Los Alamos Study Group

Nuclear Disarmament • Environmental Protection • Social Justice • Economic Sustainability

Memorandum

October 13, 2008

Re: National Nuclear Security Administration's (NNSA's) Kansas City Plant (KCP) plans

To: Hon. Thomas P. D'Agostino, Administrator, NNSA
Mr. William C. Ostendorff, NNSA Principal Deputy Administrator
Mr. Steve C. Taylor, Manager, NNSA Kansas City Site Office
Ms. Neile Miller, Director, Office of Budget, Department of Energy (DOE)
Mr. Paul Rehmus, Office of Management and Budget (OMB)
Hon. James A. Williams, Acting Administrator, General Services Administration (GSA)
Mr. Bradley Scott, Heartland Regional Administrator, GSA
Mr. Vince Trim, President, Honeywell Federal Manufacturing and Technology
Hon. Mark Funkhouser, Mayor, Kansas City
Hon. Terry Riley, Councilman and Chair, Planning and Zoning Committee

cc: Rep. Pete Visclosky, Chairman, House Appropriations Subcommittee for Energy and Water Development, c/o Mr. Robert Sherman
Rep. David Hobson, Ranking Member, House Appropriations Subcommittee for Energy and Water Development, c/o Mr. Kevin Cook
Sen. Byron Dorgan, Chairman, Senate Appropriations Subcommittee for Energy and Water Development, c/o Mr. Douglas Clapp
Sen. Pete Domenici, Ranking Member, Senate Appropriations Subcommittee for Energy and Water Development
Rep. Hon. Ellen Tauscher, Chairwoman, House Armed Services Subcommittee on Strategic Forces, c/o Mr. Rudy Barnes
Sen. Bill Nelson, Chairman, Senate Armed Services Subcommittee on Strategic Forces, c/o Ms. Madelyn Creedon
Senator Claire McCaskill, c/o Ms. Corey Dillon
Senator Kit Bond, c/o Jamie Hollenberg
Rep. Emanuel Cleaver, II, c/o Mr. Danny Rotert
Mr. Patrick T. Hoopes, NNSA Senior Technical Advisor, Kansas City Site Office
Mr. Charlie Cook, Public Affairs Officer, GSA
Mr. David Pack, Chair, PeaceWorks Kansas City
Mr. Kevin Collison, *Kansas City Star*

What follows is a short, interim summary of our views on this subject for your convenience. For most of the issues we raise more details are available upon request and we would be happy to talk any of you about any of them. What we don't know – which is considerable – we can try to find out.

The Study Group has almost two decades of experience in vetting NNSA infrastructure proposals and we would like to be of service in this situation.

We would like to thank a number of you for your kind assistance over the past few months, especially those of you who met with us on our recent trip to Kansas City and KCP.

Summary

1) We believe NNSA should abandon its Kansas City Responsive Infrastructure Manufacturing & Sourcing" (KCRIMS) proposal to the extent KCRIMS relies on a newly-built, non-federally-owned manufacturing facility.

   Strong fiscal, managerial, and national security concerns underlie this judgment.

   While we at the Study Group can and do define national security more broadly than NNSA's congressional mandate, the national security concerns we are raising here are NNSA's.

2) *We believe NNSA has much better option*s. Superior options for fulfilling KCP's current and planned functions, in what we believe to be declining order of overall fiscal, managerial, and mission effectiveness, are these:

   a) *Retaining all or part of NNSA's present KCP facilities* in the Bannister Federal Complex (BFC);

   Or, if a new facility absolutely must be built for reasons that still escape us,

   b) *Building a new government-owned facility in Kansas City via a congressional line item*, possibly at the Botts Road site. The delay would be, we believe, quite manageable – less than a year. Should an environmental impact statement (EIS) be required, much of the work involved has already been done, provided the only alternatives included are the Kansas City alternatives already analyzed in the previous environmental assessment (EA). Inclusion of non-Kansas City alternatives would necessitate extensive delays and additional National Environmental Policy Act (NEPA) analyses.

   All other options are dramatically less attractive than these – fiscally, managerially, and in terms of mission effectiveness.

3) The ultimate resolution of remaining environmental issues at the BFC is important. *As far as we can tell from the information we have, resolution of remaining environmental issues at the BFC is not particularly sensitive to which option is chosen*.

4) *Options involving moving KCP to Albuquerque, NM are highly unrealistic.* Costs, risks, and delays would be much greater than other options. NNSA's business-case analysis of this option, which found this option *not* to be cost-effective, could only be constructed on the basis of assumptions so optimistic they were self-described as impractical and "problematic."

   We also believe there is considerable uncertainty as to the potential ultimate success of this option for geographic and cultural reasons.

   NNSA's Albuquerque options will be examined closely in a subsequent memorandum, now in preparation.

5) *We believe NNSA is incurring risks to its Life Extension Programs (LEPs)* by pursuing a private development path for a complex manufacturing facility under any circumstance, and especially now in an extremely uncertain financial and economic environment. *Some of these concerns have arisen only recently and have not been properly evaluated by NNSA.* Current and potential future economic and financial uncertainty affects several aspects of the KCRIMS proposal:

   a) The ability to finance and service approximately $500 million (M) in private debt;

   b) The future financial health and therefore management competence and reliability of the private developer, should financially stressful conditions arise;

c) The adequacy of local tax receipts to finance or otherwise support infrastructure required by the new facility.

6) *<u>In our opinion NNSA is underrating the management challenges of a three- or four-party management and ownership structure.</u>* Leaving out the GSA, NNSA is setting itself up to manage a situation in which it would inevitably own some (though not all) of the internal production equipment and infrastructure – which however functions integrally and in a complex way. The plant would actually be operated by a third party, the operating contractor. When problems arise, who is responsible?

   A fourth party, the Kansas City Planned Industrial Expansion Authority, would own the land and any environmental impacts to it for the duration of the initial lease.

   This is a much more complex management situation than a federal-private office lease – or the current situation at BFC. KCRIMS as currently configured would involve three "grey areas" of responsibility and potential misunderstanding: owner-operator, NNSA-owner, and NNSA-operator. The typical NNSA government-owned, contractor operated (GOCO) facility has just one of such "grey area," which has often proven difficult enough to manage.

   The proposed KCRIMS management structure is also more complicated than a contractor-owned, contractor-operated (COCO) facility in which the *<u>same</u>* DoD contractor both owns and operates the plant and delivers the products to DoD.

   Subcontractors add a layer of complexity in all these cases. Responsibility and accountability are further diffused.

   The complexity of KCRIMS management makes NNSA and its mission hostage to management failures by more parties than is the case at present. Failures may occur due to events in financial or economic markets over which no one involved has any control. *<u>KCRIMS as planned takes away federal management options and control just when they are most needed, without adding new compensatory features</u>*. KCRIMS exposes NNSA and its missions to unnecessary contingencies.

7) *<u>A new "KCRIMS" plan not involving new construction should be considered.</u>* NNSA has failed to explain its claim that moving to a new Botts Road facility would save $100 M per year in federal operating costs beyond that which could be saved by a) downsizing in place and/or b) prudently increasing outsourcing. While the KCRIMS plan has included new construction up to now, changing and inherently unpredictable circumstances, as well as the fundamental management considerations noted, warrant a reexamination of this assumption.

8) *<u>Downsizing in place was NNSA's plan until 2006</u>*. Such a plan would create minimum program disruption and management risk.

   From 1997 to 2006 NNSA invested some $174 M (over $200 M in present value), in recent line item construction at the BFC:

   a) Project 97-D-123, structural upgrades, completed in 2004;

   b) Project 99-D-127, restructuring initiative, completed in 2005; and

   c) Project 03-D-121, gas transfer capacity expansion, completed in 2006

   Other long-term capital investments at the BFC have been made during the last decade via other NNSA line items. These – especially and explicitly 99-D-127 – were investments in a downsizing-in-place alternative for KCP. What has changed?

9) *We believe the BFC fully meets NNSA's needs* today and we have not been able to find any reason why the BFC cannot serve NNSA's needs equally well for decades to come.

10) *The life-cycle savings offered by KCRIMS with the Botts Road facility, even assuming NNSA's optimistic analysis is correct, would be small*: just 17% over 20 years (net present value). Since KCP consumes 6% of NNSA Weapons Activities budget, the projected savings from KCRIMS is about 1% of NNSA's Weapons Activities expenses. We think these savings are optimistic. In any case they are not worth the significant risks identified here.

11) *We see no reason why GSA's tenancy and related decisions regarding the BFC should affect future NNSA costs*. GSA remains responsible, as far as we can tell, for its portion of the BFC.

12) *We urge NNSA to resume its suspended maintenance investments at the BFC* after what is now approximately a two-year hiatus. It is not clear that the KCRIMS proposal is financially or legally viable and upon information and belief NNSA is running unnecessary operational risks by deferring these investments.

13) *NNSA could save hundreds of millions of dollars by using ordinary line-item construction for any new facility, were one actually needed.* If it were truly necessary to build a new facility, and NNSA were to construct a new facility at Botts Road (or another comparable location) via a standard line-item construction project with federal ownership, we believe NNSA could save in the range of $320 M or $469 M (net present value over a 20 or 25 year lease, respectively), assuming full federal payment in lieu of taxes (PILT).

    These extra costs pay for private financing, private overhead, and profit. In effect NNSA is borrowing private funds to build a new factory in order to shift costs (greatly inflated by this action) to future years.

    Without PILT, savings to federal taxpayers due to line-item construction would be even more, roughly $397 M or $560[1] M (net present value over a 20 or 25 year lease, respectively). Of course in that event local jurisdictions would lose about $77 M or $91 M in property taxes over the lease period (in net present value, again).

    These figures assume a 3% cost of money and a one year construction delay beyond that assumed for KCRIMS that would cost an extra $100 M in up-front operating costs, which is NNSA's working assumption. As noted above, we question this.

14) *Given the fiscal, managerial, and legal questions surrounding the Botts Road site, we believe the most certain approach to retaining KCP's high-paying jobs in the Kansas City area would be to retain them via a downsized KCP at the BFC.*

[1] A previous edition of this memo said "$469 M" here, the same as the 20-year case, which was a transcription error.