Final DFARS OCI Rules

by Robert S. Metzger

On December 29, 2010, the Department of Defense ("DoD") issued a final rule[1] regarding Organizational Conflict of Interest ("OCI") in Major Defense Acquisition Programs ("MDAPs"). The final rule surprised many who expected that the final DoD OCI rules would follow the tough and expansive approach of the rules DoD proposed on April 22, 2010.[2] DoD's retreat may prove a temporary respite as many of the issues which troubled contractors are likely to resurface when new FAR rules are proposed. The MDAP rules are unlikely to bring clarity to this important and often contentious area.

As proposed in April, DoD's ambitious OCI rules would have applied generally to defense acquisitions, not just to MDAPs, treated OCI as an ethics issue, imposed massive new disclosure obligations, and could have had great impact on the defense industrial base by prompting a "partition" between companies providing advisory services, on the one hand, and firms doing development and production, on the other. OCI was treated as a matter of contracting integrity; the rigor of the proposed rules followed that premise.

As issued in December, however, the final DFARS were drawn much more narrowly. One announced explanation is that DoD accepted the criticism that the proposed rules exceeded statutory requirements because they applied generally to defense acquisitions rather than only to MDAPs. Another stated reason is that DoD concluded that it should not appear to preempt the Federal Acquisition Regulation ("FAR") Council, by issuing an OCI rule of broad applicability while rulemaking was continuing for a general FAR OCI revision. Also contributing were practical considerations. First, the proposed rule would have greatly increased the workload of contracting officers ("COs") while arguably limiting their freedom of action in making OCI decisions. Second, the proposed rules lacked the flexibility necessary to enable DoD to serve its own best interests. Specifically, a perception was present that COs, faced with a potential OCI, would default to resolution measures resulting either in "avoidance" or "restrictions on future contracting." In sensitive areas, where performance requirements are most critical, this could have meant that DoD was denying itself access to the most capable and best informed contractors.

[1] Department of Defense Federal Acquisition Regulation Supplement ("DFARS") Case 2009-D015). 75 Fed. Reg. 81908 (to be codified at 48 C.F.R. pt. 209 and 252).

[2] DFARS; OCI in MDAPs (DFARS Case 2009-D015), 75 Fed. Reg. 20954 (proposed Apr. 22, 2010).

A related concern, as reflected in the final DFARS, was how new OCI rules would affect competition. Arguably, the proposed rules would have promoted the growth of "pure play" advisory companies and encouraged competition by removing from the playing field for advisory services those larger, integrated companies which also have design and build capabilities. In certain areas where advisory services are required, however, DoD may have concluded that too strict an approach would have resulted in insufficient competence and capability available. Thus, the final rule, ostensibly to promote competition, allows significantly greater opportunity for integrated firms to remain eligible for DoD work on major programs. At various places in the final DFARS (and in the accompanying explanations), the concept is articulated that DoD's policy is to "promote competition and preserve DoD access to the expertise and experience of qualified contractors." (E.g., DFARS 209.571-3.)[3]

Though the new DFARS apply only to MDAPs (and "pre-MDAPs"), and have far less draconian impact than some anticipated from the April 2010 proposal, they should not be understood as the definitive or final expression of DoD's intentions or as controlling what will emerge from the FAR Council as a rule of general applicability to federal procurement. As evident from the explanation accompanying the new rule, DoD continues to view OCI issues as a key issue which applies equally to small procurements as to large MDAPs. Some of the controversial features of April proposal may return in the eventual FAR revision.

Background

Section 207(a) of the Weapon System Acquisition Reform Act ("WSARA"), Pub. L. No. 111-23, required the Secretary of Defense, not later than 270 days after the date of the enactment, to revise the DFARS to "provide uniform guidance and tighten existing requirements for organizational conflicts of interest by contractors in major defense acquisition programs." [4]

Section 207 required that the new regulations, at a minimum, address OCI that can arise in each of four circumstances: (1) lead system integrator contracts; (2) systems engineering and technical assistance ("SETA") functions on programs where performed by contractors who simultaneously are competing to perform as either prime contractor or a supplier of a "major subsystem or component" for such programs; (3) awards by a prime to affiliated business units, particularly as concerns subcontracts for software integration or the development of a proprietary software system architecture; and (4) performance by contractors in "technical evaluations" on major defense acquisition programs. At Section 207(b)(3), Congress specifically required that contracts for SETA functions prohibit a contractor (or affiliate) from participating as a prime contractor or major subcontractor in the "development or construction" of a weapon system under the program. Congress permitted "limited exceptions" to these requirements, at Section 207(b)(4), "as may be necessary" to ensure that DoD has "continued access to advice" on systems architecture and systems engineering matters from "highly qualified contractors with domain experience and expertise."

[3] In the April proposed rules, DoD announced that OCI, "by their mere appearance, call into question the integrity and fairness of the competitive procurement process." 75 Fed. Reg. 20959. The "tilt" of the rules then was to exclude parties with apparent, actual or potential OCI, in part because they could realize unfair competitive advantage. The final DFARS OCI rules appear oriented in an opposing direction, as reconciliation of the twin goals -- "promote competition" and "preserve access" – may be accomplished by refraining from exclusion companies with distinctive capabilities or special knowledge.

[4] A "major defense acquisition program," as defined at 10 U.S.C. § 2430, is one so designated by the Secretary of Defense or one that is estimated to require an eventual total expenditure for Research Development Test and Evaluation of more than $300 Million (approximately $442 million in FY 2009 dollars) or an eventual total expenditure of more than $1.8 Billion (approximately $2.578 billion in FY 2009 dollars). *See* CONG. RESEARCH SERV., 7-5700, Defense Acquisitions: How DOD Acquires Weapon Systems and Recent Efforts to Reform the Process (2009), *available at* http://www.fas.org/sgp/crs/natsec/RL34026.pdf. The GAO reported, as of April 2009, that there were 96 major defense acquisition programs. U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-09-543T , Defense Acquisitions: Measuring the Value of DOD's Weapons Programs Requires Starting with Realistic Baselines, at 3 (2009).

The regulations as proposed on April 22, 2010 went beyond WSARA but, in the main, expanded the reach and the rigor of principles expressed in the statute. In contrast, the final rule hews more closely the specific mandates of Section 207. The initial comment period was to close on June 21, 2010. It was extended to July 21, 2010. DoD received comments from 21 respondents. 75 Fed. Reg. 81909.

Expansive Classification of SETA Functions

The final DFARS will have powerful impact in certain, focused areas. A key feature which first appears in the final rule is an expansive and inclusive definition for "systems engineering and technical assistance." In promulgation comments, DoD announced its decision to provide a "unified" definition of this (SETA) function. *See* 75 Fed. Reg. 81910; DFARS 209.571-1. Also in the comments, DoD established that SETA contracts are not limited to MDAPs but "could be for other types of programs as well," implying that the heightened OCI scrutiny will apply wherever there is a SETA contract. In the rule itself, the definition of SETA functions includes a lengthy list of (non-exclusive) "examples." The table below compares the relevant prior definition, at FAR 9.505, to the new DFARS:

FAR 9.505(b)	**DFARS 209.571-1**
Systems engineering includes a combination of substantially all of the following activities: determining specifications, identifying and resolving interface problems, developing test requirements, evaluating test data, and supervising design. Technical direction includes a combination of substantially all of the following activities: developing work statements, determining parameters, directing other contractors' operations, and resolving technical controversies	(3) "Systems engineering and technical assistance"— (i) Means a combination of activities related to the development of technical information to support various acquisition processes. Examples of systems engineering and technical assistance activities include, but are not limited to, supporting acquisition efforts such as— (A) Deriving requirements; (B) Performing technology assessments; (C) Developing acquisition strategies; (D) Conducting risk assessments; (E) Developing cost estimates; (F) Determining specifications; (G) Evaluating contractor performance and conducting independent verification and validation; (H) Directing other contractors' (other than subcontractors) operations; (I) Developing test requirements and evaluating test data; (J) Developing work statements (but see paragraph (ii)(B) of this definition)

The FAR definition (of "systems engineering") enumerated four (4) representative activities but required that "a combination of *substantially all*" of them be present. FAR 9.505(b) (emphasis added). DFARS 209.571-1, in contrast, lists ten (10) functions and these are but non-exclusive "examples" of SETA functions – conceivably, *any* of the enumerated functions qualifies as SETA work. Consequently, contractors who presently perform advisory functions – on MDAPs or otherwise – will need to consider very carefully whether they will now be classified as performing SETA functions. There is significance to

such a classification. DFARS 209.571-7 reflects the "statutory" prohibition imposed by WSARA § 207 that a contract for SETA functions (for MDAP or "pre-MDAP") must prohibit the contractor *or any affiliate* from participating in the development or production of a weapon system under such program. Integrated firms are well-counseled to be wary of performing advisory functions if they could be characterized as SETA and the consequence would be downstream preclusion at higher value acquisition phases.

Features of the Final Rule

Part 209 Placement	The final rule is placed under DFARS Part 209 ("Contractor Qualifications").
New Definitions	MDAPs are defined as including "Pre-MDAPs," the latter being "a program that is in the Materiel Solution Analysis or Technology Development Phases preceding Milestone B of the Defense Acquisition System and has been identified to have the potential to become a major defense acquisition program." DFARS 209.571-1.
	A new definition of "Systems engineering and technical assistance" is provided at DFARS 209.571-1. As explained above, the definition is a substantial expansion beyond prior FAR treatment.
Limited to MDAPs	The final rule applies only to MDAPs (and in certain respects to Pre-MDAPs) and not to all DoD acquisitions. DFARS 209.571-0.
Statement of Policy	DoD policy, according to the final rule, is that agencies "shall" obtain advice on MDAPs and Pre-MDAPs "from sources that are objective and unbiased." DFARS 209.571-3. COs are to resolve OCIs "in a manner that will promote competition and preserve DoD access to the expertise and experience of qualified contractors." *Id*.
Mitigation	The final rule defines mitigation and, where the CO and contractor have agreed to mitigation of an OCI, the mitigation plan must be incorporated into the contract. The new rule no longer states a preference for mitigation over other resolution techniques, i.e., avoidance or limitation on future contracting (avoidance). If an otherwise successful offeror is unable to effectively mitigate the OCI, then the CO shall use other approaches to resolve the OCI, such as selecting another offeror or requesting a waiver (where not precluded by statute). DFARS 209.571-4.
Identification of OCI	When evaluating OCI for MDAPs, the CO shall "consider" ownership of business units performing SETA or other advisory functions to a MDAP by a contractor who owns businesses competing or potentially competing to perform as the prime or be a supplier of a major subsystem on the same MDAP. The CO also is to consider the proposed award "of a major subsystem" by a prime contractor to affiliates and "particularly the award of a subcontract for software integration or the development of proprietary software architecture." DFARS 209.571-6. The final rule does not instruct the CO on what to do if the facts to be considered are present.
SETA Contracts	The final rule tracks WSARA § 207(b)(2) by stating that agencies shall obtain advice on systems architecture and systems engineering on MDAPs from Federally Funded Research and Development Centers "or other sources independent of the [MDAP] program contractor." DFARS 209.571-7. Similarly, the statute is followed in the prohibition for any SETA contractor on a MDAP (or Pre-MDAP) from participating as a contractor or major subcontractor in the "development or production of a weapons system under such program." *Id*.

Certain Exceptions	Further tracking the statute, an exception is allowed if the head of contracting activity determines that DoD "needs the domain experience of the highly qualified apparently successful offeror" and there is assurance, based on the "agreed-to resolution strategy," that the offeror "will be able to provide objective and unbiased advice" without a limitation on future participation in development and production. DFARS 209.571-7(c). The regulation does not explain how DoD is to determine or document its need, set any standard for sufficiency of the documentation, or what factors may be considered in evaluating whether the offeror can and will provide objective and unbiased advice.
Solicitation and Contract Clauses	One clause, DFARS 252.209-7008, Notice of Prohibition Relating to Organizational Conflict of Interest – Major Defense Acquisition Program, is to be incorporated where a solicitation is for a MDAP or Pre-MDAP. This clause advises potential offerors of the WSARA § 207 prohibition and provides a procedure by which an offeror may request an exception and submit a Mitigation Plan. If adopted, the Mitigation Plan is to be incorporated in the contract. The second clause, DFARS 252.209-7009, Organizational Conflict of Interest – Major Defense Acquisition Program, contains a definition of "major subcontractor." The definition provides that a subcontract less than the cost or pricing data threshold is not a "major subcontract;" a subcontract equal to or exceeding $50 million, however, automatically is a "major subcontract." No discretion is afforded to the CO in applying these definitions. This clause also recites the WSARA § 207 prohibition and obligates a contractor to comply with an OCI Mitigation Plan if one is incorporated in the contract. Several sanctions are specified for noncompliance.

Key Distinctions between the Proposed and Final Rule

Proposed Rule	**Final Rule**
Not limited to MDAPs but applied generally to DoD acquisitions.	*Limited to MDAPs. DFARS 209.571-2.*
Located in DFARS Part 203 ("Improper Business Practices") and OCI treated as an "ethics" obligation of a contractor.	*Retained in Part 209 ("Contractor Qualifications").*
New coverage extended to task and delivery orders awarded under ID/IQ contracts and to procurement of commercial items (excepting COTS). Proposed DFARS 203.1202.	*Limited to MDAPs. DFARS 209.571-2.*
Contained new definitions of "Contractor" to include total contractor organization" and "all subsidiaries and business units." Proposed DFARS 203.1201.	*Contains no definition of contractor; does include new definitions of "systems engineering," "technical assistance" and "systems engineering and technical assistance." DFARS 209.571-1.*
OCI policy described as having two principal purposes. The first, protecting the Government's "ability to acquire supplies and services that are the best value to the Government," sought to assure the Government of receipt of objective advice and to assure the integrity of	*Policy is less expansive. One key purpose is that agencies obtain advice "from sources that are objective and independent." The second is to encourage COs to resolve OCI "in a manner that will promote competition and preserve DoD access to the*

Proposed Rule	Final Rule
competition against compromise by reason of contractor access to non-public information. The second is to protect the "public trust" by avoidance of even the "appearance of impropriety." Proposed DFARS 203.1204.	*expertise and experience of qualified contractors." No discussion whatsoever of the "public trust," "integrity" or "appearance of impropriety." DFARS 209.571-3.*
Contained definitions of each of three types of organizational conflicts of interest – "impaired objectivity," "unfair access to non-public information," and "biased ground rules." Proposed DFARS 203.1204. Follows GAO caselaw. 75 Fed. Reg. 20954-55.	*No comparable definitions included. No reference to GAO decisions.*
Contained broad and continuing disclosure obligations; contractors were "required to disclose facts bearing on the possible existence of organizational conflict of interest both prior to award and on a continuing basis during contract performance."	*No counterpart.*
Imposition of substantial additional obligations on COs, including identification of OCIs and resolution of OCIs. Guidance provided on distinction between a "potential OCI" and an "actual OCI" based on nature of work to be performed and financial interests of the offeror. Proposed DFARS 203.1205.	*No comparable obligations. No discussion of "potential" vs. "actual" OCIs. COs to "consider" ownership of business units performing advisory functions and proposed awards to affiliates of the same parent company. Rule appears to increase latitude of COs to choose resolution strategies. DFARS 209.571-6.*
In competitive acquisitions, including competitive negotiations, a CO "shall" communicate to any offeror "any issues or concerns raised by the offeror's proposed organizational conflict of interest resolution plan" and the CO shall provide the offeror "an opportunity to craft an acceptable solution." Proposed DFARS 203.1205-2(c)(3). Communications between a CO and a contractor about an OCI mitigation plan are not to be treated as "discussions" requiring equivalent opportunity to other offerors in the competitive range.[5]	*No direct counterpart. However, the contract clause at DFARS 252.209-7008, applicable to MDAPs, provides that an offeror may request an "exception" to the statutory prohibition against SETA contractors from participation in development or production and with such a request for exception the contractor may submit an OCI Mitigation Plan with its offer "for evaluation."*
Three methods of resolution were provided – "avoidance," "limitation on future contracting" and "mitigation." Preference expressed for mitigation but strong statement of Policy against the "appearance" of mitigation was perceived to reduce likelihood COs would accept mitigation except in situations such as unequal access to information where OCI is considered fully remediable by full disclosure. Proposed DFARS 203.1205-3.	*Retains same choices for resolution but COs given greater latitude "to the extent feasible" to use techniques, other than avoidance or limitation on future contracting, which will not "unnecessarily restrict the pool of potential offerors." DFARS 209.571-3(b). Final rule discourages "across the board restrictions" Likely outcome is that COs will consider themselves to have more discretion to adopt mitigation measures as satisfactory resolution to OCI.*

[5] Here, the proposed regulation cited *Overlook Systems Technologies, Inc.*, B-298099.4, *et al*., Nov. 28, 2006, 2006 CPD ¶ 185 and explained that the holding in *Overlook* only applies when OCI is an eligibility factor. The proposed regulation included a contract clause, at 252.203-70XX ("Notice of Potential Organizational Conflict of Interest") which provided a formal mechanism for a CO to notify potential offerors that an OCI may be present and to require contractors, before preparing an offer, to disclose potential OCI. No counterpart to this clause is present in the final rule.

Proposed Rule	Final Rule
Resolution actions, including mitigation, where adopted, subject to DFARS contract clause which includes duties to notify Government of changed OCI circumstances and specifies sanctions for noncompliance. Mitigation contract clause to flow down to subcontractors. Proposed DFARS 252.203-70YY.	*No counterpart DFARS contract clause, although DFARS 252.209-7008 and -7009 indicate that an OCI Mitigation Plan, if accepted, will be incorporated into the contract. No obligation to update, disclose changes, or flowdown. Sanctions for failure to comply with a Mitigation Plan at DFARS 252.209-7009 .*
Waiver available only if other OCI resolution techniques are first attempted but are "not feasible" or "not in the best interest of the Government." Waivers unavailable in competitive acquisition unless solicitation contains DFARS clause advising offerors that Government reserves the right to waive OCI. Proposed DFARS 203.1205-4(c)(3) and Proposed DFARS 252.203-70XX(h).	*No requirement that potential for waiver must be disclosed in the solicitation. No requirement that other means of resolution be found "not feasible." Waiver may be requested by CO if the "otherwise successful offeror" is unable to effectively mitigate OCI. Waivers unavailable as to statutory prohibition on SETA contractors on MDAPs (or Pre-MDAPs) participating as development or production contractor or major subcontractor.*
A CO is empowered to withhold award from an apparent successful offeror, based on OCI considerations, provided that the contractor receives written notice and is afforded a reasonable opportunity to respond. Only if all OCIs are resolved may a CO award a contract. Proposed DFARS 203.1205-4.	*Final rule contains no comparable provisions. However, notice to an offeror from whom award would be withheld by reason of OCI is provided by the present FAR 9.504(e).*
The proposed DFARS included four contract clauses of general applicability and two clauses to apply only to MDAPs. Considerable disclosure obligations would have resulted from Proposed DFARS 252.203-70XX, Notice of Potential Organizational Conflict of Interest; the clause included the specific requirement that a contractor must "disclose all relevant information" regarding any OCI, or, where a contractor believes there is no OCI, make representation of that there will be no OCI. *Id*., at 252.203-70XX (e).	*There are no counterpart contract clauses of general applicability. No clause contains a disclosure obligation or requires an affirmative representation of absence of OCI. Two clauses applicable only to MDAPs are included. One (DFARS 252.209-7008) applies to SETA contracts and contains the prohibition on participation in development or production as required by WSARA §207. The other (DFARS 252.209-7009) contains new definitions of what constitutes a "major subcontractor" and states the prohibition, also required by WSARA § 207, that a contractor which performs SETA work is prohibited from participating as a prime contractor or major subcontractor in the development or production of an MDAP.*
Proposed DFARS 252.203-70ZZ,Disclosure of Organizational Conflict of Interest after Contract Award, contained a requirement for the contractor to make "prompt and full disclosure" where it identifies an OCI that has not already been resolved during the course of contract performance. This clause would have imposed on contractors a continuing obligation to monitor the relationship between their business segments and units and activities under contract and also would have prompted monitoring of subcontract relationships.	*The final DFARS contains no counterpart.*

Certain Unresolved Issues

Unsurprisingly, while the final DFARS will not have effects as potentially draconian (or unpredictable) as the proposed rule, there are a number of critical issues left unresolved.

Will DoD Components Uniformly Apply the Final DFARS?

The proposed rules were explicitly to be "general rules" applicable to all DoD contracts with limited exceptions. *See* 75 Fed. Reg. 20954; Proposed DFARS 203.1200, 203.1202. Even so, and notwithstanding the many rigors the proposed rules would have imposed, it was not clear then whether DoD intended to require its various components to use the rules consistently and limit exceptions or varying approaches. The final rules have less certainty still, in this regard. Very likely, the experience will be that DoD applies "not less than" the new DFARS at Part 209 to Pre-MDAP and MDAP procurements. However, it is a fact that many agencies, departments and contracting activities have developed and employed "unique" approaches to OCI going well beyond, both in substance and process, the core authority which resides at FAR Subpart 9.5. (As one example, it is not uncommon for certain DoD components to use a "2-step" acquisition process with a separate, first phase of the procurement to address and resolve potential OCIs. Companies proceed to the second step if they are found not to present OCIs or to have offered an acceptable Mitigation Plan.)

Acting on the FY 2011 defense authorization measure, the Senate Armed Services Committee ("SASC") weighed in on this subject. Report 111-201, Committee on Armed Services, U.S. Senate, to accompany S.3454. The Committee expressed concern that the proposed rule offered an exception to the prohibition, of WSARA § 207, intended to prevent a SETA contractor from participating in development or construction of an MDAP weapon system. The Committee made the following statement:

> In addition, the committee notes that several DOD components already have issued guidance that is tighter than, but not inconsistent with, the proposed DFARS rule. The committee believes that the final DFARS rule should make it clear that it is not intended to override tighter standards that have been issued by DOD components.

Id., at pp.172. The final rule is silent on the subject. (DFARS 209.571-2 states that this subsection applies to MDAPs and that the DFARS takes precedence if inconsistent with FAR subpart 9.5.) In the context of the SASC guidance, one should expect individual DoD components to continue to pursue their own approach to OCI if more demanding than required by the new DFARS at Subpart 209.

How Will the Final DFARS Affect the Defense Industrial Base?

To be determined is how the final DFARS will affect the defense industrial base and whether it will slow the merger and acquisition activity prompted by OCI concerns from late 2009 through 2010. Beginning with the spinoff by Northrop Grumman of TASC in December 2009, a number of transactions have transpired where OCI was acknowledged as a contributing cause or where this was believed to be the case. Some analysts predicted that a severe DFARS OCI implementation, as indicated by the proposed DFARS, represented a deliberate decision by DoD planners and policy-makers to encourage the formation of firms exclusively focused on advisory functions and completely free of responsibilities of design/development/production as would trigger OCI. A number of such firms have emerged, in fact, and other firms with an advisory emphasis have responded to expected OCI rules to building up their advisory portfolio. Even more firms have sold or spun off advisory functions in order to concentrate on development and manufacturing.

The final DFARS, however, may slow this trend and could cause larger, integrated systems and solutions providers to reconsider whether to retain or dispose of advisory functions. Several features will be perceived as increasing the ability of larger firms to compete for MDAPs (and perform Pre-MDAPS) without the risk that any actual, prospective or "apparent" OCI will result in their disqualification. For example, in the new "Policy" section, at DFARS 209.571-3, Contacting Officers are explicitly told that they should seek to resolve OCIs "in a manner that will promote competition and preserve DoD access to the expertise and experience of qualified contractors." Moreover, COs are told specifically that they should "to the extent feasible," employ OCI resolution strategies "that do not unnecessarily restrict the pool of potential offerors in current or future acquisitions." *Id.* COs will be wary of using "avoidance" or "limitation on future contracting" as resolution techniques *because* the essentially unavoidable import of these resolution methods is to limit competition (by excluding one or more offerors with OCI issues) either in current competition (if avoidance is used) or future acquisitions (if limitation on future contracting is employed).

Will the Final DFARS Prove Functional?

Though the final rules are cut back sharply, one may question whether they will prove effective even to address OCI concerns as affect MDAPs. *Nothing* in the final DFARS requires *any* additional or specific OCI disclosures. The contrast to what was proposed by DoD in April 2010 is startling. Then, a fundamental policy was that offerors were "*required* to disclose facts bearing on the possible existence of organizational conflicts of interest both prior to contract award *and* on a continuing basis during contract performance." Proposed DFARS 203.1203(b)(1) (emphasis added). The policy was backed up by the proposed contract clause, 25.203-70XX ("Notice of Potential Organizational Conflict of Interest"), which required, *inter alia*, that an offeror disclose "all relevant information regarding any organizational conflicts of interest" or certify absence of OCI, and further that the offeror describe "any other work" performed within the previous five years that was "associated with" the work on which it was bidding. If the proposed clause drew complaints as suffering ambiguities and for its potential burden, the final rule may be faulted for doing nothing to assure that the CO has sufficient contractor-provided information to make a fully informed decision.[6] Moreover, little in the final rule encourages contractors to create and refine the internal business systems as could be described as necessary and prudent internal controls to avoid OCI.

Will the Final DFARS Facilitate Business Planning and Promote Certainty?

Here again, in several respects the final rules fall short. It may be questioned whether they will make easier the job of the CO or enable contractor executives to plan ahead prudently and accurately. In several critical areas, the new rules produce ambiguity and doubt from what appear to have been attempts at "compromise" or "concession." This is especially evident in the statement of Policy at DFARS 209.571-3. The central problem resides in paragraph (b) thereof, describing the responsibilities of the CO:

> Contracting officers generally should seek to resolve organizational conflicts of interest in a manner that will promote competition and preserve DoD access to the expertise and experience of qualified contractors. Accordingly, contracting officers should, to the extent feasible, employ organizational conflict of interest resolution strategies that do not unnecessarily restrict the pool of potential offerors in current or future acquisitions. Further, contracting activities shall not impose per se restrictions or

[6] Late in 2009, the Department of Defense, Office of Inspector General, issued a critical report on the Future Combat System. The IG concluded that "agencies frequently used the same services contractors for advisory and assistance services that were developing the FCS." Among the reasons cited, explaining how this occurred, was that:

> "solicitation provisions and contract clauses used to prevent contractors from providing advisory and assistance services for systems they helped develop or produce were inadequate and ineffective and contractor disclosures of potential OCIs were vague."

Report, "*Contracted Advisory and Assistance Services for the U.S. Army Future Combat Systems*," No. D-2010-024 (Department of Defense, Inspector General) (Nov. 24, 2009), at 9.

limitations on the use of particular resolution methods, except as may be required under 209.571-7 or as may be appropriate in particular acquisitions.

As drafted, there is "something for everyone" but what is absent is clarity. Arguably, one or more fundamental contradictions are present. One is the difficulty of reconciliation of the policy that OCI is undesirable, and should be avoided or at least mitigated, with the companion proposition that COs should "promote competition" and "preserve DoD access to the expertise and experience of qualified contractors." A further obscurity is in the use, at critical junctures, of indeterminate terms such as "generally," "to the extent feasible," "not unnecessarily restrict" or "as may be appropriate." No standards are even suggested to inform these important but highly judgmental decisions.

Are the Final DFARS Consistent with the FAR and the Caselaw?

In issuing the final DFARS, DoD explained that it would not express a "preference" for mitigation as was present in Proposed DFARS 203.1205-1(b). Instead, DoD articulated a policy to "promote competition and, to the extent possible, preserve DoD access to the expertise and experience of highly qualified contractors." 75 Fed. Reg. 81911; DFARS 209.571-3(b). This language may be taken by a CO as an invitation for "outcome-determined" decision, i.e., to make OCI decisions based on the outcome which will produce the largest number of eligible competitors and accommodate whatever preferences for specific, expert vendors as may be communicated by DoD component for whom an acquisition is being conducted. Potentially, the distinction between a CO's "determination" of whether OCI is present and the "decision" on the appropriate resolution will be obscured.[7] In this sense, the final DFARS Policy differs from FAR Subpart 9.5, as FAR 9.504(e) states that COs are not to award a contract where an OCI is present unless the OCI can be avoided or mitigated.

The new rule asserts that it takes precedence over the FAR to the extent there are inconsistencies. 75 Fed. Reg. 81909; DFARS 209.571-2(b). However, the reach of the DFARS are explicitly limited, to "major defense acquisition programs." DFARS 209.571-2(a). It is not now knowable how the GAO or the courts will assess contentions that the DFARS impose rules inconsistent with the FAR such as might render tenuous past OCI caselaw. From a policy standpoint, however, it is clear that Congressional intention, in enacting WSARA, was to increase the rigor to be applied to OCI reviews, at least as to MDAPs. This suggests the GAO, and the courts, will not be more "accommodating" to potential OCI, in protests brought under the new DFARS, than would be the case under the FAR. In this regard, there exists some tension between the potentially expansive (and permissive) authority seemingly extended to COs by DFARS 209.571-3(b), on the one hand, and principles, such as suggested in *L-3 Services, Inc*., B-400134.11, *et al.*, Sept. 3, 2009, 2009 CPD ¶ 171, at 12, that certain kinds of OCI by their nature cannot be mitigated.

Concluding Observations

The final DFARS reflects a different policy agenda and a considerably limited ambition than what had been proposed. What DoD released late in December should not be taken as the "last word" on the subject. While DoD bowed to practicalities, and to orderly process (by following rather than displacing the FAR), some key issues and objectives, surfaced by the proposed regulations, likely have been deferred rather than abandoned.

[7] FAR 9.504(a) requires contracting officers to exercise OCI duties in two steps – the first "identification" and the second "resolution." This distinction has been recognized by a number of cases of the Court of Appeals for the Federal Circuit as well as the Court of Federal Claims. E.g., *PAI Corp. v. United States*, No. 2010-5003, 2010 WL 3064174, at *5 (Fed. Cir. Aug. 5, 2010); *Filtration Dev. Co., LLC v. United States*, 60 Fed. Cl. 371, 277 (2004).

As *proposed,* the OCI DFARS could be seen as part of a systematic initiative serving several key purposes. One was to evolve federal acquisition practices to reflect an increased emphasis on procurement of services and solutions. Another was to respond to industry consolidation and vertical integration. A third was to reinforce competition and encourage independence and initiative in advisory functions. A fourth was to restore and reinforce the "public trust" by treating OCI as an improper and impermissible form of "self dealing" which could impair the integrity of public contracting.

Several of these objectives were "left on the table" and given short shrift by the Final Rule. Nevertheless, the conditions which gave rise to the expansive approach of the proposed rules have not gone away. As expressed in the Defense Science Board Report, *Creating an Effective National Security Industrial Base for the 21st Century* (July 2008), *available at* http://www.acq.osd.mil/ip/docs/dsb_task_force_on_def_ind_structure_for_transf.pdf

> [C]ontinued vertical integration poses significantly increased risks to competition, due to inherent attributes of the consolidating defense market structure.
>
> There is also significant risk of emerging [OCIs] with consolidation of systems and/or product firms with [SETA] service providers …. Clusters of these conflicts in a market are not inherently resolvable through firewalls or similar mitigations. Recusals and other structural solutions are necessary.

Indeed, at several places in the explanation accompanying the final rule, DoD made pointed comments at once endorsing core principles of the proposed rule while abandoning their application (for the time being). For example, DoD retreated from coverage greater than MDAPs, deciding "to remove coverage from the rules that is not required to comply with section 207 of WSARA." 75 Fed. Reg. 81909. Yet, DoD affirmed that its intent was to "provide coverage that would *improve* all aspects of OCI policy" and averred that "some OCI issues involved" in SETA contracting "are no different from those raised on any other procurement." *Id*. (emphasis added). As to the original intention to place OCI coverage in Part 203, DoD did not accept criticism that OCI should not be addressed among other "Improper Business Practices;" rather, DoD allowed that the rule as to MDAPs should be placed in Part 209 "until such time as the FAR coverage on OCIs may be relocated." 75 Fed. Reg. 81910.

DoD may find that its policy objectives – at least those communicated quite dramatically in the proposed DFARS – are not well served by the final DFARS at subpart 209. Also, DoD may find that it does not achieve either certainty of process or discipline and documentation of OCI decision. These limitations, combined, may fail to resolve the issues of "integrity" and "public trust" which remain, at the core, key reasons for OCI restraints. Not to be neglected is the view from the White House. President Obama, when signing into law WSARA on May 22, 2009, made the following statement:

> **This law will also enhance competition and end conflicts of interest in the weapons acquisitions process so that American taxpayers and the American military can get the best weapons at the lowest cost.**

Against this standard, the new DFARS may prove to be little more than a transitory method of minimally satisfying the *requirement* of WSARA that OCI regulations address MDAPs. The OCI subject is very much alive in the deliberations of the Office of Federal Procurement Policy, the Office of Government Ethics and the FAR Council. Section 841(b) of the FY 2009 National Defense Authorization Act required the acquisition community to address OCI. As of December 20, 2010, DoD reports that FAR Case 2011-001 is addressing OCI. *See http://www.acq.osd.mil/dpap/dars/opencases/farcasenum/far.pdf*, last accessed on January 6, 2011. One may expect that new proposed FAR rules governing OCI will emerge during 2011.

Many of the debates begun with the issuance of the proposed DFARS in April 2010, and now abated with release of the final DFARS, may be revived.

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