



DEPARTMENT OF THE NAVY  
NAVAL FACILITIES ENGINEERING COMMAND  
WASHINGTON NAVY YARD  
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WASHINGTON, DC 20374-5065

IN REPLY REFER TO  
ACQ 021  
23 May 00

MEMORANDUM FOR NAVFAC ACQUISITION PERSONNEL

Subj: CONTRACTOR INCENTIVES (00-23)

Ref: (a) [NAVFAC Policy Memo of 10 Jun 99 \(99-19\)](#)

Encl: (1) OASN(RD&A) ABM memo of 22 Dec 99

1. Reference (a) requested that award fee contracts be reviewed to determine whether award fee periods, evaluation factors, and earned award fee percentages are commensurate with overall contractor performance.

2. Enclosure (1) is furnished for your information. Particular attention should be focused on the principles addressed in the Contractor Incentives IPT report when structuring future contract incentives. These principles are intended to improve the process for establishing contract incentives that compel the contractor's performance.

3. Award fee evaluation plans and factors should be tailored to fit the circumstances of each individual procurement. Rigid standardization tends to generate evaluation plans that are either too broad or include factors inapplicable to a given function. In either case, evaluators are likely to experience difficulties in providing meaningful comments and ratings. If the Government's relative priorities change as work progresses from one phase into the next, or as unexpected problems or developments occur such as schedule slippages, the evaluation plan may be revised on a unilateral basis, to communicate such changes to all parties.

4. A properly structured and administered award fee contract encourages the desired quality of performance, contractor efficiency, and innovation. An additional benefit is the opportunity for more effective communications among Government and contractor personnel, at management levels where decisions can be made and results achieved. Throughout the period of performance, the contractor should be encouraged to submit suggestions for improving or changing the evaluation process. Both the Government and the contractor should work to eliminate any unnecessary contractual,

Subj: CONTRACTOR INCENTIVES (00-##)

organizational or conceptual barriers that constrain information sharing and other communications needed for successful joint problem solving.

A handwritten signature in black ink, appearing to read "M. F. Howard". The signature is stylized and cursive.

MICHAEL F. HOWARD  
Director, Strategic Management  
Community Management Section



DEPARTMENT OF THE NAVY  
OFFICE OF THE ASSISTANT SECRETARY  
RESEARCH, DEVELOPMENT AND ACQUISITION  
1000 NAVY PENTAGON  
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DEC 22 1999

MEMORANDUM FOR PROGRAM EXECUTIVE OFFICERS  
DIRECT REPORTING PROGRAM MANAGERS  
COMMANDERS OF THE SYSTEMS COMMANDS

Subj: CONTRACTOR INCENTIVES

Encl: (1) USD (AT&L) memorandum of November 23, 1999

The Under Secretary of Defense (Acquisition, Technology and Logistics), concerned that contractors do not have incentives which focus on the outcomes the Government most desires, established an Integrated Process Team to address this issue. By enclosure (1), USD (AT&L) provides several principles that will be useful when structuring contract incentives. The report of the Contractor Incentives IPT can be accessed at the ABM Homepage [<http://www.abm.rda.hq.navy.mil>].

Program managers often have conflicting goals such as long-term issues of life cycle management and near term issues of performance. By effectively prioritizing performance outcomes and structuring contract incentives to coincide with the desired outcomes for a specific evaluation period, the contractor is motivated to produce outcomes that better reflect the Government's requirements.

  
Paul P. Buonaccorsi  
Executive Director  
Acquisition and Business  
Management

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ACQUISITION AND  
TECHNOLOGY

## THE UNDER SECRETARY OF DEFENSE

3010 DEFENSE PENTAGON  
WASHINGTON, DC 20301-3010

23 NOV 1999

MEMORANDUM FOR SECRETARIES OF THE MILITARY DEPARTMENTS  
ATTENTION: SERVICE ACQUISITION EXECUTIVES

SUBJECT: Contractor Incentives

During the Contractor Assessment Reviews that I conducted earlier this year, it was apparent that contractors do not always have an incentive to focus their attention on the outcomes that the government desires most. I asked the Director, Defense Procurement to establish an Integrated Process Team to address this issue. The team established several principles which I believe you will find useful when structuring future contract incentives:

- Contract incentives should be flexible and structured on a case-by-case basis.
- Award fee contracts should provide short evaluation periods with a limited number of evaluation criteria.
- Effective motivators were found to include allowances for special rewards for achievement of superior performance.
- An incentive fee arrangement with multiple incentives may be used when contract performance is measurable in objective terms. Regardless of contract type, earned fee should be commensurate to performance, and consistently applied among the varying arrangements.
- The correlation of award fee payments and performance evaluations would be enhanced by using an award fee evaluation that roughly corresponds to achievements addressed in the performance evaluation, and by using consistent definitions for evaluation terms.
- Obtain support from the Comptroller early where the award fee plan contemplates retention of dollars in an award fee pool for long periods of time.



The report of the Contractor Incentives IPT is attached for your information. I appreciate the support each of you afforded to this effort, and I am encouraged that there is continuing activity to improve the process. I urge you to continue to evaluate your experience with contract incentives, and to publish effective incentive arrangements for potential application throughout the Department.



J. S. Gansler

Attachment:  
As stated