



Phase III Contracting Q&A

References:

SBIR Reauthorization Law; PL 112-81:

<http://www.gpo.gov/fdsys/pkg/PLAW-112publ81/pdf/PLAW-112publ81.pdf>

SBIR in the US Code; 15 USC 638 (Section 9 of US Small Business Act):

http://www.law.cornell.edu/uscode/pdf/uscode15/lii_usc_TI_15_CH_14A_SE_638.pdf

SBA 2012 SBIR Policy Directive:

<http://www.sbir.gov/about/sbir-policy-directive>

1. If a company wins a Phase I or Phase II SBIR, can the Government enter into a contract with the SBIR company to purchase or develop the SBIR technology?
 - a. Yes, not only *can* the Government do so, but follow-on SBIR contracts are also encouraged. The National Defense Authorization Act of 2012 contains the 2011 SBIR/STTR Reauthorization Act, and includes new language that indicates strong Congressional intent to improve the process of rapidly transitioning SBIR/STTR innovative technologies for insertion into DOD fielded systems and platforms. The law specifically states:

“Sec. 5108: To the **greatest extent practicable**, Federal agencies and Federal prime contractors ***shall*** issue Phase III awards relating to technology, including sole source awards, to the SBIR and STTR award recipients that developed the technology.”¹ [Emphasis added.] [Phase III is further defined as, see Sec. 5125 – “for work that derives from, extends, or completes efforts made under prior funding agreements under the SBIR program [and is funded by non-SBIR funds].”²]

This provision is the strongest statement to date that Congress is serious that agencies and prime contractors accord SBIR producers of a technology a preference for any Phase III follow-up work. The preference is a mandate, not an issue of discretion. Congress added the word "greatest" to the preference, and for the first time incorporated the preference into the statute in strong terms.

¹ 15 USC §638 (r)(4) Phase III Awards.

² 15 USC §638 (e)(4)(C).

2. Can an agency enter into a Phase III contract even if a different agency awarded the Phase I or II SBIR award?
 - a. Yes.³

3. May an agency enter into a Phase III contract as a sole source contract?
 - a. Yes, see Section 5108 that specifically authorized sole source awards to SBIR and STTR recipients. See also SBA's August 6, 2012 SBIR Policy Directive, (as amended on January 8, 2014), section 4(c)(3)⁴ which states:

“The competition for SBIR Phase I and Phase II awards satisfies any competition requirement of the Armed Services Procurement Act, the Federal Property and Administrative Services Act, and the Competition in Contracting Act. Therefore, an agency that wishes to fund an SBIR Phase III project is not required to conduct another competition in order to satisfy those statutory provisions. As a result, in conducting actions relative to a Phase III SBIR award, it is sufficient to state for purposes of a Justification and Approval pursuant to FAR 6.302-5, that the project is a SBIR Phase III award that is derived from, extends, or completes efforts made under prior SBIR funding agreements and is authorized under 10 U.S.C. 2304(b)(2) or 41 U.S.C. 3303(b).”
 - b. Agencies may issue sole source Phase III awards to the SBIR Phase I or Phase II awardee to meet these statutory and regulatory requirements. At times, agencies have failed to use this authority, by-passed the small business that created the technology, and pursued the Phase III work with another business. Congress has expressed, again, and now in stronger terms, **a clear intent for the agencies to accord a preference to the SBIR awardees that created the technology** so that these small businesses can commercialize the technology they created.⁵
 - c. However, note that even fully-competed government contracts or Prime subcontracts can also constitute SBIR Phase III awards if they meet the Phase III criteria: “ work that derives from, extends, or completes efforts made under prior funding agreements under the SBIR program [and are funded with non SBIR Program funds].”

4. Does the law require an agency award to award a phase III contract to the SBIR company that developed the technology?
 - a. No. The law requires that the agency (or agencies) provide a "preference" to the SBIR and STTR technology developer. The title of Section 5108 is “SBIR and STTR special acquisition preference”, and states: “To the greatest extent practicable, Federal agencies and Prime contractors shall issue Phase III awards relating to...SBIR and STTR Phase I or II awards.” The preference is legally required and sets a difficult path for an agency to bypass it. SBA has stated that the preference process consists of the agency determining whether or not the SBIR/STTR developing firm is: 1) available; and 2)

³ 15 USC §638 (bb)(1) Agency Flexibility.

⁴ SBA 2012 SBIR Policy Directive Section 4(c)(3)

⁵ 15 USC §638 (r)(4) Phase III Awards

capable of performing the requirement. Once these tests are met, a compelling case exists for the agency to make a sole-source award to the SBIR/STTR developer..

5. Does this preference apply to DOD prime contractors?
 - a. Yes. US Code 15 USC 638(r)(4) specifically states that to the greatest extent practicable Federal agencies and Federal prime contractor shall issue phase III awards relating to SBIR technology. The Directive at 4(c)(3) relating to the authorization to make sole-source awards also specifically references the Armed Services Procurement Act.⁶
6. Are there goals for agencies and prime contractor for transitioning SBIR and STTR technology into programs of record and fielded systems?
 - a. Yes, Section 5122(a)(7) of the SBIR reauthorization language provides that the Secretary of Defense shall establish goals for transitioning SBIR technology into Phase III.⁷
7. Are there incentives for agency program managers and prime contractors to use Phase III?
 - a. Yes. Section 5122(a)(7) of the SBIR reauthorization language provides that the Secretary of Defense use any incentive in existence at the enactment of the law or create any new incentive to encourage the transition SBIR technology.⁸
8. Has the Secretary of Defense established goals for SBIR Phase III?
 - a. As of April 2014, the DOD has not yet implemented goals.
9. Is it a problem for an agency if it doesn't use an SBIR technology that derives from, extends, or completes prior SBIR effort?
 - a. Yes. In fact, the Act requires at 638(b)(7)⁹ that SBA report to Congress all instances in which an agency pursues research, development, or production of a technology developed by an SBIR awardees, with a business concern or entity other than the one that developed the SBIR technology. The SBA policy Directive at section 4(c)(8) also requires agencies to notify SBA prior to award of such a funding agreement.¹⁰ SBA will report such instances, including those discovered independently by SBA, to Congress.
 - b. If an agency refuses to acknowledge that a requirement is a Phase III, first attempt to persuade the agency that it is. Develop a "side by side" comparison of prior SBIR research (SBIR proposals and contracts or funding agreements) with the requirement. Compare functionalities, metrics, language and other similarities. Show this to the agency. Once the Phase III status is established, the rest of the SBIR rights, including the preference, follow by law. It is this document, in addition to a persuasive paper arguing the case, that will become part of the appeal of the case (see below).

⁶ 15 USC §638 (r)(4) Phase III Awards

⁷ 15 USC §638 (y)(5)(A)

⁸ 15 USC §638 (y)(5)(B)

⁹ 15 USC §638 (b)(7)

¹⁰ SBA 2012 SBIR Policy Directive 4(c)(8)

- c. Agencies, their Government-owned, contractor-operated facilities, or Federally-funded research and development centers, that intend to pursue R/R&D, production, services, or any combination thereof of a technology developed under an SBIR award, with an entity other than that SBIR awardee, must notify SBA in writing prior to such an award. This notification must include, at a minimum:
 - i. The reasons why the follow-on funding agreement with the SBIR awardee is not practicable;
 - ii. The identity of the entity with which the agency intends to make an award to perform research, development, or production.
10. If an agency decides to award a contract for SBIR technology to a different company can an SBIR company object?
- a. Yes, SBA may appeal an agency decision to pursue Phase III work with a business concern other than the SBIR awardee that developed the technology to the head of the contracting activity within 5 days.¹¹ Only then can an agency proceed to make an award to the non-SBIR company.
 - b. That said, it is advisable to object to the agency as soon as possible, preferably before award of the technology to another firm, and make the case that this is a Phase III and must be afforded preference rights. If an agency threatens to compete a Phase III requirement, letters to and meetings with the agency are preferable to waiting until an award is made to other than the SBIR/STTR firm. Protests of solicitations that constitute a Phase III could be considered. Protests of a solicitation must be brought to GAO no later than the time and date bids are due, and to the Court of Federal Claims no later than the same time and date.
11. What should an SBIR winner do if an agency or Prime contractor should be using SBIR technology and is not sourcing it from the SBIR winner?
- a. You would presumably have to prove that the technology derives from, extends, or completes prior SBIR work. Then, help them understand this and understand the appropriateness therefore of your claim. Work with the Prime and the government technical point of contact and the SBIR program office. If that does not work, notify them that you plan on going to SBA with the situation. Submit a clear and detailed statement showing that the technology developed under your SBIR awards, that it was “for work that derives from, extends, or completes efforts made under prior funding agreements under the SBIR program” Section 5125.

¹¹ SBA 2012 SBIR Policy Directive 4(c)(8)(iii)

12. Why don't agencies use SBIR Phase III awards more often?

- a. First, the contracting officers and program managers are not aware of the law. Many contracting officers and program managers have not been trained on the use of SBIR technology. Second, the goals and incentives for using SBIR Phase III have not been issued by the Secretary of Defense. Third, SBA has not codified the Directive, which has the force of law, into the Code of Federal Regulations. Thus, this law exists as a free-standing document about which a great many contracting officials are ignorant. The FAR, DFARS, other agency FAR supplements, and some program manuals have not been updated to reflect the Phase III laws. Fourth, many agency officials do not want the restrictions that come with SBIR data rights. Contracting officials are taught that competition lowers costs, and sole-source contracts, and SBIR rights and obligations not to disclose SBIR DATA, and thus, an inability to compete it, run counter to these ingrained principles. Once agency officials become aware of the provisions of the SBIR reauthorization, they may be more inclined to comply with the law..

13. Should SBIR Data Rights (inclusion of DFARS 252.227-7018 clause) be granted to all Phase III contracts awarded by government and prime contractors? Yes.

- a. How does a prime contractor include the SBIR clause in a subcontract to a small business?

This is done by "insertion" of the clause into the subcontract, not flowing it down, since the large firm will not have the SBIR clause in its prime contract. This is a common hang-up and misconception for large firm lawyers.

- b. Is there a requirement to do so since the prime may argue that it has to deliver to the government with unlimited rights?

The answer to this is "Yes," the law requires the SBIR clause in the subcontract. Section 4(c)(2) of the Directive states that a Phase III is in essence an SBIR contract, and must be accorded all SBIR rights, including SBIR data rights. The most recent version of the Directive added several provisions that reiterate that a Phase III can be a subcontract and a subcontract can be a Phase III. This was always the case, but now the Directive states this expressly.

- c. A DOD Agency or Prime may not in any way make issuance of an SBIR award, including a Phase III, conditional on giving up or diminishing SBIR data rights.¹²

¹² 15 USC §638(ee)(2)(C)

14. Who has rights and title (ownership) to the technology developed under SBIR Phase I, II, and III contracts?

a. What are the government rights in the technology?

The small business owns the technical data generated under an SBIR contract and the government receives a royalty-free license to use it. The Government's right to use is limited and does not include authorization of others (e.g. Primes) to use on Government's behalf. The stated preference in SBIR legislation is for the small business company to use the data on the government's behalf.

b. What is meant by the fact that the government can disclose SBIR Data to support government contractors, and for what purposes?

This applies only to government support contractors. A true support contractor is one that has signed a nondisclosure agreement consistent with the DFARS, and has an organizational conflict of interest provision in its contract for support prohibiting that contractor from bidding on any contract involving that data or technology. The terms "on-site" contractor is not a good substitute for the term "support contractor," since many outside (non-support contractors) have people who work on-site at federal agencies.

15. Can an SBIR technology be licensed or sold to a prime contractor, e.g. for production for prime contractor purposes?

a. Yes. Lines of SBIR technology can be sold as assets or licensed to the Prime. These sales may transfer SBIR rights to the prime contractor.

b. Would licensing costs incurred by a prime contractor be allowable by the government?

Yes. Licensing costs can be recovered by the prime contractor. While at times certain government representatives may assert (or feel) that they have paid for the SBIR technology, in fact, that has not actually occurred (see 14b).¹³

i. While the government has a royalty-free use right to SBIR data *itself*, it does not have the right to have the prime contractor use that information even for the government's purpose. This is enforced by the fact that the Government cannot even disclose SBIR Data to any outside source, including a prime contractor. In fact the preference clauses in SBIR indicate the SBC should be the one to use it for the government's benefit. For the government to get the benefit that the prime is to use it in place of the SBC, there is a basis for a license for the prime's

¹³ In addition to costs being allowable, costs charged to Government need to be reasonable. While the agreed upon sales/licensing costs is a private matter between Prime and SBC, there is a third party that determines whether costs are reasonable, i.e. the Government. Products are sold by the prime to the Government with a certain profit or fee. Part of such product may constitute SBIR/STTR technologies belonging to one or more SBIR Small Business Concerns (SBC). As a guideline, it is reasonable if the SBC receives a percentage of such fee (or profit) that is commensurate with the share of their product/part in the overall system. This would introduce the notion of profit sharing between large and small business, as is very common in STTR Allocation of Rights agreements and patent licensing agreements. This would be similar to the SBC manufacturing the part (or have it manufactured) and sell it to the prime with a fee.

use even though on the government's behalf. The government has no right to data not generated under the SBIR contract that was developed at private expense. Most SBIR technologies will contain a mix of data developed under SBIR awards and changed, updated or otherwise developed between or subsequent to such awards. A practical option for some may be to include reference to such data also in a license, simplifying the justification for the Prime and government.