

A.

Identifying IP Issues When Reviewing Government Solicitations And Contracts

I. Summary of Review Process

- Sales to Federal State, and Local Governments by commercial companies can raise issues related to intellectual property ("IP") terms and conditions that Government customers may insist on including in the sales agreement or contract.
 - It is important to carefully review all Government solicitations -- frequently called Request for Information ("RFI"), Request for Quote ("RFQ"), Request for Proposal ("RFP"), Invitation for Bid ("IFB") -- as well as Government sales agreements or contracts to ensure that unique IP-related terms and conditions in Government contracts do not negatively impact a commercial company's overall business.
 - These unique government IP-related terms and conditions may potentially impact the Company's overall business in many ways, including:
 - How and to whom the Company sells its goods and services
 - How it protects its intellectual property
 - How it keeps its records and what records it will need to disclose
 - Potential risks and liabilities also may be created that are unique to doing business with the government (*e.g.*, potentially providing the Government unlimited rights in the Company's IP or potentially breaching 3rd-party agreements by improperly providing 3rd-party IP to the Government).
- The process for reviewing Government solicitations and contracts to identify IP-related terms and conditions that frequently pose problems for commercial companies must be timely and thorough.
 - Timing is critical because feedback provided to the Government by a company early in the procurement process significantly increases the likelihood that the Government will change or eliminate IP-related terms and conditions that are not consistent with standard commercial practices.

- Thorough review is critical because the solicitation or contract format, and the language in the terms and conditions vary widely. As a result, they must be read carefully and understood from the front to the back, including any clauses that may be incorporated by reference.
- Red Flag issues include any IP-related terms and conditions that are inconsistent with standard commercial practices. Government customers can and often do enforce the IP-related terms and conditions in contracts literally -- commercial companies cannot assume that their standard commercial practices will trump the contract language.

II. Commercial Versus Government Sales

- Most commercial companies are wise to limit pursuit of Government business to Commercial Item Acquisitions under Part 12 of the Federal Acquisition Regulation ("FAR"), rather than the traditional non-commercial FAR contract.¹ This approach is frequently driven by the burdensome and unique business infrastructure requirements that the traditional FAR contract generally impose on Federal Government contractors.
- Commercial Item Acquisitions under FAR Part 12 include terms and conditions that are much closer to standard commercial terms and conditions. FAR Part 12 requires that the Contracting Officer only include two FAR provisions in solicitations² and two FAR clauses in prime contracts³ for the acquisition of Commercial Items.⁴

¹ The FAR is the primary governing document that applies to any procurement contract awarded by a Federal agency, and it contains the various standard clauses that are included in Federal contracts. Numerous statutes on a wide range of topics relating to Federal acquisitions of products and services are implemented through the regulations contained in the FAR. *See* 48 C.F.R. Chapter 1.

² FAR 52.212-1, Instructions to Offerors - Commercial Items; FAR 52.212-3, Offeror Representations and Certifications - Commercial Items.

³ FAR 52.212-4, Contract Terms and Conditions - Commercial Items; FAR 52.212-5, Contract Terms and Conditions Required to Implement Statutes or Executive Orders - Commercial Items.

⁴ In addition, the FAR specifically exempts Commercial Item prime and subcontracts from many procurement statutes. *See* FAR 12.503 and 12.504, respectively.

- The mandatory terms and conditions clause for Commercial Items includes different (lesser) requirements and obligations for, among others, data rights and other forms of IP.⁵
- When reviewing Government solicitations or contracts at the Federal level, look for language that states the procurement is under "FAR Part 12," or is a "Commercial Item Acquisition." In addition, the FAR Part 12 contracts often use "Standard Form (SF) 1449" for the signature page of the contract. In contrast, traditional FAR contracts typically incorporate numerous pages of FAR clauses by reference and lack any reference to commercial terms and conditions.
- When reviewing Government solicitations or contracts at the State or Local level, look for language that makes it clear the Government is buying commercial services or products, and you may see language that recognizes the contractor's standard commercial terms and conditions.

III. Timing of the Review Process

- Timing is critical when dealing with Government solicitations because early involvement in the procurement process and providing feedback concerning a Company's standard commercial practices significantly increases the likelihood the Government will be agreeable to amending the solicitation to eliminate or modify Government-unique requirements.
 - Commercial companies should monitor Government activity and make sure their personnel are on the "bidders' list" to receive RFIs and draft RFPs.
 - RFIs and draft RFPs should be reviewed carefully to identify all terms and conditions that are inconsistent with companies' standard commercial practices.
 - Companies should submit timely responses to each of the IP-related terms and conditions that are inconsistent with commercial practices. The responses should include a full explanation of why the IP-related terms and conditions are inconsistent with commercial practices, and how the IP-related terms and conditions

⁵ FAR 52.212-4, Contract Terms and Conditions - Commercial Items.

will impact performance (*e.g.*, increasing performance costs, timeliness of deliveries, etc.), or limit competition (*e.g.*, causing commercial companies to no-bid the solicitation).

- If responses are submitted to the Government at the RFI or draft RFP stage of the procurement, or if there still is time available to submit questions and receive answers ("Q&As") on the RFP, commercial companies should include both the rationale as to why the terms and conditions are inconsistent with standard commercial practices and suggested language for the Government to use instead of the problematic terms and conditions.
- If there is not adequate time left in the procurement process to ask for clarification or for Q&As, commercial companies may need to take exception to Government-unique IP-related terms and conditions. Caution: the solicitation should be reviewed carefully to ensure that exceptions to terms and conditions are allowed. Some solicitations prohibit exceptions and provide that any proposals taking exception to the Government requirements will be eliminated from the competition.
- Caution: problematic IP-related terms and conditions are often included even in FAR Part 12 Commercial Item solicitations, as well as in traditional FAR solicitations. Therefore, commercial companies should not assume that further review is not needed if the Government states it is using FAR Part 12. The responses submitted to the Government that question the use of such terms and conditions are intended both to educate the Government procurement personnel and persuade them to eliminate or modify the IP-related terms and conditions.

IV. IP Related Terms And Conditions That Are Inconsistent With Commercial Practices

- While IP-related terms and conditions that are inconsistent with companies' standard commercial practices may be found anywhere in the Government solicitation, the following are examples of categories of frequently occurring issues:
 - The Government may include terms and conditions that require commercial companies to give ownership or unlimited license rights in their intellectual property or proprietary information even after the contract terminates or ends.

- The Government may require access to, use of, and the right to disclose at its discretion IP-related information, such as patents, technical data, copyrights, and software.
- The Government may include terms and conditions requiring that commercial companies provide the Government rights in trade secrets, e.g., confidential cost, pricing, operational or technical information.
- Government IP-related terms and conditions may transfer ownership of commercial companies' and 3rd party software used in performing the contract or agreement.
- The Government may require that all IP delivered to the Government be marked with expressly specified restrictive legends; failure to appropriately mark delivered IP can result in the Government obtaining unlimited or unrestricted rights in the IP.

B.

OUTLINE OF ISSUES TO CONSIDER FOR LICENSING TECHNOLOGY TO THE U.S. GOVERNMENT

A. Structure of the License

1. Amendment to Existing Government Contract:
 - a. Need to consider and address if and how existing contractual terms could affect the license (e.g., Technical Data Rights clauses that could affect the Government's rights to disclose confidential information provided as a part of licensed know-how).
2. Stand Alone Agreement with the Government
 - a. Will the Government sign a "commercial" license agreement? (Sometimes agencies are willing to do this.)
 - b. Will the Government insist on negotiating "special license rights" under the DFARS, and attach the license to a contract awarded for the purpose of developing/purchasing/maintaining technology?
 - c. Will the Government be willing to name the contractor as a third party beneficiary of any sublicenses granted to prime contractors to use the licensed technology for Government purposes?
3. License Agreement with each Prime Contractor, as needed.
 - a. Requires negotiating multiple licenses, often with large companies with strong leverage in negotiations.
 - b. Provides more control over the use of the technology by such contractors, including ability to audit more readily, sue directly for breaches of contract, etc. (Note, however, that the contractor would always have a direct cause of action against contractors for intellectual property infringement.)

B. What is Being Licensed?

1. Patents/Patent Applications?
2. Know-How (Confidential Information/Trade Secrets)?
3. Software (Copyrights/Trade Secrets/Perhaps Patents)?

C. Scope of the Licenses?

1. To Whom is the License Granted?
 - a. Directly to the Government? (or Prime Contractor?)
 - b. Government's (or Prime Contractor's) right to sublicense and/or distribute the technology?

- (1) Scope of sublicense rights? Government contractors only?
Other Government agencies?
- (2) Approval rights over sublicenses?
- (3) Duty of the Government to provide copies of the
sublicenses?

2. Rights Granted?

- a. Patent Rights: use, make, offer to sell, sell, import
- b. Copyright Rights: reproduce, distribute, create derivative works
(modify), publicly display, publicly perform
- c. Trade Secret Rights: use and disclose
- d. Other Rights? Bundling with other products/integrate, etc.

3. Limits on the Field of Use or Purpose?

4. Will the License Cover Improvements to Patented Inventions? Updates,
Enhancements or New Versions of Software?

- a. If so, when must improvements be disclosed?
- b. How is maintenance and support of software provided? (Will this
be addressed in the license or a stand alone maintenance
agreement?)

5. Other Limitations?

- a. U.S./Territory vs. Worldwide?
- b. Duration of the license?
- c. Revocable/Irrevocable?

D. Are There Any Deliverables That Must Be Provided? If so, what, when, and in what format? For example, will there be any software deliverables, and if so, will software be delivered in object code and/or source code forms? (Avoiding source code deliverables would give the contractor more control over the technology.) Would the contractor wish to specify acceptance procedures for such deliverables?

E. Fees and Payment

1. Fees:

- a. Upfront License Fees?
- b. Annual License Fees?
- c. Per Unit Royalties?
 - (1) Based on a percentage of sales price to the Government?
Fixed dollar amount per unit? etc. (Note: fixed dollar
amount per unit may be easier to address if the

Government will not permit extensive auditing of its records, which is often the case.)

- (2) If royalties are tied to a percentage of price/revenues, etc., will there be any minimum royalty?
- d. Government's duty to report royalties and maintain records?
- e. Payment of Royalties? Presumably, if the Government is the licensee, payment will be made by the Government directly, and not by its contractors.

F. Term of the Agreement?

G. Under What Circumstances May Either Party Terminate? (Note: in Government contracts, normally the Government is the only party that may terminate a contract. The contractor, however, should try to include a right to terminate for breach, including misuse of the intellectual property outside the scope of the licenses.)

1. Termination for Material Breach?
2. Termination Without Cause?
3. What are the Effects of Termination?
 - a. On the licenses?
 - b. On existing sublicenses?
 - c. On the payment obligations? (i.e., if existing sublicenses survive, then payment obligations associated with those sublicenses must also survive.)
 - d. Return of confidential information.
 - e. No further obligation to provide any improvements/enhancements, etc.

H. What Warranties and Indemnities, if any, is the Contractor Willing to Provide to the Government?

1. Intellectual Property Warranties/Indemnity?
2. Performance Warranties? (would apply only if deliverables of some sort are provided)

C.

GOVERNMENT CONTRACTS IP RELATED M&A DILIGENCE ISSUES

Key Considerations When Developing a Due Diligence Plan

Obtaining and analyzing meaningful data and information from the target is central to the due diligence review, but there is no one-size-fits-all due diligence plan for government contracts. The risks involved in government contracts M&A will vary in each transaction depending on the nature of the transaction (*e.g.*, whether it is a stock or asset purchase) and the circumstances related to the target's work that it is performing for the government. As a starting point, an acquiror should develop and tailor its due diligence plan based on the following factors and the answers to the questions posed under each factor:

- **Nature of the Products or Services Provided to the Federal Government**
 - Are the products being provided commercial off-the-shelf or are they modified for unique Government requirements?
 - Are the services being provided in support of the company's products or are they stand-alone services?
 - Are the intellectual property rights associated with the products or services important to the valuation of the company?
- **Type of Contracts With the Federal Government**
 - Are the Federal Government contracts or subcontracts commercial item contracts under FAR Part 12 or something else?
 - What types of Federal Government contracts or subcontracts does the company have (*e.g.*, fixed-price, cost reimbursement, time and materials)?
- **Intellectual Property Issues.** Rights in intellectual property often are a significant factor in the value of the target, and government rights in that intellectual property may substantially diminish the value of both the target's government and commercial business. Generally, the government obtains rights in intellectual property (which may include patentable inventions, computer software, technical data, and trade secrets) based upon the nature of the work performed and the product/service delivered under a contract. The rights obtained by the government in intellectual property generally depend on the extent to which the government paid for development of the intellectual property through the contract price. The rules applicable to the entire subject of intellectual property rights are complex, however, and protection of a contractor's interests in such data requires development of procedures and vigilance. Accordingly, review is needed of the target's files and contracts to assess the adequacy of the intellectual property procedures, and to assess the extent of the government's interest in the intellectual property, with a focus on the following:
 - Has the target documented a baseline of all its intellectual property that was developed at private expense?

- Does the target have a process in place to thoroughly document development work and track the source of funding (*e.g.*, at private expense or funded by the government)?
- Does the target have a system of recordkeeping that provides centralized control and preservation of records?
- Does the target have policies and procedures in place to ensure that contract and subcontract administrators review solicitations and terms and conditions related to the FAR IP clauses (*e.g.*, patents, authorization and consent, technical data rights, computer software, and related clauses)?
- Does the target have policies and procedures in place to ensure that the government obtains only the minimum rights it really needs?
- Does the target have policies and procedures for ensuring all proposals and deliverables provided to government customers are appropriately marked to protect the company's IP?
- Does the target have policies and procedures for identifying when government funded work may produce a "subject" invention (*e.g.*, requiring engineers and other personnel engaged in development work to track and record progress)?
- Does the target have policies and procedures for ensuring timely disclosure to the government of subject inventions?
- Does the target have policies and procedures for ensuring timely reporting to the government on subject inventions and on invention utilization as required by the FAR?
- Does the target have policies and procedures for ensuring timely election of patent rights and including appropriate legends in patent applications as required by the FAR?
- Does the target do any development work under CRADAs, grants, cooperative agreements, the Advanced Technology Program, or technology transfer programs for small businesses?