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FOCI Vetting Expands to Unclassified DoD Contracts

The Department of Defense is preparing to subject tens of thousands of contractors to foreign ownership, control, or influence (FOCI) scrutiny for the first time.

BY STEPHEN L. BACON

For decades, contractors handling classified work have been subject to foreign ownership, control, or influence (FOCI) reviews by the Department of Defense (DoD). Before granting access to classified information, DoD will scrutinize a company's ownership structure, foreign relationships, and corporate governance arrangements as part of the FOCI review process.

But the vast majority of defense contractors do not require security clearances and have avoided FOCI examination. To date, these companies have been able to pursue and perform unclassified DoD contracts without ever facing questions about their foreign connections. This is about to change.

Section 847 of the National Defense Authorization Act for Fiscal Year 2020 mandates a dramatic expansion of FOCI vetting to cover unclassified DoD contracts valued above \$5 million. This change will subject an estimated \$200 billion worth of acquisitions to pre-award FOCI reviews. As a result, the Defense Counterintelligence and Security Agency (DCSA) expects its annual caseload to skyrocket from roughly 2,000 matters to over 41,000. This would amount to a nearly 2000% increase in cases per year.

The learning curve for contractors and acquisition professionals that have never dealt with FOCI requirements will be steep. The FOCI review process for unclassified contracts will add a new and significant layer of complexity and potential delays to an already challenging procurement environment.

Contractors that fail to comply with FOCI disclosure and mitigation requirements may face a variety of adverse consequences including contract ineligibility or termination. As DoD prepares to implement Section 847, now is the time for contractors to understand what these new requirements will entail and how they will impact doing business with DoD.

Section 847 Requirements

Congress recognized that foreign adversaries do not need to access classified information to threaten national security. Unclassified contracts can provide valuable intelligence about defense capabilities, establish opportunities for future influence operations, or create vulnerabilities in critical systems.

To address these concerns, Section 847 requires “covered contractors and subcontractors” to disclose their beneficial ownership and whether they are under FOCI.¹ The statute

defines “covered contractors and subcontractors” to include “an existing or prospective contractor or subcontractor of the Department of Defense on a contract or subcontract with a value in excess of \$5,000,000.”²

Notably, Section 847 generally excludes contracts for commercial products or services.³ However, a commercial contract may be subject to FOCI review if a senior DoD official specifically determines that the contract “involves a risk or potential risk to national security or potential compromise because of sensitive data, systems, or processes.”⁴

The disclosure requirements under Section 847 mirror those long used for cleared contractors under the National Industrial Security Program Operating Manual (NISPOM), which is now codified at 32 C.F.R. Part 117. This requires disclosure of information about foreign shareholders, foreign board members, foreign debt arrangements, significant foreign contacts, and other indicators of potential foreign influence.

Section 847 requires DoD to consider FOCI risks as part of a contracting officer's pre-award responsibility determination. Moreover, consistent with the NISPOM, covered contractors and subcontractors have an obligation to update their disclosures when there are material changes to information previously reported.⁵

DCSA's Expanded Role

To implement Section 847, the Office of the Undersecretary of Defense for Intelligence and Security issued DoD Instruction 5205.87 on May 13, 2024. It designates DCSA as the lead agency for conducting FOCI assessments on all covered DoD contractors and subcontractors. This represents a massive expansion of DCSA's role, extending its oversight to an estimated 41,000 companies.

When reviewing uncleared contractors, DCSA will apply a modified version of its existing FOCI framework. Specifically, a

company will be deemed under FOCI if a foreign interest has the power to direct or decide matters in a way that could pose a risk to national security or potentially compromise sensitive data, systems, or processes, or could otherwise control or influence the business or management of the contractor in a manner that could adversely affect its ability to perform the contract or subcontract.

DoD components will be required to collect FOCI disclosure information from offerors during source selections and provide it to DCSA for analysis. DCSA will, in turn, provide recommendations to contracting officers about whether the contractor poses unacceptable risks and what mitigation measures may be required.

DCSA will have 25 working days to complete its assessment and provide a FOCI risk report and mitigation strategy. This timeline is designed to prevent FOCI reviews from creating undue delays in the procurement process, but it represents an ambitious goal given the expected surge in DCSA's caseload.

DCSA may use interim mitigation measures, such as commitment letters, to avoid delaying contract awards while more comprehensive mitigation measures are negotiated and finalized. DCSA is expected to execute final FOCI mitigation measures within 90 working days of award.

For contractors that have mitigation measures in place, DCSA will conduct annual reviews to determine if there are any changes to their FOCI status. DCSA will also complete new case reviews for any contractors that report changes to their beneficial ownership.

The Forthcoming DFARS Rule

While DCSA is preparing to expand its workload, formal implementation of the new regime will occur through a new *Defense Federal Acquisition Regulation Supplement (DFARS)* rule currently under development.

Contractors should expect the rule to include several key elements:

- **Solicitation Requirements.** Offerors will be required to disclose FOCI matters as part of their proposals, likely through a form similar to SF-328 or a new solicitation provision.
- **Contract Clauses.** The rule will include standard contract clauses obligating contractors to report changes in ownership or control during performance and enabling the government to address emerging FOCI risks.
- **Mitigation Procedures.** The rule will formalize the process for assessing and implementing FOCI mitigation measures prior to contract award.
- **Enforcement Mechanisms.** Contractors who cannot

satisfactorily mitigate FOCI concerns will be ineligible for award, and existing contracts may be terminated if mitigation proves inadequate.

The *DFARS* rule was originally scheduled for completion in 2021, but implementation has been substantially delayed. Current projections suggest the rule could be finalized as early as 2026, though this timeline could shift further.

It is possible that the ongoing efforts to overhaul the *FAR* and agency supplements may impact Section 847's implementation timeline. However, because the expanded FOCI requirements are based in statute, contractors should expect that the new *DFARS* rule will go forward unless there is a change in law.

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How Contractors Can Prepare

As defense contractors await the roll out of the new *DFARS*, they should take proactive steps to prepare so they are in the best position to comply with the new requirements. These steps should include:

■ **Map Ownership and Control.**

Companies should review their ownership structures now to identify any direct and indirect beneficial owners. This includes mapping complex ownership chains and identifying any foreign connections that might trigger DCSA scrutiny. Companies must also be prepared to document equity percentages, voting rights, negative control provisions, and veto rights, as well as any foreign lenders, creditors, or contractual rights that could create foreign leverage.

■ **Develop Disclosure Capabilities.**

Contractors need systems to gather and present ownership and control information quickly and accurately to avoid impacts to proposals. This information may include, for example, ownership charts, governing agreements, and debt obligations. Documentation should be readily available for disclosure during the proposal phase, and whenever changes occur that must be reported.

■ **Plan for Mitigation.** Companies with potential FOCI issues should consider mitigation measures and evaluate which options might be feasible for their business model and acceptable to DCSA. Early planning can facilitate a smoother review process with DCSA that avoids contract delays.

■ **Build Compliance Infrastructure.**

Section 847 creates ongoing compliance obligations that require dedicated attention and resources. Companies should assign responsibility for FOCI compliance and integrate these requirements into their existing compliance programs. Those persons responsible for compliance should be aware of any changes to ownership or corporate governance that may impact the company's FOCI status.

Key Areas to Watch

There are a number of issues that are likely to emerge as implementation of Section 847 ramps up over the next year.

■ **DCSA Capacity and Performance.**

DCSA is currently recruiting and training civilian and contractor personnel to assist with implementation. However, the 20-fold increase in DCSA's caseload represents an unprecedented challenge. It remains to be seen whether DCSA can meet its 25-working day timeline for conducting FOCI reviews.

■ **Mitigation Standards.** DCSA's approach to FOCI mitigation for unclassified contracts remains largely undefined. Mitigation measures for unclassified contracts may be less stringent than those adopted for classified contracts, but this will likely not be known until standards emerge through practice. Contractors should expect DCSA to use familiar mitigation tools including, for example, board resolutions, commitment letters, appointment of independent directors with no foreign ties, Security Control Agreements (SCAs) that limit a foreign owner's control, proxy arrangements, and Technology



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■ **Commercial Contract Application.**

The specific circumstances in which DoD will require FOCI review for commercial contracts is unknown and also likely to develop through practice. It is possible that the forthcoming DFARS rule or other DoD guidance will explain the factors DoD should use to determine whether a commercial contract should be subject to the FOCI review requirement.

■ **Competitive Implications.**

Section 847 may advantage domestically-owned contractors over those with foreign connections. The extent of this impact will depend on how burdensome and costly mitigation requirements prove to be and

how effectively DoD manages the review process.

Conclusion

Section 847 represents a fundamental shift in defense contracting, extending rigorous security oversight to a vast segment of the defense industrial base that previously operated with minimal scrutiny. Although significant implementation questions remain, it is clear that contractors that want to perform significant DoD work must be prepared to address foreign influence concerns.

The companies that prepare early and approach FOCI compliance proactively will be best positioned to compete successfully in this new environment. Those companies that ignore these changes risk finding themselves locked out of lucrative defense opportunities when the new rules take effect. **CM**

Stephen L. Bacon is a shareholder in the Washington, D.C. office of the law firm Rogers Joseph O'Donnell, where he represents government contractors in bid protests, claims, terminations, investigations, and suspension and debarment proceedings. He frequently litigates cases at the Court of Federal Claims, the Government Accountability Office, the Boards of Contract Appeals, and the Small Business Administration's Office of Hearings and Appeals. He also provides advice and counsel to clients on a broad range of contractual and regulatory compliance issues that confront government contractors.

The views expressed in this article are those of the author and do not necessarily reflect the views of Rogers Joseph O'Donnell or its clients. This article is for general information purposes and is not intended to be and should not be construed as legal advice.

ENDNOTES

- 1 National Defense Authorization Act for Fiscal Year 2020, Pub. L. No. 116-92 (Dec. 20, 2019), § 847(b)(2)(A)(i).
- 2 Id. § 847(a)(3).
- 3 Id. § 847(c)(1).
- 4 Id.
- 5 Id. § 847(b)(2)(A)(ii).

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