The Honorable Tim Murphy

1. **Your report recommends abandoning incentive award fees for M&O contracts in favor of a fixed fee.**

    a. **What prompted this recommendation?**

The Commission found that contracting organizations may be motivated to run laboratories out of a sense of service to the Nation, for reputational enhancement, for access to quality technical staff, and/or for other reasons, but management fee is not, and should not be, the primary motivation. Incentive fees may be appropriate for some types of production operations, but are not the best mechanism for research organizations. Fees must be adequate to cover unallowable costs, such as gaps in salary, community and educational contributions, employee scholarships, and potential risks, but they do not need to be as high as some of the recent NNSA laboratory contracts.[1]

The Commission also noted that approximately six years ago, NASA changed its contract for the Jet Propulsion Laboratory (JPL), also an FFRDC, from an incentive fee to a fixed fee. JPL personnel have found the change to be positive in that it has decreased bureaucracy associated with the annual fee awarding process. The primary incentive for the laboratory to perform well is that it will receive more research funding from NASA; the punishment is that it will receive less.

    b. **What are the advantages of a fixed fee versus an incentive fee?**

The Commissioners find that a high fee perpetuates the stereotype that laboratory managers and M&O contractors are focused only on profit and are merely "contractors" rather than partners. In addition, the process to evaluate performance and award fee has led to box checking and transactional compliance for the laboratories. Both of these have contributed to a breakdown in trust between some of the laboratories and DOE. The Commission agrees with the Augustine/Mies panel finding that the relationship between the NNSA laboratories and the government has been eroded by a fee structure and contract approach that invites detailed, tactical, and transactional oversight rather than a strategic, performance-based management approach.[2]

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[1] In FY 2014 the average available award fee as a percentage of the laboratory budget from DOE was 1.76%. While Sandia's (1.56%) was lower than the average, both Lawrence Livermore's (3.83%) and Los Alamos' (3.17%) were higher. This translated to an available award fee of $28.1M for Sandia, $45.9M for Lawrence Livermore, and $63.4M for Los Alamos.

[2] See Congressional Advisory Panel on the Governance of the Nuclear Security Enterprise (Augustine/Mies panel), *A New Foundation for the Nuclear Security Enterprise*, 12–14.

c. What is your reaction to the Department's response to this recommendation?

As noted, the Commission recommended that DOE abandon incentive award fees in the M&O contracts of the National Laboratories in favor of a fixed fee set at competitive rates with risk and necessary investment in mind. We are encouraged by the Department's recent step in this direction as outlined in the Draft Request for Proposal (RFP) for Sandia National Laboratories' M&O Contract Competition. The Draft RFP delineates three categories of work: (1) management and operation of the laboratory, for which the contractor will receive cost-plus-fixed-fee and award fee; (2) strategic partnership projects (formerly known as work for others), for which the contractor will receive only cost-plus-fixed-fee; and (3) capital construction projects, the price and price structure of which will be agreed upon individually.[3] This represents a significant step away from incentive fees and towards fixed fees and we are hopeful it will be extended to all laboratory contracts over time.

d. How can we measure meaningful progress by the Department in addressing this recommendation?

The most effective way to ensure meaningful progress is through the creation of an independent standing body as described in the final recommendation of our report. Such a standing body could track implementation of all the recommendations and actions in our report, and to report regularly to DOE, the laboratories, the Administration, and the Congress on progress, results, and needed corrective actions. The standing body could also assist congressional committees in developing a rational plan for future evaluations of the DOE laboratories.

2. Your report highlights opportunities for NNSA to leverage best practices from other DOE program offices – such as the Office of Science – to improve engagement between NNSA and their labs.

a. Why hasn't this occurred in the past?

We would like to note that NNSA has begun to leverage the best practices of other DOE program offices in certain areas. For example, according to the Department's response to the Commission report, "NNSA will execute plans to improve its governance and oversight of field operations at its laboratories, sites, and plants and clarifying roles and responsibilities. The new approach will clarify the oversight roles of headquarters and field office personnel, placing emphasis on new rigorous and dependable Contractor Assurance Systems (described below), and leveraging best practices from the Office of Science, including enhancing peer review and corporate parent involvement as appropriate for each site." (p.12) In

[3] Draft Request for Proposal No. DE-SOL-0008470

addition, "NNSA and the applied energy offices will model their revised [laboratory planning] processes using core elements and attributes from the lab planning process used by the Office of Science." (p.16)

We are encouraged by these initial steps, but it remains to be seen whether a true partnership between the weapons laboratories and NNSA can be established.

b. How does the current organizational and statutory structure between NNSA and DOE affect this type of collaboration?

There is no question that DOE's ability to influence NNSA's treatment and relationship with its laboratories is hampered by NNSA's semi-autonomous state. In the past, NNSA leadership and staff have chosen to ignore the best practices of other program offices within DOE and do things their own way, sometimes to the detriment of the relationship with their laboratories. As we said, the jury is still out on whether the latest effort to normalize their practices will have a lasting impact.