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DEPARTMENT OF ENERGY

Views on Proposed Legislation on Civil Penalties for Nuclear Safety Violations by Nonprofit Contractors

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Mr. Chairman and Members of the Subcommittee:

I am pleased to be here today to provide our views on H.R. 723, a bill that would modify the Atomic Energy Act of 1954 by changing how the Department of Energy (DOE) treats nonprofit contractors who violate DOE's nuclear safety requirements. Various nonprofit contractors, such as the Universities of California and Chicago, which operate DOE research laboratories in several states, are currently exempted from paying the civil penalties that DOE assesses under the act. H.R. 723 would remove that exemption. In a 1999 report on DOE's nuclear safety enforcement program, we recommended that the exemption be eliminated.[1] My testimony today will briefly explain why we continue to support this position and will also offer specific observations on H.R. 723.

In summary, we support eliminating the exemption because the primary reason for instituting it no longer exists. The exemption was enacted in 1988 at the same time the civil monetary penalty was established. The purpose of the exemption was to ensure that the nonprofit contractors operating DOE's laboratories at the time, who were being reimbursed only for their costs, would not have their assets at risk for violating nuclear safety requirements. At the present time, however, virtually all of DOE's nonprofit contractors have an opportunity to earn a fee in addition to payments for allowable costs. This fee could be used to pay the civil monetary penalties. Our review of DOE's nuclear safety enforcement program shows that it appears to be a useful and important tool for ensuring safe nuclear practices at all contractor locations. Eliminating the exemption would further strengthen this tool and provide more consistent accountability among contractors for violating nuclear safety rules.

We have four observations about the specific language in the bill. First, the definition of the amount of fee at risk is unclear. H.R. 723, while eliminating the exemption, provides a limitation on the amount of civil penalties that can be imposed on nonprofit contractors. The bill would limit the amount of any payment for penalties assessed against tax-exempt contractors to a contractor's "discretionary fee." In general, a contractor's total fee consists of a base fee, which is set in the contract, and an incentive fee, which is based on performance. It is not clear whether the term " discretionary fee" applies to all, or only a part of, a contractor's fee.

Second, if the Congress decides to limit the amount of fee at risk by specifying that "discretionary fee" means only the incentive fee portion of the total fee, the ability to impose penalties on nonprofit contractors may be limited. Two of the nonprofit contractors receive only a base fee (and no incentive fee) and, therefore, would continue to be exempt from paying civil penalties. Contractors may also try to limit their exposure to penalties by shifting more of their total fee to a base fee and away from an

[1] *Department of Energy: DOE's Nuclear Safety Enforcement Program Should Be Strengthened* (GAO/RCED-99-146, Jun. 10, 1999).

incentive fee. Such an action could undermine both the penalty provision and DOE's emphasis on performance-based contracting because a lower fee will depend on the contractor's performance. If the Congress decides to put the entire fee at risk, other statutory provisions already in place give the Secretary flexibility in setting penalty amounts by considering factors such as the contractor's ability to pay and, therefore, can be used to limit nonprofit contractors' financial risk.

Third, under the proposed bill, limitations on payments for civil penalties would be extended to all tax-exempt nonprofit contractors, not just nonprofit educational institutions. A contractor such as Brookhaven Science Associates, a nonprofit organization but not an educational institution, is now subject to the penalty provisions without limit for its work at Brookhaven National Laboratory. Under H.R. 723, Brookhaven Science Associates would be able to limit its payments to the amount of any discretionary fee received. This would provide for a more consistent treatment of nonprofit contractors.

Fourth, the penalty provisions specified in H.R. 723 would apply to contracts entered into after the date of enactment. Consequently, it could be many years before some of the contractors would have to pay a penalty. For example, the University of California potentially would not be subject to paying any penalties until at least 2005 because it recently received a 4-year contract extension to operate its DOE laboratories. In contrast to the proposed bill, when the Congress established the initial program of civil monetary penalties in 1988, the penalties applied to existing contracts.

Mr. Chairman, we suggest that the language in H.R. 723 be clarified to address these issues.

Background

DOE maintains nuclear facilities at 34 sites in 13 states. To carry out its missions at these sites, DOE relies on outside contractors. Because of the risks and the potential liabilities inherent in handling nuclear materials, the Price-Anderson Amendments Act of 1988 required DOE to indemnify, or agree to pay damages for, those contractors who could have an accident associated with handling nuclear materials and whose actions could cause damage to persons and property. DOE thus has a clear financial interest in ensuring that its contractors operate in a safe manner. DOE's primary approach to ensuring safe nuclear operations has been to require its contractors to follow DOE directives, including policies, orders, and standards, by incorporating these requirements into the contracts.

The Price-Anderson Amendments Act of 1988 gave DOE another tool for ensuring safe nuclear operations. This legislation allowed DOE to hold its contractors accountable for

meeting its nuclear safety requirements through a system of civil monetary penalties. In doing so, the legislation specifically exempted seven contractors at research laboratories, along with their subcontractors and suppliers, from having to pay any penalties assessed. In addition to the specific exemptions, the legislation also gave the Secretary of Energy the authority to exempt from paying penalties other nonprofit educational institutions under contract to DOE. In a 1993 rule describing the procedures it would follow in carrying out the enforcement program, DOE specified that all nonprofit educational institutions would receive an automatic exemption from paying the penalties. DOE established its nuclear safety enforcement program and began enforcing nuclear safety rules in 1996. As of February 2001, DOE had taken 57 enforcement actions and assessed penalties of over $5.5 million.

Continued Exemption of Nonprofit Contractors From Paying Civil Penalties Is Not Warranted

The rationale for exempting certain nonprofit contractors from paying the civil penalties no longer exists. During the initial congressional debates that led to the exemption being established in 1988, several reasons were cited for this exemption. The primary reason appears to have been that the contractors operating DOE's laboratories at the time received no fees in addition to their reimbursable costs and, therefore, had no contract-generated funds available to pay any penalties assessed. There was concern that the contractors operating the national laboratories, mostly nonprofit educational institutions, would be unwilling to assume the financial risk of being subject to penalties and thus put the assets of their organizations at risk, and that these contractors might leave the research field rather than accept this financial exposure. In contrast to the situation in 1988, DOE now pays a fee in addition to reimbursing allowable costs to virtually all of its major contractors, including the nonprofit educational institutions.[2] This fee is used by the nonprofit contractors to cover certain nonreimbursable contract costs and to conduct other laboratory research. The fee could also be used to pay civil penalties if they were imposed on the contractor.

Some of these nonprofit contractors have committed significant violations of nuclear safety requirements. Since 1996, a total of 13 of the 57 enforcement actions brought by DOE were against contractors managing DOE's laboratories that were exempt from paying the penalties. Their penalties, which DOE assessed but cannot collect, amounted to $1.8 million of the $5.5 million assessed thus far under the program. Table 1 summarizes the number of safety violations and the amount of penalties assessed against DOE laboratory contractors.

[2] Stanford University operates the Stanford Linear Accelerator Center without receiving a fee.

Table 1: Enforcement Actions Taken and Penalties Assessed Against Contractors Operating DOE Laboratories Exempted by Statute, 1996 Through February 2001

Laboratory	Contractor	Number of enforcement actions	Total penalties assessed exempt	Total penalties assessed nonexempt
Los Alamos National Laboratory, New Mexico	University of California	4[a]	$937,500	
Lawrence Livermore National Laboratory, California	University of California	3	395,625	
Brookhaven National Laboratory, New York[b]	Associated Universities, Inc.	1	142,500	
	Petsco & Son, Inc. (subcontractor)	1	37,500	
	Brookhaven Science Associates	1		$27,500
Argonne National Laboratory East, Illinois	University of Chicago	1	110,000	
	MOTA Corporation (subcontractor)	1	55,000	
Argonne National Laboratory West, Idaho	University of Chicago	1	110,000	
Sandia National Laboratory, New Mexico[c]	Sandia Corporation (Lockheed Martin)	4		61,250
Pacific Northwest National Laboratory, Washington	Battelle Memorial Institute	1	0	
Total			**$1,788,125**	**$88,750**

Note: The table includes penalties assessed against those DOE contractors exempted from paying civil penalties under the Price-Anderson Amendments Act of 1988, and their successor contractors. The 1988 amendments also exempted Universities Research Associates, Inc., at Fermi National Accelerator Laboratory in Illinois and Princeton University at the Princeton Plasma Physics Laboratory in New Jersey. No enforcement actions under the Price-Anderson Amendments Act of 1988 have been taken against those contractors.

[a]For one of these enforcement actions, no penalty was assessed.

[b]Brookhaven National Laboratory was operated by Associated Universities, Inc., one of the seven contractors identified as exempt from paying civil penalties in the Price-Anderson Amendments Act of 1988. Brookhaven Science Associates began operating the laboratory in March 1998, and is not exempt from paying the civil penalties.

[c]Sandia National Laboratory, previously operated by American Telephone and Telegraph Company, was identified as exempt from paying civil penalties in the Price-Anderson Amendments Act of 1988. Lockheed Martin, the successor contractor at Sandia National Laboratory, is not exempt.

As the following examples illustrate, these violations are cause for considerable concern:

- **Los Alamos National Laboratory, New Mexico**. In January 2001, DOE found that the University of California had inadequate work controls at one of its laboratory facilities, resulting in eight workers being exposed to airborne plutonium and five of those workers receiving detectable intakes of plutonium. This was identified as one of the 10 worst radiological intake events in the United States in over 40 years. DOE assessed, but cannot collect, a penalty of $605,000 for these violations.

- **Argonne National Laboratory West, Idaho**. In February 2001, DOE found that the University of Chicago had violated the radiation protection and quality assurance rules, leading to worker contamination and violations of controls intended to prevent an uncontrolled nuclear reaction from occurring. DOE assessed, but cannot collect, a penalty of $110,000 for these violations.

DOE has cited two other reasons for continuing the exemption, but as we indicated in our 1999 report, we did not think either reason was valid:

- DOE said that contract provisions are a better mechanism than civil penalties for holding nonprofit contractors accountable for safe nuclear practices. We certainly agree that contract mechanisms are an important tool for holding contractors accountable, whether they earn a profit or not. However, since 1990 we have described DOE's contracting practices as being at high risk for fraud, waste, abuse, and mismanagement.[3] Similarly, in November 2000, the Department's Inspector General identified contract administration as one of the most significant management challenges facing the Department.[4] We have noted that, recently, DOE has been more aggressive in reducing contractor fees for poor performance in a number of areas. However, having a separate nuclear safety enforcement program provides DOE with an additional tool to use when needed to ensure that safe nuclear practices are followed. Eliminating the exemption enjoyed by the nonprofit contractors would strengthen this tool.

- DOE said that its current approach of exempting nonprofit educational institutions is consistent with Nuclear Regulatory Commission's (NRC) treatment of nonprofit organizations because DOE issues notices of violation to nonprofit contractors without collecting penalties but can apply financial incentives or disincentives through the contract. However, NRC can and does impose monetary penalties for violations of safety requirements, without regard to the profit-making status of the organization. NRC sets lower penalty amounts for nonprofit organizations than for-profit organizations. The Secretary could do the same, but does not currently take this approach.[5] Furthermore, both NRC and other regulatory agencies have assessed and collected penalties or additional administrative costs from some of the same organizations that DOE exempts from payment. For example, the University of California has made payments to states for violating environmental laws in California and New Mexico because of activities at Lawrence Livermore and Los Alamos National Laboratories.

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[3] *Major Management Challenges and Program Risks: Department of Energy* (GAO-01-246, Jan. 2001).

[4] *Management Challenges at the Department of Energy* (DOE/IG-0491, Nov. 28, 2000).

[5] Although DOE does not collect payments from the exempted contractors, it does assess penalties in the same way as for the for-profit contractors.

The enforcement program appears to be a useful and important tool for ensuring safe nuclear practices. Our 1999 review of the enforcement program found that, although it needed to be strengthened, the enforcement program complemented other contract mechanisms DOE had to help ensure safe nuclear practices. Advantages of the program include its relatively objective and independent review process, a follow-up mechanism to ensure that contractors take corrective action, and the practice of making information readily available to the contractor community and the public.

Modifications to H.R. 723 Could Help Clarify and Strengthen the Penalty Provisions

H.R. 723 eliminates both the exemption from paying the penalties provided by statute and the exemption allowed at the Secretary's discretion. While addressing the main problems we discussed in our 1999 report, we have several observations about clarifications needed to the proposed bill.

The "discretionary fee" referred to in the bill is unclear. H.R. 723, while eliminating the exemption, limits the amount of civil penalties that can be imposed on nonprofit contractors. This limit is the amount of "discretionary fees" paid to the contractor under the contract under which the violation occurs. The meaning of the term "discretionary fee" is unclear and might be interpreted to mean all or only a portion of the fee paid.[6] In general, the total fee—that is, the amount that exceeds the contractor's reimbursable costs—under DOE's management and operating contracts consists of a base fee amount and an incentive fee amount. The base fee is set in the contract. The amount of the available incentive fee paid to the contractor is determined by the contracting officer on the basis of the contractor's performance.

Since the base fee is a set amount, and the incentive fee is determined at the contracting officer's discretion, the term "discretionary fee" may be interpreted to refer only to the incentive fee and to exclude the base fee amount. However, an alternate interpretation also is possible. Certain DOE contracts contain a provision known as the "Conditional Payment of Fee, Profit, Or Incentives" clause. Under this contract provision, on the basis of the contractor's performance, a contractor's entire fee, including the base fee, may be reduced at the discretion of the contracting officer. Thus, in contracts that contain this clause, the term "discretionary fee" might be read to include a base fee.

If the Congress intends to have the entire fee earned be subject to penalties, we suggest that the bill language be revised to replace the term "discretionary fee" with "total amount of fees." If, on the other hand, the Congress wants to limit the amount of fee that would be subject to penalties to the performance or incentive amount, and exclude the

[6] The term was also used in H.R. 3383, in the 106th Congress, and was defined in accompanying committee reports to refer to that portion of the contract fee which is paid, or not, at the discretion of the DOE contracting officer based on the contractor's performance.

base fee amount, we suggest that the bill be revised to replace the term "discretionary fee" with "performance or incentive fee."

Limiting the amount of any payment for penalties made by tax-exempt contractors to the amount of the incentive fee could have unintended effects. Several potential consequences could arise by focusing only on the contractor's incentive fee. Specifically:

- **Contractors would be affected in an inconsistent way**. Two of the nonprofit contractors—University Research Associates at the Fermi National Accelerator Laboratory and Princeton University—do not receive an incentive fee (they do receive a base fee). Therefore, depending on the interpretation of the term "discretionary fee" as discussed above, limiting payment to the amount of the incentive fee could exempt these two contractors from paying any penalty for violating nuclear safety requirements.

- **Enforcement of nuclear safety violations would differ from enforcement of security violations**. The National Defense Authorization Act for Fiscal Year 2000 established a system of civil monetary penalties for violations of DOE regulations regarding the safeguarding and security of restricted data. The legislation contained no exemption for nonprofit contractors but limited the amount of any payment for penalties made by certain nonprofit contractors to the total fees paid to the contractor in that fiscal year.[7] In contrast, these same contractors could have only a portion of their fee (the "discretionary fee") at risk for violations of nuclear safety requirements. It is not clear why limitations on the enforcement of nuclear safety requirements should be different than existing limitations on the enforcement of security requirements.

- **Disincentives could be created if the Congress decides to limit the penalty payment to the amount of the incentive fee**. We are concerned that contractors might try to shift more of their fee to a base or fixed fee and away from an incentive fee, in order to minimize their exposure to any financial liability. Such an action would have the effect of undermining the purpose of the penalty and DOE's overall emphasis on performance-based contracting. In fact, recent negotiations between DOE and the University of California to extend the laboratory contracts illustrate this issue. According to the DOE contracting officer, of the total fee available to the University of California, more of the fee was shifted from incentive fee to base fee

[7] The institutions receiving the payment limitation included the University of Chicago; the University of California; American Telephone and Telegraph; Universities Research Associates, Inc.; Princeton University; Associated Universities, Inc.; and Battelle Memorial Institute. American Telephone and Telegraph and The Associated Universities, Inc. no longer have contracts to operate DOE laboratories.

during recent negotiations because of the increased liability expected from the civil penalties associated with security violations.[8]

If a nonprofit contractor's entire fee was subject to the civil penalty, the Secretary has discretion that should ensure that no nonprofit contractor's assets are at risk because of having to pay the civil penalty. This is because the Secretary has considerable latitude to adjust the amount of any civil penalty to meet the circumstances of any specific situation. The Secretary can consider factors such as the contractor's ability to pay and the effect of the penalty on the contractor's ability to do business.

Preferential treatment would be expanded to all tax-exempt contractors. Under the existing law, in addition to the seven contractors exempted by name in the statute, the Secretary was given the authority to exempt nonprofit educational institutions. H.R. 723 takes a somewhat different approach by exempting all tax-exempt nonprofit contractors whether or not they are educational institutions. This provision would actually reduce the liability faced by some contractors. For example, Brookhaven Science Associates, the contractor at Brookhaven National Laboratory, is currently subject to paying civil penalties for nuclear safety violations regardless of any fee paid because, although it is a nonprofit organization, it is not an educational institution. Under the provisions of H.R. 723, however, Brookhaven Science Associates would be able to limit its payments for civil penalties. This change would result in a more consistent application of civil penalties among nonprofit contractors.

Some contractors might not be subject to the penalty provisions until many years in the future. As currently written, H.R. 723 would not apply to any violation occurring under a contract entered into before the date of the enactment of the act. Thus, contractors would have to enter into a new contract with DOE before this provision takes effect. For some contractors that could be a considerable period of time. The University of California, for example, recently negotiated a 4-year extension of its contract with DOE. It is possible, therefore, that if H.R. 723 is enacted in 2001, the University of California might not have to pay a civil penalty for any violation of nuclear safety occurring through 2005. In contrast, when the Congress set up the civil penalties in 1988, it did not require that new contracts be entered into before contractors were subject to the penalty provisions. Instead, the penalty provisions applied to the existing contracts. In reviewing the fairness of this issue as DOE prepared its implementing regulations, in 1991 DOE stated in the *Federal Register* that a contractor's obligation to comply with nuclear safety requirements and its liability for penalties for violations of the requirements are independent of any contractual arrangements and cannot be modified or eliminated by the operation of a contract.[9] Thus, DOE considered it appropriate to apply the penalties to the contracts existing at the time.

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[8] In fiscal years 1999 and 2000, DOE's contract with the University of California did not use the term base fee but instead identified an amount of fee that was not subject to reduction for poor performance.

[9] See 56 *Fed. Reg.* 64290, 64291 (Dec. 9, 1991).

If the Congress chooses to keep the effective date provision in H.R. 723, we believe it should consider clarifying the language as to whether a modification or extension of an existing contract meets the test of a contract entered into after the date of the enactment of the act. This is important because a number of the contracts to operate DOE's laboratories have been extended rather than recompeted.

Thank you, Mr. Chairman and Members of the Subcommittee. This concludes my testimony. I will be happy to respond to any questions that you may have.

GAO Contact and Staff Acknowledgment

For future contacts regarding this testimony, please contact (Ms.) Gary L. Jones at (202) 512-3841. Carole Blackwell, Doreen Feldman, and Bill Swick also made key contributions to this testimony.

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