL MANAGEMENT

CONTRACT MANAGEMENT ADVISORY COUNCIL CHARTER

I. Purpose/Scope

a The Contract Management Advisory Council (CMAC) has been established to advise the Assistant Secretary for Environmental Management (EM) on contracting issues and to serve as an interactive channel to address contracting services in support of the EM program. The council will address: (1) contracting strategies for HQ and field management contracts; (2) recommendations on extend/compete decisions for field management and EM HQ contracts; (3) review of performance-based incentives; (4) review of contractor fee earnings and (5) special studies as directed by the Assistant Secretary or determined to be necessary by the CMAC.

b The scope of this Charter applies to all contracts awarded and administered by EM at Headquarters and at those sites where EM is the designated Lead Program Secretarial Organization and other sites where the primary purpose of the contract work scope is to support the EM mission.

II. Authority

The Council is established by the Assistant Secretary for Environmental Management (EM-1) to make recommendations and provide a sound analytic basis for recommendations concerning contracting strategies and decisions related to contracts awarded to support the Department of Energy’s clean up mission. Recommendations are to be based on the consensus judgement of the Council members, taking into consideration input from field office managers, contractor self assessments, independent reviews of teams specifically tasked to evaluate contractor performance, and other factors determined by the Council to be relevant to making informed recommendations to EM-1.

III. Membership

a The CMAC shall be comprised of three EM HQ members appointed by the Assistant Secretary to two-year terms coinciding with the fiscal year. Board members selected from HQ will be either a Deputy Assistant Secretary, an Associate Deputy Assistant Secretary, and/or an Office Director from EM-5 or EM-6, or the Chief Operating Officer. There will be one at-large representative from an EM field site to be determined by the Assistant Secretary. The field representative shall serve for a one-year term on a fiscal year basis. Any member of the CMAC may be reappointed for an additional one-year term.
b The Office of Procurement and Assistance Management (ME) will be invited to name an Ex Officio advisor to the Council to provide guidance on Departmental procurement and acquisition policy. The term of the ME member shall be for one year, to be extended for a period of one-year as mutually agreed upon by the Council Chair and ME.

c The Council Executive Secretariat will be the Director of the Office of Management and Information. Operational support to the CMAC will be performed by an EM-7 staff member with the approval of the Assistant Secretary.

d The Chair of the CMAC (Chair) will be named by EM-1 from the three Headquarters members. The Chair will serve a one-year term coinciding with the fiscal year and may, at the discretion of EM-1, be named to serve as the Chair for an additional one-year term.

IV. Procedures

Council meetings may take place provided a minimum of two members are present. Decisions of the Council require a majority vote of the members present. In the event of a tie vote when only two members are present, the proposed action must be reconsidered at a Council meeting when the full complement of members are in attendance.

The Board will schedule 12 meetings each fiscal year - one each calendar month. The specific date of each meeting will be determined and published by the Executive Secretariat. As required by special circumstances, the Council may schedule emergency meetings ensuring that proper notification of such emergency meetings is provided to Council members and affected organization both at HQ and in the field.

The Council will establish in writing for EM-1 approval, a process for reviewing extend/compete decisions, contract planning and strategy decisions, annual contractor performance incentives, as appropriate, and annual contractor fee earnings. The process will be distributed to Council members and affected organizations in the field and at HQ.

V. Reports

TBD

VI. Termination

The Council will remain in existence until terminated by the Assistant Secretary for Environmental Management.