

Federal Contracting: Timely Actions Needed to Address Risks Posed by Consultants Working for China

GAO-24-106932

Q&A Report to Congressional Requesters

September 19, 2024

Why This Matters

From fiscal years 2019 through 2023, federal agencies obligated more than \$500 billion on contracts associated with a broad range of consulting services. The Departments of Defense (DOD) and Homeland Security (DHS) accounted for over 50 percent of those obligations and have national security focused missions. Certain types of consulting services support important national security issues, such as energy or technology research, defense analyses, and intelligence.

The U.S. National Security Strategy identifies China as the U.S.'s only competitor with both the intent and power to reshape the international order, with ambitions to expand its sphere of influence and become the world's leading power. Members of Congress have expressed concerns that companies that consult for both for the U.S. government and a foreign government—particularly potential U.S. adversaries—could present conflicts of interest that put U.S. national security interests at risk. The Federal Acquisition Regulation (FAR) defines an organizational conflict of interest (OCI) generally to include a situation where an entity, such as a contractor, may be unable to provide impartial assistance or advice as a result of its relationships or activities with another entity. As discussed below, recently enacted legislation references a contractor's relationship with a foreign entity as a possible cause of an OCI.

You asked us to assess the national security risks posed when contractors consult for both the U.S. and Chinese governments, including the types of information federal agencies have on whether contractors work for the Chinese government or its proxies and affiliates. Proxies or affiliates can include Chinese state-owned enterprises and other entities connected to the People's Republic of China and the Chinese Communist Party. You also asked us to assess how agencies assess, mitigate, and report on OCI involving foreign influence.

This report describes existing and pending regulations and policies most relevant to these issues. It also discusses steps that DOD and DHS take to collect information, assess, and mitigate such national security risks when awarding contracts.

Key Takeaways

- Current acquisition regulations do not specifically direct agencies to consider if contractors consulting for the U.S. government also have consulting contracts with China. Therefore, acquisition personnel do not typically collect information on, assess, or mitigate potential national security risks posed by these consultants when awarding contracts.
- DOD has a process for granting clearances to contractor facilities that involves consideration of contractors' business relationships with foreign

governments. However, this process typically happens after contracts are awarded and is limited to contracts that involve classified materials.

- Recently enacted legislation is driving multiple efforts to update acquisition regulations and policies to address these potential risks before awarding contracts, including those that do not involve classified materials. These efforts are largely ongoing. How these efforts, when implemented, will specifically address this topic is not yet clear.
- We recommend that the Secretary of Defense take steps to ensure prompt updates are made to the Defense Federal Acquisition Regulation Supplement (DFARS), in response to legislation on (1) how acquisition personnel use information on foreign ownership, control, or influence when awarding or modifying contracts; and (2) new requirements for contracts involving certain types of consulting services. Additionally, we recommend the Director of the Office of Management and Budget ensures prompt updates are made to the FAR that are responsive to recent legislation.

What are consulting services?

The FAR, which establishes uniform policies and procedures for acquisition by all executive agencies, does not expressly define consulting services. Recent legislation on prevention of conflicts of interest related to consulting services generally defines the term using the FAR's definition for advisory and assistance services.¹ That definition includes services such as providing advice, analyses, evaluations, and recommendations to improve government operations.²

For this report, we examined services associated with certain product and service codes in federal acquisition data. These data show that agencies procure these services from thousands of contractors each year. We found that many contractors providing these services to federal agencies are not captured in federal contracting data as consulting firms.

What are some key regulations and policies related to this topic?

Current acquisition regulations and security policies contain some requirements related to OCI and addressing risks related to foreign ownership, control, or influence (FOCI).

- **OCI.** FAR part 2.101 defines "organizational conflict of interest" as situations where, based on activities or relationships with others, a person is unable or potentially unable to render impartial assistance or advice to the government.³ The definition also includes instances where the person's objectivity in performing the contract work is or might be impaired, or if a person has an unfair competitive advantage.⁴
- **FOCI.** The National Industrial Security Program Operating Manual describes FOCI as arising when a foreign interest has the power to direct or decide issues affecting a contractor's management or operations in a way that could either (1) result in unauthorized access to classified information; or (2) adversely affect the performance of classified contracts or agreements.⁵

Existing OCI and FOCI requirements and procedures do not specifically address if, or how, acquisition personnel should consider consultants' contracting activity with China or other foreign governments prior to awarding contracts.

DOD and DHS acquisition officials told us that some sections of the FAR and its departmental supplements could potentially be used to consider OCI or FOCI risks when awarding contracts to consultants that also work for the Chinese government.⁶ However, they clarified that they were not aware of any instances where their departments applied those sections for that purpose, and they expressed concerns about attempting to do so without more guidance in

acquisition regulations. These acquisition officials also could not identify any acquisition policies that specifically require contracting personnel to collect and consider information related to potential risks from consultants' contracting activity with China when awarding contracts.

Do acquisition officials currently address these types of risks when awarding consulting contracts?

Generally, no. DOD and DHS officials noted that that current regulations and policies do not specifically direct acquisition personnel to collect information, assess, or mitigate these types of national security risks when awarding most contracts for consulting services.⁷ These officials acknowledged, however, that the need to identify and assess this type of risk is a valid concern that should be addressed in some way. Those officials also told us that intelligence officials in their departments may examine some of these areas, but findings are not typically shared with acquisition personnel. They also told us they were not sure what information sources they could use to help them identify contractors that have contracts with the Chinese government or its proxies and affiliates.⁸

Do DOD or DHS address these risks in other ways?

They do so indirectly, and to a limited extent. The Defense Counterintelligence and Security Agency (DCSA) collects information on foreign relationships, assesses risks, and identifies steps to mitigate these risks for many federal agencies.⁹ DCSA officials consider this information when investigating contractors with an existing government contract that need a facility that is cleared to handle classified materials to perform their responsibilities. For that subset of contracts, DCSA takes the following steps:

- **Collect information.** Contractors must provide DCSA with a completed questionnaire and supporting documentation to obtain a security clearance for their facility. That questionnaire asks contractors to identify contracts with foreign governments or entities. However, it does not currently include explicit distinctions about state-owned enterprises or affiliates. DOD officials told us they are working to formally update that questionnaire to, among other things, include more specific instructions about how to respond to the questionnaire.
- **Assess risks.** DCSA analyzes contractors' questionnaire responses and supporting documentation to assess FOCI risks, among other things. DCSA officials told us they also use internal information, both classified and unclassified, as well as commercial data and open-source data, to validate or refute contractors' submitted information. DCSA documents and analyzes these risks in risk assessment reports that are used primarily by DCSA officials to document whether a contractor is eligible for a facility clearance.
- **Mitigate risks.** DCSA officials told us they develop mitigation strategies to address FOCI risks and oversee implementation of these strategies when providing facility clearances.

DCSA conducts these investigations for many federal agencies, including DOD and DHS. We reviewed a nongeneralizable sample of 12 risk assessments that DCSA produced during these investigations and found the assessments generally identified issues and risk mitigation needs or other steps for further assessment.

However, because DCSA's investigations and reports have a broader purpose, there are some limitations to using them in relation to assessing national security risks posed when contractors consult for both the U.S. and Chinese governments. Specifically:

- DCSA's investigations generally occur after agencies award contracts.

- Because of their purpose, these investigations are specific to classified requirements. Therefore, these investigations would not be conducted on contracts, such as consulting contracts, that do not involve classified material.

What laws have been enacted to help address these risks when awarding contracts for consulting services?

Several recently enacted laws include provisions related to risks involving contracting and foreign entities. These laws could help address such risks when agencies award contracts for consulting services. See table 1 for some key examples.

Table 1: GAO Reviewed Recently Enacted Laws Related to Addressing Risks Involving Contracting and Foreign Entities

Laws	New requirements
NDAAs for Fiscal Year 2020 § 847: Mitigating Risks Related to Foreign Ownership, Control, or Influence of DOD Contractors or Subcontractors ^a	Requires the Department of Defense (DOD) to improve its process and procedures for performing foreign ownership, control, or influence risk assessments for defense contracts and subcontracts valued above \$5 million, generally excluding awards for commercial products and services. A provision in a subsequent NDAAs required DOD to revise the Defense Federal Acquisition Regulation Supplement (DFARS) and internal guidance to implement these requirements by July 1, 2021. ^b
NDAAs for Fiscal Year 2022 § 855: Employment Transparency Regarding Individuals Who Perform Work in the People's Republic of China ^c	Directs DOD to generally require contractors to disclose whether they employ individuals who will work in China on contracts valued over \$5 million, excluding awards for commercial products and services.
Small Business Innovation Research (SBIR) and Small Business Technology Transfer (STTR) Extension Act of 2022 ^d	Requires participating agencies, including the Department of Homeland Security and DOD, to implement a risk-based approach, as appropriate, for assessing specific aspects of small businesses seeking SBIR/STTR awards, including foreign ownership, by June 27, 2023.
Preventing Organizational Conflicts of Interest in Federal Acquisition Act ^e	Requires the Federal Acquisition Regulation to be updated with definitions, guidance, and illustrative examples related to contractor relationships with, among other things, foreign entities that may cause potential organizational conflicts of interest involving undue influence within 18 months of enactment, which was by June 27, 2024.
NDAAs for Fiscal Year 2024 § 812: Preventing Conflicts of Interest for Entities that Provide Certain Consulting Services to DOD ^f	Directs DOD to revise the DFARS to prohibit DOD from contracting for consulting services—as defined in the provision—with vendors that provide consulting services to certain foreign entities, including China. This prohibition would not apply if the vendor maintains an auditable conflict of interest mitigation plan or a waiver is issued. This provision directs DOD to update the DFARS with these requirements by June 19, 2024.

Source: GAO analysis of National Defense Authorization Acts (NDAAs) for Fiscal Years 2020-2024 and Public Laws 117-324 and 117-183. | GAO-24-106932

Notes:

^aJohn S. McCain National Defense Authorization Act for Fiscal Year 2020, Pub. L. No. 116-92, § 847 (2019) (codified as amended at 10 U.S.C. § 4819 note).

^bPub. L. No. 116-283, § 819 (c)(2) (2021) (codified at 10 U.S.C. § 4819 note).

^cPub. L. No. 117-81, § 855 (2021) (codified at 10 U.S.C. § 4651 note prec.).

^dPub. L. No. 117-183, § 4(b) (2022) (codified at 15 U.S.C. § 638(vv) and § 638 note).

^ePub. L. No. 117-324 (2022) (codified at 41 U.S.C. § 2303 note).

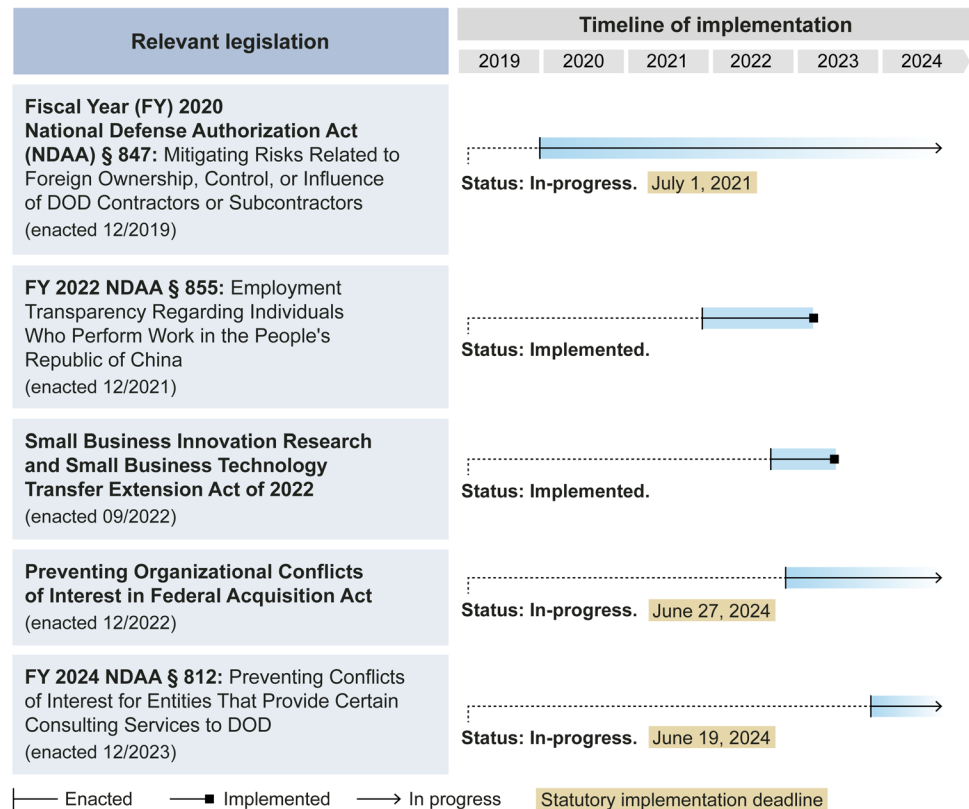
^fPub. L. No. 118-31, § 812 (2023) (codified at 10 U.S.C. § 4501 note prec.).

We discuss the implementation status of these requirements below.

To what extent have these laws been implemented?

As of July 1, 2024, two of the five laws had been implemented and three had not been, even though statutory deadlines passed (see fig. 1).

Figure 1: Timeline of Recently Enacted Laws Related to Risks Involving Contracting and Foreign Entities as of July 1, 2024



Source: GAO analysis of federal rulemaking documentation and Department of Defense (DOD) information. | GAO-24-106932

As of July 2024, DOD had not fully implemented one law nearly 3 years after its statutory deadline for implementation, and the Office of Management and Budget’s Office of Federal Procurement Policy (OFPP) and DOD recently missed statutory deadlines for implementing two other laws. In general, for the laws that remain unimplemented, the Defense Acquisition Regulation (DAR) Council—which is responsible for coordinating revisions to the DFARS and coordinating with the Civilian Agency Acquisition Council to update the FAR—has begun the legally required processes for rulemaking.¹⁰ However, it has not completed all of the required steps.

- National Defense Authorization Act (NDAA) for Fiscal Year 2021 § 847.** The NDAA for Fiscal Year 2021 included a provision that directed DOD to revise relevant directives, guidance, training, and policies, including the DFARS, to fully implement the requirements of section 847 no later than July 1, 2021.¹¹ However, nearly 3 years after that deadline, DOD officials reported that the DAR Council is still in the earliest stages of rulemaking for implementing this law.

DOD officials told us they needed to implement a departmental instruction before updating the DFARS. The Office of the Under Secretary of Defense for Intelligence and Security issued this instruction in May 2024. According to that instruction, DCSA will conduct FOCI risk reviews for DOD contract awards valued over \$5 million, generally excluding those for commercial goods or services.¹² Specifically, DCSA will review FOCI risk for companies being considered for these awards and share its findings with contracting

officers to inform award decisions. DCSA's findings are to include, as necessary, a risk assessment and proposed risk mitigation strategy.

The May 2024 instruction directs the Office of the Under Secretary of Defense for Acquisition and Sustainment to establish policy on how acquisition personnel are to award, modify, or terminate contracts when DCSA confirms that a company is under FOCI and poses a risk to national security.¹³ DOD officials told us they believe the planned update to the DFARS (pursuant to the statutory provision) and associated procedures, guidance, and instruction will provide this direction. Acquisition personnel at the military departments told us that they would need such guidance to address risks involving foreign influence when awarding contracts. However, DOD officials told us the Office of the Under Secretary of Defense for Acquisition and Sustainment has not established timelines or milestones for updating the DFARS to finish implementing the law.¹⁴

- **Preventing Organizational Conflicts of Interest in Federal Acquisition Act.** The FAR Council—chaired by the Administrator of OFPP within the Office of Management and Budget, and responsible for updates to the FAR—did not meet the statutory deadline to update the FAR by June 27, 2024.¹⁵ As of July 2024, more than 18 months after the law was enacted, the FAR Council, which is working to implement this law through its rulemaking process, had not published a proposed rule for public comment. Guidance for processing FAR rules says that the standard time for publishing a final FAR rule is 16 months.

OFPP staff told us the milestones for processing FAR rules do not address the more complex rulemaking required by the law. They further advised that they have worked closely with the FAR Council to establish a publication date for a proposed rule, which is a key step in the rulemaking process. However, OFPP staff did not provide any additional information on the date, and have not identified any milestones or time frames for issuing the final rule needed to implement this law. Members of the team working to develop a proposed rule for this FAR update told us that this particular case is complex and has required more time than normal to address. We have similarly reported that complex regulatory changes can take multiple years to complete.¹⁶

- **NDAA for Fiscal Year 2024 § 812.** This provision directs DOD to update the DFARS with new requirements for contracts involving a specific set of consulting services by June 19, 2024.¹⁷ As of July 1, 2024, this provision had not been implemented. The DAR Council is currently working to implement this provision through its rulemaking process by issuing an interim rule. Guidance for updating the FAR shows that final rules are published in the Federal Register following a public comment period and other key reviews. Unlike a proposed rule, which does not go into effect until after a period for public comment, an interim rule goes into effect as soon as it is published in the Federal Register. Interim rules are used when urgent and compelling circumstances make solicitation of public comments impracticable prior to the effective date of coverage.¹⁸ DOD officials reported that a regulatory control officer had identified issues with the interim rule developed by the DAR Council, delaying its publication. Acquisition personnel at the military departments told us they need more guidance to address risks involving foreign influence when awarding contracts. As with NDAA for Fiscal Year 2020 § 847, DOD officials told us that the Office of the Under Secretary of Defense for Acquisition has not established timelines or milestones for updating the DFARS to finish implementing this law.

Standards for Internal Control in the Federal Government state that management should establish performance measures such as milestones for its defined objectives.¹⁹ Establishing milestones for updating the DFARS and the FAR can help to ensure that these efforts are kept on pace to be completed. In the meantime, acquisition officials will continue to lack knowledge or guidance about how to identify and address risks involving foreign influence when procuring consulting services.

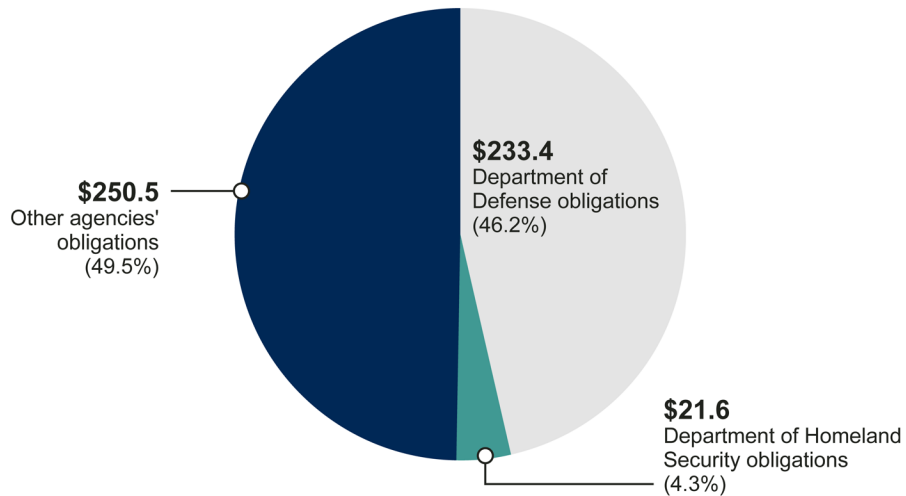
What proportion of consulting services might these laws apply to?

The degree to which contracts associated with consulting services will be covered by recent laws—or the value of obligations for such contracts—cannot be fully assessed until each law has been fully implemented. However, there are certain elements of the laws—for example, a general applicability to contracts above certain dollar values—that allow us to present relevant historical data on contract obligations from the Federal Procurement Data System (FPDS). To present this data, we identified spending on contracts associated with consulting services, which we defined as obligations for contracts for which agencies selected certain FPDS Product and Service codes.²⁰

We determined that federal agencies obligated more than \$505 billion on contracts associated with consulting services during fiscal years 2019 through 2023. For example, obligations on contracts for advisory services related to energy or technology research, defense analyses, and intelligence are included in this total. Figure 2 shows DOD and DHS’s share of obligations for these contracts.

Figure 2: Obligations on Contracts Associated with Consulting Services, Fiscal Years 2019-2023

Dollars (billions) in obligations on contracts associated with consulting services during fiscal years 2019-2023



Source: GAO analysis of Federal Procurement Data System data. | GAO-24-106932

Note: Obligations represented are associated with contracts for which the Department of Defense and other federal agencies assigned Federal Procurement Data System Product and Service codes that GAO determined generally encompass consulting services.

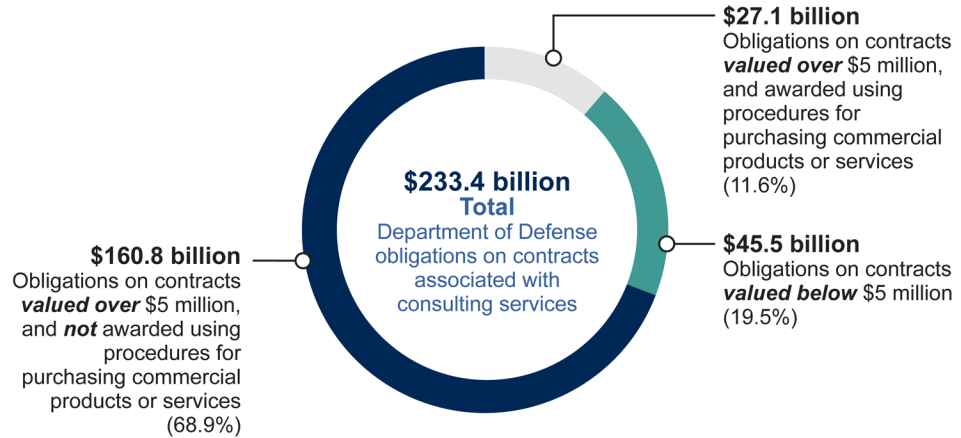
Our analysis of FPDS data found that the recently enacted laws are likely to vary widely in terms of the types of contracts and proportion of agencies’ contracting activities that may be covered when these laws are implemented.

- **NDA for Fiscal Year 2020 § 847 and NDA for Fiscal Year 2022 § 855.** These two laws call for changes that apply to DOD contracts and subcontracts valued over \$5 million and include exceptions, in part for commercial products and services. We found that during fiscal years 2019

through 2023, DOD obligated over \$160.8 billion on contracts that were not awarded using procedures for purchasing commercial products and services that were identified as consulting services.²¹ Figure 3 shows the share of DOD’s obligations on contracts we determined fit these parameters.

Figure 3: DOD Obligations on Contracts Associated with Consulting Services, Fiscal Years 2019-2023

Dollars (billions) in obligations on contracts associated with consulting services during fiscal years 2019-2023



Source: GAO analysis of Federal Procurement Data System data. | GAO-24-106932

Note: Obligations represented are associated with contracts for which the Department of Defense (DOD) assigned Federal Procurement Data System Product and Service codes that GAO determined generally encompass consulting services.

- Small Business Innovation Research (SBIR) and Small Business Technology Transfer (STTR) Extension Act of 2022.** The SBIR/STTR programs enable small businesses to provide research and development support for federal agencies.²² We analyzed FPDS data that show agencies obligated just over \$1 billion for contracts associated with consulting services that were also coded as SBIR/STTR awards in fiscal years 2019 through 2023. Those obligations represent less than 1 percent of federal spending on contracts associated with consulting services that we analyzed.
- Preventing Organizational Conflicts of Interest in Federal Contracting Act.** The proportion of obligations on contracts covered by this law will depend on the specifics of its implementation. This law does not include dollar value thresholds or address applicability to commercial services. Further, the applicability of the FAR’s general rules and procedures for identifying, evaluating, and resolving OCIs are not limited to any particular kind of acquisition.²³ Therefore, implementation decisions related to dollar value thresholds and applicability to commercial services could greatly vary the scope of the impact of this provision. The law requires revisions to the FAR’s definitions, examples, provisions, and clauses for OCI, among other things. As potentially related to risks involving consultants contracting for both the U.S. and Chinese governments, the law requires revisions to the FAR’s definitions, guidance, and examples related to contractor relationships with, among others, foreign entities that may cause potential organizational conflicts of interest, including undue influence.²⁴
- NDAA for Fiscal Year 2024 § 812.** This law applies to a specific set of consulting services only. The law calls for a revision to the DFARS that will apply to entities that provide consulting services—as specifically defined in the law—and that are assigned a North American Industry Classification

System (NAICS) code beginning with prefix 5416, which includes management, scientific, and technical consulting services.²⁵ The NAICS Manual states that these entities provide advice and assistance to businesses and other organizations on management, environmental, scientific, and technical issues, among other services.²⁶ Federal procurement data show that DOD obligated \$233.4 billion on contracts associated with consulting services in fiscal years 2019 through 2023. Of that total, \$21.3 billion of the obligations were on contracts with entities assigned a NAICS code beginning with this prefix, representing less than 10 percent of the total FPDS obligations that we analyzed.

What are the primary results from recently implemented laws?

As previously shown in figure 1, as of July 1, 2024, only two of the relevant laws have been implemented. However, DOD and DHS officials stated that they are not aware of any risks involving foreign influence that have been identified based on the application of the policy and regulations that implemented these two laws.

- **SBIR and STTR Extension Act.** As part of their due diligence programs that were implemented last year, DOD and DHS now require small businesses to complete a disclosure of foreign affiliations and relationships when seeking SBIR/STTR awards. As of June 2024, DOD and DHS officials we met with told us that they have not identified any risks related to foreign influence as a result of new risk-based approaches for identifying security risks before awarding SBIR/STTR contracts.²⁷ The processes in place are to help ensure the agencies continue their efforts to identify such risks. We are also conducting a separate review of agencies' efforts to identify foreign influence in accordance with this law.
- **NDAA for Fiscal Year 2022 § 855.** DOD implemented the law by revising the DFARS to include a new solicitation provision and contract clause for contractor disclosures on whether they employ individuals who will work in China on contracts valued over \$5 million, excluding awards for commercial products and services.²⁸ This provision requires DOD to semiannually brief congressional committees on contractor disclosures of employees working in China on contracts valued over \$5 million (excluding contracts for commercial products and services).²⁹ DOD's reports to the committees state that DOD has not received any disclosures since the law was implemented. Should a contracting officer have concerns with a contractor or prospective contractor's response to the provision or clause, the contracting officer could take various actions pursuant to their responsibility for ensuring compliance with the terms of a contract and safeguarding the interests of the United States in its contractual relationships.³⁰

DOD officials told us they do not expect many disclosures in the future because section 855 generally excludes commercial services and the number of noncommercial service contracts valued over \$5 million is relatively small. We reviewed FPDS data for DOD contract awards associated with consulting services made during fiscal years 2019 through 2023, valued over \$5 million, and for which DOD indicated it did not use procedures for the purchase of commercial products or services. Our review of these data revealed that less than 15 percent of those awards matched these parameters.

Conclusions

China is America's top adversary, and foreign influence remains a key risk for the country's national security. DOD and DHS officials lack specific guidance on how acquisition personnel should collect information, assess, or mitigate potential national security risks when awarding contracts for consulting services. Yet, in three instances (section 847 of the 2020 NDAA, the Preventing Organizational Conflicts of Interest in Federal Acquisitions Act, and section 812 of the 2024 NDAA), laws to address such risks have yet to see fruition, as the statutory deadlines to implement them have been missed. Without DOD and the Office of Management and Budget's Office of Federal Procurement Policy establishing milestones for completing the necessary and legally required steps to ensure these laws are implemented as expeditiously as possible, acquisition officials will continue to lack the knowledge that could help protect U.S. national security when awarding contracts to consultants.

Recommendations for Executive Action

The Secretary of Defense should direct the Office of the Under Secretary of Defense for Acquisition and Sustainment to take steps—including establishing milestones—to ensure the DAR Council develops DFARS updates responsive to NDAA for Fiscal Year 2020 Section 847, in a timely manner while also following applicable legal rulemaking procedures. (Recommendation 1)

The Director of the Office of Management and Budget should ensure that the Administrator of the Office of Federal Procurement Policy takes steps—including establishing milestones—to ensure the FAR Council finalizes FAR updates responsive to the Preventing Organizational Conflicts of Interest in Federal Acquisitions Act, in a timely manner while also following applicable legal rulemaking procedures. (Recommendation 2)

The Secretary of Defense should direct the Office of the Under Secretary of Defense for Acquisition and Sustainment to take steps—including establishing milestones—to ensure the DAR Council develops DFARS updates responsive to NDAA for Fiscal Year 2024 Section 812, in a timely manner while also following applicable legal rulemaking procedures. (Recommendation 3)

Agency Comments

We provided a draft of this report to DOD, DHS, and OMB for review and comment. DOD provided written comments, which are reproduced in appendix I. DOD concurred with the recommendations made to it. In an e-mail, OMB concurred with the recommendation directed to it. DOD, OMB and DHS also provided technical comments, which we incorporated into the report as appropriate.

Appendix I: Comments from the Department of Defense



ACQUISITION
AND SUSTAINMENT

OFFICE OF THE UNDER SECRETARY OF DEFENSE
3000 DEFENSE PENTAGON
WASHINGTON, DC 20301-3000

Mr. William Russell
Director
Contracting and National Security Acquisitions
U.S. Government Accountability Office
441 G Street, NW
Washington DC 20548

Dear Mr. Russell:

This is the Department of Defense response to Government Accountability Office (GAO) Draft Report GAO-24-106932, "FEDERAL CONTRACTING: Timely Actions Needed to Address Risks Posed by Consultants Working for China," dated July 19, 2024 (GAO Code 106932). Detailed responses to the draft report recommendations are enclosed.

Sincerely,

TENAGLIA.JOHN. Digitally signed by
M.1154945926 TENAGLIA.JOHN.M.1154945926
Date: 2024.08.27 18:43:54 -04'00'

John M. Tenaglia
Principal Director,
Defense Pricing, Contracting, and
Acquisition Policy

Enclosure:
As stated

**GAO DRAFT REPORT DATED JULY 19, 2024
GAO-24-106932 (GAO CODE 106932)**

**“FEDERAL CONTRACTING: TIMELY ACTIONS NEEDED TO ADDRESS RISKS
POSED BY CONSULTANTS WORKING FOR CHINA”**

**DEPARTMENT OF DEFENSE COMMENTS
TO THE GAO RECOMMENDATION**

Recommendation 1: The Secretary of Defense should direct the Office of the Under Secretary of Defense for Acquisition and Sustainment to take steps—including establishing milestones—to ensure the Defense Acquisition Regulations System (DAR) Council develops Defense Federal Acquisition Regulation Supplement (DFARS) updates responsive to FY 2020 National Defense Authorization Act (NDAA) Section 847, in a timely manner while also following applicable legal rulemaking procedures.

Response: Concur. As indicated on page 5 of this draft report, the implementation of Section 847 required the publication of a Department of Defense Instruction (DoDI) in advance of public rulemaking. Effective May 13, 2024, DoDI 5205.87 Mitigating Risks Related to Foreign Ownership, Control, or Influence for Covered DoD Contractors and Subcontractors was published and the DAR Council is now proceeding with title 48 rulemaking to amend the DFARS.

Recommendation 3: The Secretary of Defense should direct the Office of the Under Secretary of Defense for Acquisition and Sustainment to take steps—including establishing milestones—to ensure the DAR Council develops DFARS updates responsive to FY 2024 NDAA Section 812, in a timely manner while also following applicable legal rulemaking procedures.

Response: Concur. The Department is advancing a DFARS rule that will implement Section 812 to expressly require a certification from offerors and contractors.

How GAO Did This Study

To select agencies to include in our review, we analyzed FPDS data to identify federal spending on contracts with Product and Service codes that generally encompass consulting services by agency. Specifically, we assessed data on contract actions from fiscal years 2019 through 2023—the most recent 5 fiscal years for which there were complete data—that had FPDS Product and Service Codes that include analyses, studies, and professional, administrative, and management support services. We selected DOD and DHS because they were among the top five federal agencies with the highest total obligations for contracts having these codes during fiscal years 2019-2023, and because of their national security-related missions. The other three agencies within the top five were the Department of Health and Human Services, General Services Administration, and U.S. Agency for International Development.

We also analyzed the data to examine the percentage of spending related to key parameters, including awards coded as involving—or not involving—the use of procedures for the purchase of commercial products and services and spending on contracts valued over \$5 million. We supplemented our FPDS data analysis by using the Small Business Administration’s dataset for SBIR/STTR spending to identify additional contract obligations that were not coded as SBIR/STTR awards in FPDS.

To assess the reliability of the data we used, we reviewed FPDS manuals and quality assurance processes, internally reviewed data for accuracy, and reviewed our methodology with knowledgeable DOD and DHS officials. We also used SBIR data that were similarly assessed for data reliability by our analysts. Based on these steps, we found the FPDS and Small Business Administration data reliable for the purpose of reporting on consulting services obligations.

To describe the regulations and policies most relevant for federal agencies’ collection of information for contractors consulting for the U.S. and Chinese governments, we reviewed existing and proposed acquisition regulations and DOD and DHS policies related to OCI and FOCI risks. We also reviewed NDAAAs for fiscal years 2015-2024 and their provisions related to OCI and FOCI. We then identified DOD, DHS, and OFPP actions to address these provisions. We interviewed DOD and DHS acquisition officials about the applicability of existing regulations, particularly the FAR and its supplements, for identifying OCIs involving foreign influence and FOCI risks.

To describe the steps that DOD and DHS take to collect information about contractors that consult for the Chinese government and the agencies’ assessments of national security risks when awarding contracts to such contractors, we reviewed agency regulations, policies, and procedures for assessing OCI and FOCI risks. We also reviewed a nongeneralizable sample of 12 DCSA risk assessments from fiscal years 2020-2023 to determine the extent to which information about contractors’ contracting activity with foreign governments was included. DCSA provided a range of assessments that reflect the type of reports that will be used for activities related to NDAA for Fiscal Year 2020 § 847 in the future, which we reviewed to determine the type of information generally included in those assessments. We interviewed knowledgeable acquisition, intelligence, and security officials at DOD and DHS to better understand how, during the acquisition process, DOD and DHS assess risks posed by consultants that also work for China.

To describe the steps that agencies take to mitigate national security risks related to consultants’ contracting relationships with the Chinese government, we reviewed mitigation steps identified in agency risk assessments. We also

interviewed knowledgeable DOD and DHS officials to better understand how they mitigate OCI and FOCI risks.

We conducted this performance audit from June 2023 to September 2024 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

List of Addressees

The Honorable Gary C. Peters
Chairman
Committee on Homeland Security and Governmental Affairs
United States Senate

The Honorable Josh Hawley
United States Senate

We are sending copies of this report to the appropriate congressional committees; the Secretary of Defense, the Secretary of Homeland Security, and the Director of the Office of Management and Budget. In addition, the report is available at no charge on the GAO website at <https://www.gao.gov>.

GAO Contact Information

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Endnotes

¹National Defense Authorization Act for Fiscal Year 2024, Pub. L. No. 118-31, § 812(f)(1) (2023) (codified at 10 U.S.C. § 4501 note prec.).

²FAR 2.101 defines “advisory and assistance services” as services provided under contract by nongovernmental sources to support or improve organizational policy development, decision-making, management and administration, program and/or project management, or research and development activities. The FAR definition states that advisory and assistance services can also mean providing professional advice or assistance to improve the effectiveness of federal management processes or procedures, including those of an engineering and technical nature. The definition states that these services may result in advice, opinions, analyses, evaluations, recommendations, training, and the aid of support personnel needed for successful performance of ongoing federal operations. The definition also states that all advisory and assistance services are classified within one of three definitional subdivisions: (1) management and professional support services, (2) studies, analyses, and evaluations, and (3) engineering and technical services.

³FAR 2.101. While the FAR definition refers to a “person,” the FAR’s procedures for identifying, evaluating, and resolving OCI apply to contracts with profit or nonprofit organizations. FAR 9.500(a), 9.502(a).

⁴FAR 2.101.

⁵FOCI is addressed in the *National Industrial Security Program Operating Manual*, which establishes the requirements, restrictions, and safeguards for the protection of classified information that is disclosed to, or developed by, contractors of the U.S. government. 32 C.F.R. §§ 117.1(a), 117.11. Section 117.11 of the operating manual includes procedures intended to mitigate FOCI risks. 32 C.F.R. § 117.11.

⁶Subject to certain authorities listed in the FAR, federal agencies may issue acquisition regulations that implement and supplement the FAR. FAR 1.301(a)(1). They may incorporate agency policies, procedures, contract clauses, solicitation provisions, and forms that govern the contracting process or otherwise control the relationship between the agency, including any of its suborganizations, and contractors or prospective contractors. *Id.* The Departments of Defense and Homeland Security follow the Defense Federal Acquisition Regulation Supplement and the Homeland Security Acquisition Regulations, respectively.

⁷As discussed later in this report, portions of DHS and DOD procedures for assessing Small Business Innovation Research and Small Business Technology Transfer awards for potential foreign influence address this issue, in part.

⁸Our prior work noted similar challenges with identifying foreign entities of concern, including those in China. GAO, *Research Security: Strengthening Interagency Collaboration Could Help Agencies Safeguard Federal Funding from Foreign Threats*, [GAO-24-106227](#) (Washington, D.C.: Jan. 11, 2024).

⁹The Personnel Security Directorate within DCSA also conducts risk management activities with respect to the U.S. government’s workforce through investigations, screening, adjudications, vetted workforce data repository maintenance, and other vetting and personnel security management services.

¹⁰See 41 U.S.C. § 1707; FAR subpart 1.5.

¹¹Pub. L. No. 116-283, § 819(c)(2) (codified at 10 U.S.C. § 4819 note).

¹²According to the DOD instruction, DCSA also will conduct FOCI risk reviews for DOD subcontracts and defense research assistance awards valued over \$5 million, generally excluding awards for commercial goods and services.

¹³The policy is also to address how acquisition personnel are to direct the award, modification, or termination of subcontracts when DCSA confirms that a company is under FOCI and poses a risk to national security.

¹⁴The Defense Acquisition Regulations Council is responsible for developing fully coordinated recommendations for revisions to the DFARS. The Under Secretary of Defense for Acquisition and Sustainment delegates authority to the Principal Director of Defense Pricing and Contracting to develop, coordinate, issue, and maintain the Federal Acquisition Regulation, DFARS, and supplementing DOD regulations.

¹⁵Pub. L. No. 117-324, § 2(a) (codified at 41 U.S.C. § 2303 note).

¹⁶GAO, *Defense Acquisitions: DOD Needs to Improve How It Communicates the Status of Regulation Changes*, [GAO-19-489](#) (Washington, D.C.: July 11, 2019).

¹⁷Pub. L. No. 118-31, § 812(a)(1) (codified at 10 U.S.C. § 4501 note prec.).

¹⁸See 41 U.S.C. § 1707(d); FAR 1.501-3(b).

¹⁹GAO, *Standards for Internal Control in the Federal Government*, [GAO-14-704](#) (Washington, D.C.: Sept. 10, 2014).

²⁰To identify federal spending on contracts involving consulting services, we analyzed FPDS data for contract actions for services for which agencies selected FPDS Product and Service Code (PSC) groups “B” and “R.” These groups include those for special studies or analysis, and professional, administrative, and management support services.

²¹Our analysis was based on a review of contract actions reported under FPDS Product and Service groups “B” and “R.” These groups include special studies or analysis, and professional, administrative, and management support services.

²²GAO, *Small Business Research Programs: Agencies Are Implementing Programs to Manage Foreign Risks and Plan Further Refinement*, [GAO-24-106400](#) (Washington, D.C.: Nov. 16, 2023).

²³FAR 9.502(b).

²⁴Pub. L. No. 117-324, § (2)(a)(1)(B) (2022) (codified at 41 U.S.C. § 2303 note). More specifically, the law requires the FAR Council to revise the FAR to provide and update “definitions, guidance, and illustrative examples related to relationships of contractors with public, private, domestic, and foreign entities that may cause contract support to be subject to potential organizational conflicts of interest, including undue influence.” *Id.*

²⁵Pub. L. No. 118-31, § 812(a)(1) (2023) (codified at 10 U.S.C. § 4501 note prec.). The law defines the term “consulting services” to have the meaning of the term “advisory and assistance services” in FAR section 2.101, with exceptions for certain products and services. *Id.* § 812(f)(1).

²⁶Executive Office of the President, Office of Management and Budget, *The North American Industry Classification System Manual (2022)* (Washington, D.C.). The North American Industry Classification System (NAICS) was originally developed to provide a consistent framework for the collection, analysis, and dissemination of industrial statistics used by government policy analysts, by academics and researchers, by the business community, and by the public. The NAICS manual details how industrial statistics are presented.

²⁷In response to a draft of this report, DOD officials told us that around 4 percent of SBIR/STTR proposals received between July 2023 through February 2024 were flagged for assessment of risks related to ties with foreign countries of concern. Also in response to a draft of this report, DHS officials told us that the DHS SBIR program found an inconsistency that impacted an award decision in one instance. DHS’s decision to not award that contract was due to an omission rather than a determination of foreign influence risk.

²⁸DFARS 225.7021, 252.225-7057, 252.225-7058. See also 88 Fed. Reg. 12,861 (Mar. 1, 2023) (final rule implementing the law).

²⁹Pub. L. No. 117-81, § 855(c) (codified at 10 U.S.C. § 4651 note prec.).

³⁰See FAR 1.602-2.