

The Regents of the University of California

**COMMITTEE ON OVERSIGHT OF THE
DEPARTMENT OF ENERGY LABORATORIES**

September 20, 2006

The Committee on Oversight of the Department of Energy Laboratories met on the above date at UCSF–Mission Bay Community Center, San Francisco.

Members present: Regents Blum, Dynes, Marcus, Parsky, Pattiz, Preuss, and Schreiner; Advisory member Oakley

In attendance: Regents Coombs, De La Peña, Gould, Hopkinson, Island, Johnson, Lansing, Ledesma, Ruiz, Varner, and Wachter, Regents-designate Allen, Brewer, and Bugay, Faculty Representative Brown, Acting Secretary Shaw, Acting General Counsel Blair, Chief Investment Officer Berggren, Executive Vice President Darling, Provost Hume, Vice Presidents Foley and Gomes, Chancellors Córdova, Drake, Fox, Vanderhoef, and Yang, Acting Chancellors Abrams and Blumenthal, Provost Alley representing UC Merced, University Auditor Reed, and Recording Secretary Bryan

The meeting convened at 9:25 a.m. with Committee Chair Pattiz presiding.

1. **APPROVAL OF MINUTES OF PREVIOUS MEETING**

Upon motion duly made and seconded, the minutes of the meeting of July 19, 2006 were approved.

2. **STATUS OF COMPETITION AND OTHER MATTERS AT THE DEPARTMENT OF ENERGY LABORATORIES**

Vice President Foley reported that recent comments from the National Nuclear Security Administration (NNSA) indicated a very high level of satisfaction with the way in which the Los Alamos National Security team and everyone at the Los Alamos National Laboratory have been engaged in implementing the new contract structure and approach to the stewardship of the laboratory. There is a level of optimism about the laboratory that bodes well for the future.

Mr. Foley noted that the second year of the new contract has begun at the Lawrence Berkeley National Laboratory. The management team at Berkeley is performing well. The University's new oversight mechanisms, both the advisory board co-chaired by Provost Hume and former Lockheed chairman Mr. Norm Augustine and the contract assurance council, are fulfilling their missions.

Vice President Foley commented on the status of the competition for the management contract of the Lawrence Livermore National Laboratory (LLNL). He recalled that the

final Request for Proposal (RFP) for the management of the laboratory was issued by the NNSA on July 14, 2006. Responses are due on October 12. The Livermore RFP is similar to the RFP for the Los Alamos laboratory with regard to its emphasis on science and the need for critical research and management skills. He recalled that in July 2006 The Regents authorized the University to form a limited liability company with team members to be responsive to the NNSA RFP for the Livermore laboratory. The University has joined with Bechtel and is finalizing arrangements with other potential team members.

Mr. Foley noted that the cost of the University's participation in the proposal, as in the proposals for the Lawrence Berkeley and Los Alamos laboratory bids, is not funded from State funds or student fees. It is funded from past fee income earned at Los Alamos and Livermore and placed in a contingency fund that, under UC's contract with the government, is limited to paying for costs associated with the national laboratories and the competitions. Following the proposal submission, there will be an oral presentation required by the bidders. This is expected to occur between November 15 and Thanksgiving. Thereafter, the NNSA will continue its review of submitted proposals, with an award being made before the end of March 2007. Under the terms of the RFP, the winner of the competition will negotiate a transition cost proposal with the NNSA and will commence personnel transition activities in April 2007. The current contract expires at the end of September 2007. Personnel transition activities involve the presentation of a compensation, pension, and benefits design proposal to the NNSA, public review, comment on the proposal, and individual employees' evaluation of whether to accept transfer to the new employer on October 1, 2007. All employees at Livermore will remain UC employees until the expiration of the current contract. Other new contract transition activities will commence on July 1, 2007 related to preparations to take over the mission of the laboratory and all of the operational and support elements.

Chairman Parsky noted that the RFP pertaining to the Livermore laboratory is a public document and has been provided to all Regents. Once the competition is concluded, all matters that are not deemed confidential relating to the process, including the costs, will be made available to the Regents and the public. It is anticipated that the preparation costs relating to the Livermore contract will be approximately \$3 million. The RFP does not address the issue of weapons production; the production or manufacturing of weapons at Livermore is not a task in the RFP to which the University must respond. The thrust of the University's proposal needs to be that the work at the laboratory will be directed toward science and research. That is the reason the University would participate in the bid, albeit that the involvement of corporate partners is to address issues that the Regents recognize occurred in the past at Los Alamos in the areas of business operations, safety, and security.

Chairman Parsky noted that the establishment of joint ventures changes the arrangement with the DOE. It is a contract between not the University but the limited liability company and the DOE. The net fee income that will be available could be a significant amount. The Regents are being asked to inform the Office of the President that this net

fee income may be expended on science and research. It is up to President Dynes to come forward with recommendations on how that should best be done. If there will be an expenditure of any of this income for other purposes, it must come to the Regents for approval in advance.

President Dynes believed that it was the University's responsibility to assure the nation that the best science and technology is being done at Livermore and Los Alamos in the nation's interest and that using the fee to stimulate, motivate, and create science and technology at the Livermore laboratory is the appropriate use of the fee.

In response to a question asked by Regent Preuss, Vice President Foley reiterated that there were no substantive differences between the Los Alamos and Livermore RFPs with regard to the benefits and duties of the University other than that weapon pit production is not identified as an element of the statement of work. The fundamental point spread in evaluating the proposals is about the same; overwhelmingly it is focused on science and technology. He perceived no major issues that would warrant not submitting a proposal to manage the Livermore laboratory.

3. **APPROVAL TO PARTICIPATE IN A RESPONSE TO A DEPARTMENT OF ENERGY/NATIONAL NUCLEAR SECURITY ADMINISTRATION REQUEST FOR PROPOSAL TO MANAGE AND OPERATE THE LAWRENCE LIVERMORE NATIONAL LABORATORY**

The President recommended that:

- A. The University be authorized to participate in submitting a proposal in response to the Department of Energy/National Nuclear Security Administration Request for Proposal, dated July 14, 2006, for the management and operation of the Lawrence Livermore National Laboratory.
- B. The Chairman of The Regents, Gerald L. Parsky, supported by appropriate University personnel, be authorized to enter into such agreements and execute such other documents as are necessary in the course of submission of such proposal, or as a consequence of DOE/NNSA acceptance of such proposal.

It was recalled that the future management and operating contract for the Lawrence Livermore National Laboratory is being competitively awarded as required by Section 301 of the Energy and Water Appropriations Act for FY2004. A Request for Proposal was issued by the Department of Energy/National Nuclear Security Administration on July 14, 2006, asking for proposals to be submitted no later than October 12, 2006.

The Lawrence Livermore National Laboratory is a nuclear weapons research facility operated for the National Nuclear Security Administration within the Department of Energy. Since its inception, LLNL has been managed by the University, based upon a federal sole source determination that the University was uniquely qualified for the job.

As a matter of federal policy, however, the Congress directed DOE/NNSA to open to competition all contracts that had not been open to bid in excess of 50 years. Accordingly, the future contract for Lawrence Livermore will be awarded competitively.

Pursuant to the July 20, 2006 authorization of The Regents to establish a limited liability company for the purpose of competing for and performing the contract for Lawrence Livermore National Laboratory, the University is presently engaged in negotiations with prospective teaming partners to prepare a proposal and establish an LLC to bid on the contract.

The LLNL RFP differs from the LANL RFP in that weapon pit production is not identified as an element of the statement of work in the LLNL RFP. Other differences principally reflect local conditions, for example the absence of the specific regional economic development and technology transfer initiatives set forth in the LANL RFP. Further, proposal evaluation and selection point allocations are modified slightly from the LANL RFP but still reflect a preponderance of points associated with science and technology and related criteria. Out of a total of 1000 points, science and technology areas were assigned 650 points in the LANL RFP and 675 points in the LLNL RFP. As in the LANL RFP, due to federal regulations associated with competitive procurement, the future contract for management and operation of LLNL will not have certain negotiated terms that have been a part of the University's past contracts but which cannot be offered to all potential bidders:

- A right to terminate the contract at the election of the University
- Unrestricted application of the University's corporate practices and programs to the laboratory
- Exemption from termination for default

Instead, the University's team and all offerors must submit proposals that conform to the requirements of the solicitation. In such a process the University must be prepared to accept standard terms and conditions in order to be eligible to receive the contract. The principal features of the solicitation are:

- Standard contract clauses that conform to the requirements of the Federal Acquisition Regulations and the Department of Energy Acquisition Regulations as published in the Federal Register and applicable to management and operating contracts
- Special terms associated with the new Lawrence Livermore contract, to include:
 - The requirement of a separate legal entity to act as prime contractor
 - Creation of at least two site specific pension plans - one for transferring UC employees who are not retiring under UCRP or going inactive under

- UCRP, and another for new employees and rehired UCRP retirees and inactives
- A contract compliance assurance process
 - Commitment to use best practices
 - An opportunity to substitute DOE orders with external regulatory and industrial standards
 - An opportunity to extend the contract performance period from 7 years to 20 years without an extend or compete decision by DOE/NNSA
 - An opportunity to earn a DOE/NNSA fee of between \$36.7 million and .5 million per year during each year of the initial 7-year period, with additional fee earned for work performed for other federal agencies
 - DOE/NNSA approval of human resource practices and employee pensions and benefits

Given that this is a competitive federal solicitation, that The Regents will not be the contracting entity and do not own the real property or facilities at LLNL, and that The Regents does not exercise significant discretion with respect the projects to be conducted under the contract, all of which are covered by the National Environmental Protection Act; the General Counsel has determined that independent California Environmental Quality Act documentation to support a decision to authorize participation in the proposal is not necessary.

Acting General Counsel Blair will provide separate advice to the Regents on the legal implications to the University of forming the LLC, the submission by the LLC of a proposal that is responsive to the requirements of the RFP, and the acceptance by the LLC of the terms of the resulting contract.

Upon motion duly made and seconded, the Committee approved the President's recommendation and voted to present it to the Board.

4. **APPROVAL OF A UNIVERSITY PROCEDURE FOR APPROPRIATING NET FEE INCOME RECEIVED AS OWNER OF A LIMITED LIABILITY COMPANY MANAGING A DEPARTMENT OF ENERGY NATIONAL LABORATORY**

The President recommended that:

- A. Net fee income from the University's ownership of a limited liability company holding a contract to manage and operate a Department of Energy national laboratory be expended for the limited purposes of funding scientific research, defraying University liabilities associated with its ownership interest in the LLC and/or any other obligations directly between the University and DOE (including reserves for future claims), and supplementing income for certain LLC employees who, consistent with the LLC Agreement, are recruited to the laboratory by the University.

- B. The President develop, in consultation with the chancellors, laboratory director(s), and the Academic Senate, an annual plan for funding scientific research from net fee income.
- C. The President submit the annual plan to The Regents for approval in advance each year.
- D. The President report annually to The Regents on the net fee income received and expenditures made therefrom.
- E. Any expenditure of net fee income for purposes other than those identified above shall be presented by the President to The Regents for approval in advance.

It was recalled that the University is a part owner of the Los Alamos National Security LLC, the entity managing and operating the Los Alamos National Laboratory for the National Nuclear Security Administration within the United States Department of Energy. If the Regents, in a separate action item for this meeting, authorize the University to participate in the competitive proposal for management and operation of the Lawrence Livermore National Laboratory and if that proposal were to be accepted by DOE, the University would be a part owner of a second LLC managing a DOE national laboratory.

The University's sole management of LANL ended on May 31, 2006. The University's sole management of LLNL will end on September 30, 2007. The University has managed these facilities since their inception. Beginning in 1992, the University received management fees for the operation of these facilities in addition to reimbursement of direct and indirect costs associated with corporate oversight; collectively these revenues have been reported annually as "contract compensation." University practice has been to apply the management fees to scientific research insofar as they were not required to defray obligations associated with the contract activities incurred by the University that were not otherwise reimbursed by the federal government. This practice was followed due to the public service nature of the University's commitment to manage the two national security laboratories and the desire to ensure that University decisions relating to the laboratories were unaffected by the opportunity to earn additional fees. That is, fee income, as opposed to indirect and direct cost reimbursements, was not used to fund general University operations.

By virtue of the University's ownership interest in LANS LLC, and a new LLC for LLNL (if the University decides to participate in submitting a proposal and that proposal is accepted), the University will continue to receive fee income associated with DOE national laboratories. However, the nature of that income will be changed. Cost disallowances at the laboratories and any other costs of the LLC that are not reimbursed by the federal government will be paid out of fee earned by the LLC before a net income amount is distributed to the owners of the LLC. The University will not be required to expend funds for unallowable contract costs unless the costs exceed the fees paid to the LLC.

Under the prior contracts the University and DOE stated, as a contract term, the purposes and uses of fee. The new contracts contain no provision regarding how the University's net income will be spent. The University believes it is important to retain the philosophy that net fee income be expended for scientific research and not become an element of funding for University operations. Annual net fee income can be affected by numerous factors, none of which are in the direct control of the University. Accordingly, the University needs to adopt a procedure for appropriating net income actually received that can respond flexibly to changing circumstances.

The President proposes that net fee income be expended for funding scientific research and paying for obligations of the University associated with contract activities that are not paid for by the LLC. An example of the latter includes the creation of reserves for and payment of the University's share of any federal claims, or unreimbursed costs, in excess of LLC income. In the past the University created reserves for claims in the amount of \$20 million for the prior contracts. Under those contracts the University is solely liable. The prior contracts contain limitations that make those reserves unavailable for costs associated with the new contracts. The University is not solely liable under the new contracts and would create new reserves reflecting its reduced liability. Because of the restrictions on use of prior reserves, the University has used a significant portion of these funds to pay for laboratory competitions, and the net balance of this reserve, along with net fee income from LLC operations, is available for payment of any federally unreimbursed claims associated with closeout of the prior contracts.

In the past the scientific research funded by LANL and LLNL management fees was essentially divided into two categories: a Complementary and Beneficial Activities (CBA) fund managed by the Office of the President; and a second discretionary research fund managed by the laboratory director referred to as University of California-directed Research and Development (UCDRD) that featured significant laboratory-campus research collaborations. The CBA funds were expended to support the Institute of Geophysics and Planetary Physics, the Institute on Global Conflict and Cooperation, and competitive research proposals at campuses that related to mission areas of the national laboratories.

The President proposes that the University adopt an approach to identifying and funding scientific research with University net fee income that integrates the Office of the President, the chancellors, the laboratory director(s), and the faculty in the development of peer-reviewed scientific research proposed jointly by the laboratories and the campuses, as well as other University research. The focus of research would remain on activities relevant to laboratory missions and to providing graduate and post-graduate research opportunities to those who would be good recruits for one or both of the national laboratories. This would require that the research be unclassified and publishable. The research would be conducted principally at the University campuses and associated research institutes.

The President proposes that the research plan, developed as described above, be submitted annually to the Regents for their approval in advance each year, and that a financial report be made to the Regents regarding the expenditure of net fees collected during the prior year.

Regent Hopkinson expressed the concern that there are no costs under these criteria that are permitted for the Office of the President, which is likely to have legitimate costs related to oversight. Chairman Parsky explained that the arrangements with respect to each of the limited liability companies is different from the arrangements that existed in the past with DOE. The University is free to spend the fee income that comes from the LLC as it wishes. The DOE places no restriction on how the fee may be used, but the President would be obligated to seek Regental approval for spending it on things other than funding scientific research.

Upon motion duly made and seconded, the Committee approved the President's recommendation and voted to present it to the Board.

5. **APPOINTMENTS TO THE EXECUTIVE COMMITTEE OF THE BOARD OF GOVERNORS OF LAWRENCE LIVERMORE NATIONAL SECURITY, LLC**

The Vice Chairman of the Board of Regents, acting in the recusal of the Chairman for the purpose of this action, and the President of the University recommended that Chairman Gerald L. Parsky and Chancellor Marye Anne Fox be appointed as Governors of the Executive Committee of the Board of Governors of the limited liability company to be formed and known as Lawrence Livermore National Security, LLC; and that Executive Vice President Bruce B. Darling be likewise so appointed in an acting capacity pending the permanent filling of the Executive Vice President positions approved at the July 20, 2006 meeting of The Regents.

It was recalled that by action at the meeting of July 19, 2006, The Regents authorized the Chairman of The Regents to participate in the establishment of a limited liability company to be created for the purpose of competing for and performing the contract for the operation of the Lawrence Livermore National Laboratory, and authorized individuals to be appointed to the governing board of such LLC in the same manner as has been approved by The Regents with regard to the Board of Governors of Los Alamos National Security, LLC. The formation of such an LLC for the Livermore competition is expected to be completed in time to submit a responsive proposal. In order to complete the formation of an LLC for the Livermore competition, University representatives to its governing board need to be appointed.

By action at the meeting of March 15, 2006, The Regents adopted a policy on appointment of individuals to fill vacancies on the Executive Committee of Los Alamos National Security, LLC. In accordance with that policy, the Chairman and President recommend a selected candidate or candidates to The Regents, through the Committee on Oversight of the Department of Energy Laboratories, for consideration and approval.

Chairman Parsky, Executive Vice President Darling, and Chancellor Fox are serving as the University's appointees to the Executive Committee of Los Alamos National Security, LLC. By this action it is recommended that they also be appointed to serve on the Executive Committee of the counterpart LLC being formed for the purpose of competing for and performing the contract for Lawrence Livermore National Laboratory.

It is a requirement of the Request for Proposal issued by the Department of Energy's National Nuclear Security Administration, that any bidder submitting a responsive proposal form a separate legal entity, to exist for the sole purpose of performing the contract to be awarded for the management and operation of Lawrence Livermore National Laboratory.

Upon motion duly made and seconded, the Committee approved the Vice Chairman's and President's recommendation and voted to present it to the Board.

Chairman Parsky did not vote on the recommendation so as to avoid the appearance of a conflict of interest.

The meeting adjourned at 9:50 a.m.

Attest:

Acting Secretary