Patent Cost – Position of SBTC

# Introduction

There is considerable confusion within the small business community concerning allowability of patent costs associated with small business innovative research (SBIR) programs. Consequently, the Small Business Technology Council (SBTC) is seeking to clarify the allowability of these costs and establish guidelines for small businesses engaged in SBIR/STTR programs.

The SBTC is not advocating changes to the Federal Acquisition Regulations (FAR). The goal is to establish a clear and concise interpretation of how these regulations are applied to SBIR/STTR programs. This will provide guidance for small business contractors and government personnel reviewing financial performance.

# Purpose of SBIR program

The SBIR web site provides the following description of the program:

*The Small Business Innovation Research (SBIR) program is a highly competitive program that encourages domestic small businesses to engage in Federal Research/Research and Development (R/R&D) that has the potential for commercialization. Through a competitive awards-based program, SBIR enables small businesses to explore their technological potential and provides the incentive to profit from its commercialization. By including qualified small businesses in the nation's R&D arena, high-tech innovation is stimulated and the United States gains entrepreneurial spirit as it meets its specific research and development needs [1].*

A stated goal of the program is to “increase private-sector commercialization of innovations derived from Federal research and development funding.” A key requirement for commercialization is protection of intellectual property (IP). This is the role of the U.S. Patent Office, and SBIR contracts and grants include specific instructions related to the preparation and filing of patent applications

# Patent impact on commercialization

Given the stated purpose of the SBIR/STTR as defined by Congress, small businesses funded through the program have the responsibility to utilize technology developed to create commercial products or services. In most cases, this will require additional investment by the small business. Patent protection is necessary to protect both the government’s investment, as well as that of the small business.

# Implications of Leahy-Smith America Invents Act

The Leahy-Smith America Invents Actor (AIA) became law in September 2011 and represented a significant change to the U.S. patent system. The law switched patent rights from a first-to-invent” to a “first-to-file” system for applications filed after March 15, 2013. An article published in the Loyola Law Review concluded that the main unintended consequence is that big businesses, with massive financial resources, will be able to file patent applications faster than small businesses [2]. Under previous law, small businesses could wait until commerciablity of a technology was confirmed before incurring the expense associated with pursuing patent protection. With the emphasis now on “first-to-file” it is now incumbent for small businesses to seek patent protection as soon as a technology is developed rather than wait until a commercial market materializes. Unfortunately, commerciabilty of a technology may occur months or years after an SBIR/STTR program is completed. This is particularly true for “high risk” enabling technology, which allows development of additional technology to implement the concept, or component development where integration into a larger system is required for implementation.

In SBIR/STTR programs, technologies are investigated during the Phase I program and developed during the Phase II program. If the concept(s) is verified during the Phase II program, it is necessary for the small business to initiate patent protection to preserve both the small business’ and the governments interests. Since this adds value to the technology during the course of the program, it is SBTC’s contention that these should be allowable charges to the program.

# Regulations dealing with patent costs

DoD SBIR/STTR contracts reference the following FAR related to patents:

52.227-11 Patent Rights – Retention By The Contractor (Short Form) (June 1997)
252.227-7034 Patents—Subcontracts (APR 1984)
252.227-7039 Patents – Reporting of Subject Inventions (APR 1990)

DOE grants address patent issues under SBIR/STTR-GTC-0024 Patent Rights

 In order to abide by the intent of the SBIR program, it is incumbent upon the small business to protect IP developed in the program to successfully pursue commercialization. Should the small business pursue patent protection, then pursuant to FAR 52.227-11 c(3), the contractor is required to take action to file and prosecute the Government’s interest, including establishing the Government’s rights in subject inventions (52.227-11 e) and assigning appropriate government rights.

SBIR/STTER-GTC-0024 c(1) requires grantees to disclose subject inventions to the Patent Counsel within two months after the inventor discloses it in writing to grantee personnel responsible for patent matters. This is independent of whether or not the grantee elects to retain title. Additional actions are required by the contractor should a patent application be filed (SBIR/STTER-GTC-0024 c(3) and (f).

Both the U.S. Department of Energy and Department of Defense SBIR offices provide information concerning allowability of patent expenses. DOE does not allow direct charges for patent costs on Phase I programs; however, the contractor can charge up to $10,000 as direct costs to Phase II programs [3].

The DoD SBIR Desk Reference refers to the allowability of patent costs as described in FAR 31.205-30 [4], and describes how it can allowable as either direct or indirect costs. Under Special Contract Provisions, the reference indicates that “patent searches and applications may be included in the statements of work for Phase II contracts” and allowed as direct costs [4]. Alternatively, for the case where such work is not included in the workplan, the contractor may include these as indirect costs, as they benefit the contractor’s entire business organization, including the Government and industry contract activity as well as other commercial business.

# Recommendation for patent costs in SBIR programThe SBTC recommends that the Defense Contract Audit Agency provide advice and training to its auditors that patent costs related to SBIR/STTR subject inventions be allowable costs, generally treated as indirect costs unless the statement of work contains authorization for the direct charging of patent effort.

# References

1. <http://www.sbir.gov/about/about-sbir>
2. Y.M. Mattappally, “Comment: Goliath Beats David: Undoing the Leahy-Smith America Invents Act’s Harmful Effects on Small Businesses,” Loyola University New Orleans College of Law, Loyola Law Review, 58 Loy. L. Rev. 981, Winter 2012.
3. Manny Oliver, DOE SBIR/STTR Webinar: FY14 Phase I Release 1 Funding Announcement, August 16, 2013.
4. U.S. Department of Defense, Small Business Innovation Research Desk Reference for Contracting and Payment, <http://www.acq.osd.mil/osbp/sbir/sb/resources/Deskreference/index.shtml> , page 11, August 2013.
5. U.S. Department of Defense, Small Business Innovation Research Desk Reference for Contracting and Payment, <http://www.acq.osd.mil/osbp/sbir/sb/resources/Deskreference/index.shtml>, Section VIII, C. (D.), page 83, August 2013.