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1) Welcome and Introduction

- a. Thank you for inviting me to speak today and offer my views on risk and the practical management of risks.
- b. Historically KBR has had some spectacular failures in Risk Management: the South Texas nuclear project cost KBR in excess of \$700 million while the Barracuda Caratinga FPSO development cost over \$800 million
- c. Since arriving at KBR in 2006 I have sought to improve our risk management processes to avoid repeating these sins of the past, particularly since we are now a public company without the deep pocket of our former parent.
- d. At KBR our aspiration is to achieve “Best in Class Risk Awareness”. Are we the best, I don’t know, that isn’t really the objective. But we’re focused on getting better in our processes each and every day.
- e. Risk management and the pursuit of improving risk management is a conscious mind set and a never ending, continuous process

2) Risk is Part of Business

- a. There is not such thing as a business with no risks
- b. Our business only exist because we take risks from our customers and manage these risks at lower cost and more efficiently than they can
- c. The success of our business will be driven by how well we manage those risks we undertake on behalf of our customers.

3) Risk Awareness: A high level overview

- a. At KBR we employ a 6 step risk awareness process

- b. The 6 steps are: Identify, Measure, Analyze, Price, Manage and Report
- c. Identification is to understand all the areas where risk exists in your project. The most important step in this 6-step process is simply the robust identification of risks.
- d. Measurement is to understand the financial or commercial dimensions of the risk inventory. All risks have both positive as well as negative impacts. Our objective here is to understand the range of expected outcomes of each risk in our risk inventory.
- e. Analysis is the step to understand the interplay between and among risks. This can be done both qualitatively as well as with sophisticated analytical tools. Analysis also entails developing strategies to mitigate, allocate to third parties, manage or price the range of risks.
- f. Pricing is to assess the returns that are needed to justify taking the risk. This is actually a fairly simple exercise once all known risks and their mitigation strategies are understood to those reviewing the project.
- g. Management is actually a fairly straightforward process if you do a good job on the first 4 steps. Here all risks have been identified, mitigation strategies developed and critical activities really focus on identifying those risks that arise after the contract has been signed.
- h. Reporting is where KBR creates a learning environment across the company in our Risk Awareness process. We want to know how our pricing and mitigation activities compared to expectations as well as what risks we might not have identified at the beginning of the Sales process. It is our desire to learn from our risks and where possible avoid paying our tuition a second time on any discrete risk.

4) Standardizing Risk Management Processes

- a. At KBR we try to design risk awareness / risk management into our two fundamental processes: Sales or Business Development and Project Execution.
- b. We have tried to drive a consistent or standardized framework for their review and discussion of risks.
- c. We have developed specific policies to be followed across both the Sales as well as the Project Execution processes.

- d. KBR's objective is to create a consistent framework across the entire company to assess risks based on KBR's 6 step Risk Awareness process.
- e. As part of this standardized Risk Awareness process we assess risks transversally across all aspects of a project; Operations, Legal, Financial and Commercial.

5) Operations Risk

- a. At KBR, Operations risk is the costing of the direct costs of project execution
- b. At these Operations Reviews, we assess the man-hour estimates, schedules, execution risks, commodity and procurement risks, performance risks, subcontractor risks, and the capabilities of our project teams to successfully manage the work but to name a few.
- c. We have established formal processes that must be followed to make sure we follow a consistent and standard process.
- d. We employ formal risk registers with ranges of expected outcomes and use statistical models to quantify the range of outcomes from these risks.
- e. On a monthly basis, we convene meetings to review our major projects, including our activities to manage or mitigate major risks.

6) Legal Risk

- a. We have established a series of standard terms and conditions that we seek to achieve for each project pursued by KBR.
- b. We recognized the likelihood of success in achieving our standardized terms and conditions is limited.
- c. We focus our discussions on variances to our standard terms and conditions, allowing KBR to have an "exceptions based" discussion on our legal terms and conditions.
- d. By focusing most of our efforts on understanding the exceptions to our standard terms and conditions, we believe we drive a greater creativity into our legal reviews toward addressing discrete project legal issues.

7) Financial Risk

- a. Review of the project financial risks is fairly straightforward and has the least variance across the range of KBR projects.

- b. Areas we focus most on are customer credit, project net cash flow, consumption of our credit capacity, and how the project impacts our income statement and balance sheet.

8) Commercial Risk

- a. Commercial risk is probably the newest area of emphasis for KBR.
- b. This is the area where we have historically seen the greatest adverse impact on our projects at KBR.
- c. From a Commercial risk standpoint, we look at a wide range of exposures including what contributions our Joint Venture partners are making to our projects, how project risks and rewards are shared, as well as is our business strategy rationale and consistent with the overall KBR strategy.

9) Quantifying the Risk

- a. Perhaps the most difficult and most intuitive aspect of any project is attempting to distill the myriad of risks into a single number.
- b. At KBR we try to examine the impact of the various risks undertaken against the expected project economics.
- c. We try to grade each project on a risk-adjusted basis against one of three ratings: Acceptable, Moderate and Unacceptable.
- d. We have taken this methodology and applied it against several historical projects and we have seen the actual results from these historical projects are generally assessed consistently in our methodology.

10) Creating a Balanced Risk Awareness Culture

- a. There is a tendency when one implements a risk awareness culture that the organization becomes risk averse. This behavior must be avoided at all times.
- b. A careful balance must be established between those whose job it is to bring risk into the company and those whose job it is to make sure we only acquire those risks we want to bring into the company.
- c. Personalities are an important consideration. You want managers who are aggressive and customer focused to drive the business. For the risk controller community you need to make sure that those in charge of evaluating risks are not your

dreamers and are very good at applying past mitigation strategies and current policies on our projects.

- d. Project reviews must be open, transparent and robust. An open dialog must be established at an early stage of a project so that these discussions might influence the development of the project.
- e. A risk acquisition appetite must be flexible to take into account market conditions, competitor strategies and the company situation.

11) Pursuing Best in Class Risk Awareness

- a. At the end of the day, it takes people, processes, systems and culture to effectively and profitably manages all the risks across your organization.
- b. Every organization needs good people who not only understand their areas of responsibility, but also the broader objectives of the organization.
- c. At KBR our processes are consistently used across each of our projects in either the Sales or Project Execution processes.
- d. We have developed and refined our systems to look at those areas of risk that need to be tracked throughout the projects lifecycle.
- e. At KBR I believe we have established and have been implementing for several years now a commitment to achieve “Best in Class Risk Awareness”. We consistently talk at all of our management meetings about our commitment to this objective and our teams see these steps I have described in my presentation.
- f. Above all we have kept our core initiatives limited and have been consistent in our messages. I am please with the results we have achieved across KBR through our efforts in Risk Awareness.

12) Closing Comments

- a. As I wrap up my comments, I would like to highlight the following:
- b. Risks are an essential element of any business. As business becomes more complex and inter-related between customers and their suppliers, an effective Risk Management process is essential to survival.

- c. Risk Awareness or Risk Management can take many forms. There is no right way of doing things. What is important is that organizations assess what they want to manage and how these processes associated with their risk management activities are knitted into their businesses.
- d. Risk Awareness functions best when there is a clear and consistent commitment across all levels of the organization. Managing risk takes place every day on every project. There are no holidays in the risk management arena.
- e. Today I have outlined a framework that appears to work well for KBR. We are pleased with our results to date and strive to continue to refine our processes towards improving our Risk Awareness activities.
- f. I hope my comments have proved useful to each of you in how you look at risks and their management.
- g. I would be happy to take any questions you may have regarding risks and their management.
- h. Thank you.