



DEPARTMENT OF THE NAVY  
OFFICE OF THE ASSISTANT SECRETARY  
RESEARCH, DEVELOPMENT AND ACQUISITION  
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WASHINGTON DC 20350-1000

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*  
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Executive Director  
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Management

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Subj: REVISED CONTRACTOR PERFORMANCE ASSESSMENT REPORTING SYSTEM  
(CPARS) GUIDE

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ACQUISITION AND  
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## 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