

Enhancing R&D Portfolio Through US  
Government Funding  
*NCMA Boston Chapter Workshop*  
*March 16, 2016*

---

**Jennifer Plitsch**

**COVINGTON**

BEIJING BRUSSELS LONDON LOS ANGELES NEW YORK SAN FRANCISCO  
SEOUL SHANGHAI SILICON VALLEY WASHINGTON

[www.cov.com](http://www.cov.com)

# Introduction

---

The Federal Government is an important potential source of research and development funding.

Such funding comes with strings attached, in the form of compliance obligations, intellectual property costs and additional liability risk to the Government and Third Parties.

Weigh the potential risks and benefits of accepting any Government funding, and take care to choose the right contract vehicle at the right time.

Take steps to manage Government rights to IP and data and mitigate liability risk.

Assess compliance obligations and invest appropriately in meeting such obligations to minimize risks.

# Overview

---

- Contract Vehicles
- Identifying Sources of Funding
- Key Considerations
  - Intellectual Property
  - Protection of Government Property
  - Liability Risks
- Compliance
- Strategic Planning

## Contract Vehicles

---

- Cost-Reimbursement Contracts
- Fixed-Price Contracts
- Cooperative Research and Development Agreements
- Small Business Innovation Research Contracts
- Grants/Cooperative Agreements
- Other Transaction Authority Agreements

## Cost-Reimbursement Contracts

---

- Most common for R&D
- Contractor reimbursed for costs incurred in performing agreed upon Statement of Work
- Costs must be accounted for accurately and comply with FAR Part 31 and in some cases the Cost Accounting Standards
- Low financial risk, but higher risk of liability due to compliance obligations
- Typically requires significant investment in internal systems and controls
- Cost-sharing generally not required and fees are available (but limited)

## FAR Cost Principles

---

- Set out in Part 31 of the FAR.
- Define costs that will be considered “allowable” by the Government in negotiation, administration and performance of cost reimbursement contracts.
- Also used to determine incentive fees and to price adjustment under fixed price contracts.
- Standards of reasonableness, allocability and allowability of direct and indirect costs.
- Certain specific costs deemed unallowable in some or all circumstances in Part 31.

# Cost Accounting Standards

---

- Developed to achieve uniformity and consistency in cost accounting practices in estimating, accounting and reporting costs.
- If covered, contractor must disclose cost accounting practices in keeping with the CAS principles and follow them.
- Do not apply to most firm fixed price contracts, or those less than \$7.5 million.
- Full coverage for single contracts over \$50 million or more than \$50 million in a year, modified coverage at lesser levels (only need to comply with certain of the CAS standards)

## Cost and Pricing Data

---

- Generally the contracting officer must obtain cost and pricing data from bidders
- If the contracting officer has sufficient information to determine price reasonableness he may request a waiver
- Cost or pricing data not required when
  - it is determined that prices agreed upon are based on adequate price competition (usually 2 or more bidders)
  - based on prices set by law or regulation
  - acquisition of a commercial item
  - waiver

## Fixed Price Contracts

---

- Contractor is generally paid a fixed amount that is not adjustable based on cost experience.
- Shifts the risk of increased costs to contractor
- Firm-fixed price, Fixed-price economic price adjustment, Fixed-price incentive, Fixed-price prospective/retrospective redetermination
- Fixed-price contracts are required for most commercial item procurements and in some circumstances available for R&D contracting.

## Fixed-Price Contracts

---

- Less frequently available for R&D
- Higher financial risk, but lower risk of liability due to compliance obligations
- Cost-sharing not required and profit derived from cost savings can be considerable
- Negotiation and statement of milestones incredibly important.
- Agency personnel may insist on applying cost-reimbursement requirements (e.g. consent to subcontract)
- Certain standard issues such as title and delivery require additional attention for revenue recognition purposes and to set expectations

# Cooperative Research and Development Agreements

---

- The primary purpose is to allow a contractor and a federal laboratory to exchange materials, services, or intellectual property in support of a particular project without a transfer of funds from the Government.
- Often used to conduct preliminary research, but they can also be used to speed commercialization of a particular technology.
- Effectively results in cost-sharing, although funds cannot be provided to the contractor
- Standard terms are generally flexible
- More favorable intellectual property rights technically available, but in practice will often reflect Bayh-Dole requirements
- Primary vehicle for working with government laboratories or clinical sites

## Small Business Innovation Research Contracts

---

- The primary purpose is to provide funding to small businesses to further research and development with potential commercial applications.
- Phase I awards typically involve preliminary research, while Phase II awards are often targeted at specific agency needs.
- Phase III rights can be acquired from a small business participant to commercialize technology with unique SBIR data rights.
- SBIR awards can take on the form of contracts, grants, or cooperative agreements.
- Available to qualifying small businesses
- Provide low levels of initial funding, but may ultimately lead to significant sole-source contracts

## Grants/Cooperative Agreements

---

- Financial assistance vehicles generally available for specific projects.
- The primary purpose is to provide financial assistance to carry out a public purpose, rather than to acquire a particular product or service.
- Financial assistance awards are often used when a project has little to no immediate commercial benefit, such as preliminary research or the initial development of a product for a limited government market.
- Financial assistance awards can be made through a technology investment agreement (this vehicle is also used for OTAs).
- Not FAR-governed contracts, but subject to separate regulatory requirements.

## Other Transaction Authority Agreements

---

- The primary purpose is to further research and development when a standard vehicle would not be appropriate.
- Often, contractors must demonstrate a lack of experience with government contracting requirements and invest in a project under cost-sharing requirements.
- Not common outside DOD
- Agency-specific authorities vary, but typically requires agencies to make an effort to obtain cost-sharing.
- No Fee
- Extremely flexible contract terms
- Flexibility on IP requirements
- Exemption from numerous standard requirements, although agency personnel may insist on following familiar procedures.

# Identifying Sources of Funding

---

- Standard Solicitations
- Broad Agency Announcements
- SBIR Topics of Interest
- Unique Programs to Satisfy Specific Needs
- Unsolicited Proposals
- Pre-Solicitation Meetings

# Key Considerations

---

- Intellectual Property
- Government Property
- Title/Risk of Loss/Revenue Recognition
- Potential Liability

# Intellectual Property

---

- For inventions developed with Government funds or with a mix of public and private funding Government obtains some rights.
- Different types of IP
  - Technical Data: A broad category of recorded information, such as drawings and manuals
  - Computer Software: Source code, computer programs, and algorithms
  - Patent Rights
- The FAR provides policy and guidance on the acquisition of patent rights:
  - Government honors the rights in data resulting from private development and limits its demand for such rights to those essential for Government purposes.

# Patent Rights

---

- Generally, contractors may retain title to inventions made in the performance of a federal contract subject to a federal license.
- The Government shall have a nonexclusive, nontransferable, irrevocable, paid-up license to practice or have practiced for or on behalf of the United States the subject invention through the world.
- Limited conditions under which the Government may obtain title – basically where contractor fails to take certain required steps to retain title.
- Limited conditions under which Government may grant licenses or “march-in”

# Patent Rights

---

- Authorization and Consent clause permits the infringement of United States patents as necessary to perform government contracts.
- A contractor must notify the Government of claims of patent infringement in connection with performing a Government contract.
- In some instances, contractors must compensate Government for infringement damages

# Rights in Data

---

- The Government acquires “unlimited rights” in most data first produced in the performance of the contract (FAR 52.227-14).
- Unlimited rights means the right of the Government to use, disclose, reproduce, prepare derivative works, distribute copies to the public and display publically in any manner and for any purpose and to have or permit others to do so.
- Contractors generally may protect data that embodies trade secrets or are confidential and privileged to the extent that such data pertains to items or processes developed at private expense.

# Data Rights

---

- Contracts requiring the production of data generally define the parties' respective data rights
- Limited Rights Data: Contractor generally may protect data that embodies trade secrets or is confidential and privileged to the extent that such data pertains to items or processes developed at private expense
  - If the Government requires delivery of limited rights data, it generally may not use the data for manufacturing and may not disclose the data outside the Government.
  - Contractor must mark any limited rights data delivered to the Government with the restricted rights notice specified in a contract

# Protecting Data

---

- Normally, the Government receives unlimited rights in data unless the contractor takes affirmative steps
- Prior to award, offerors (and their major subcontractors) generally develop a list of any data that they will provide the Government with limited rights, including their reasons for imposing for such a restriction
- The list is often included in the successful offeror's contract
- During contract performance, the Government may have unlimited rights in any unlisted data that is provided to the Government
- In non-DoD contracts, a specific clause (FAR 52.227-14, Alt I) generally must be included in the contract to allow a contractor to mark limited rights data

# Government Property

---

- Government property furnished to contractors may include: facilities, material, special tooling, special test equipment, and production and research property
- Generally, contractors are responsible and liable for Government property in their possession, but only have risk of loss under certain fixed-price contracts or when property systems are inadequate.
  - This includes Government property in the possession or control of a subcontractor
- Contractors should develop a written property control system, approved by the Government, and maintain written records of Government property

# Government Property

---

- Contractors generally should keep Government property physically separate from contractor-owned property
  - If commingling is necessary, seek Government approval
- Periodic physical inventories must be performed by personnel other than those who maintain the property records
- Upon completion of a contract, the contractor generally needs to perform an inventory and return Government property

## Title/Risk of Loss/Revenue Recognition

---

- Under R&D contracts, deliverables are often not as clearly defined and “delivery” may take place in a non-standard way.
- Important to define which party has title to contract materials, and which party bears the risk of loss.
- This information will inform liability assessments and insurance needs, but also may inform revenue recognition.
- Under accounting rules, recognizing revenue for some research and development work requires a degree of finality that can be difficult to establish easily if the Contractor keeps physical possession of the items or material delivered under the contract.

# Potential Liability

---

- Unlicensed on untested products
- Clinical trials (scope, waiver and risk)
- Manufacturing
- Potential Protections
  - Anti-Deficiency Act – standard indemnification not available
  - PREP Act – declaration must be secured and limited protection outside the United States
  - Public Law 85-804 – covers unusually hazardous risks, difficult to obtain. Made whole after liability incurred.
  - SAFETY Act for some products
  - Limited indemnities
  - Reimbursement of insurance costs

# Sound Contract Administration

---

- Sound Contract Administration requires:
  - Centralized administration and oversight
  - Centralized contract files—good recordkeeping
  - Meeting document retention obligations
  - Adopting and following policies and procedures
  - Consistent and up-to-date completion and tracking of reps and certs
  - Consistent and accurate completion of reporting requirements

# Sound Contract Administration

---

- Elements of Sound Compliance Program:
  - Appoint a person to speak for the company and be responsible for adhering to RFP/contract requirements
  - Organize a compliance committee consisting of program, contract administration, legal, and finance personnel
  - Develop and modify internal policies, as needed
  - Provide appropriate training
  - Make sure responsible personnel have read the contract carefully; understand all terms and which must be flowed down; have trained others on key provisions

# Sound Contract Administration

---

- Elements of Sound Compliance Program (more):
  - Create and keep a well-organized, complete contract file
  - Develop formal compliance program—get management’s “buy in” on government contracts compliance
  - Conduct internal compliance reviews
  - Make sure your compliance program includes a written code of conduct, a hotline, procedures for periodic internal audits, and regularly scheduled training
  - Institute procedures for staying abreast of regulatory changes

## Final Thoughts - Strategic Planning

---

- Identify Potential Commercial and Government Markets
- Assess Funding Gaps and Stages of Development
- Minimize IP Risk
- Target Appropriate Agencies for State of Research
- Sustainable Government or Private Market?
- Invest Resources in Both Technical and Legal Compliance

# Questions?

---

[jplitsch@cov.com](mailto:jplitsch@cov.com)

**COVINGTON**

BEIJING BRUSSELS LONDON LOS ANGELES NEW YORK SAN FRANCISCO  
SEOUL SHANGHAI SILICON VALLEY WASHINGTON

[www.cov.com](http://www.cov.com)