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THE WHITE HOUSE

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PATENT BRANCH, OGC
DHEW

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MEMORANDUM FOR THE PRESIDENT

From: Stu Eizenstat
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Subject: Administration Position on H.R. 6249 Concerning FEDERAL PATENT POLICY

BACKGROUND

Statement of the Issue

The Federal Government does not have a uniform patent policy, and maintaining the status quo does not provide for an efficient Government.

H.R. 6249 is the culimination of years of discussion, agency operating experiences, and is based on the work product of the interagency Committee on Government Patent Policy. The bill also follows the basic concepts of Recommendations 1 and 2 of Part I of Volume IV of the December 1972 bipartisan report of the Commission on Government Procurement.

The major issue in H.R. 6249 is the provision covering the allocation of rights to inventions made by contractors under research and development (R&D) funded by the Federal Government.

This issue has been debated by Congress, Industry, the Executive Branch and others for approximately thirty years. H.R. 6249 seeks a compromise solution to this long debated issue. Proponents of the bill believe that its passage would provide uniformity among the twenty R&D agencies, and greatly simplify the interface between the Federal Government and its many contractors and grantees, which presently approximates 30,000 R&D transactions annually.

The debates and Congressional hearings on this evolving policy issue have produced an entanglement of policies and a myriad of complex implementing regulations. Currently, the Federal agencies must adhere to the provisions of 19 statutes and the criteria of

the 1971 Presidential Memorandum and Statement of Government Patent Policy, which H.R. 6249 would repeal or supplant. [In addition, H.R. 6249 would supplant three Executive Orders concerned with the allocation of rights to inventions made by Federal employees and Federal foreign licensing activities.]

It is certain that this controversial issue will not be resolved without the concerted efforts of the Congress and the Administration. Congressman Ray Thornton initiated action to resolve the controversy with the introduction of H.R. 6249, briefly described below, and will need the Administration's support on his proposal or an acceptable modification thereof, if the debate is not to continue for many more years.

Brief Desecription of H.R. 6249

The primary purpose of H.R. 6249 is to establish a uniform Federal system for management, protection, and utilization of the results of Federally sponsored scientific and technological research and development, and to further the public interest of the United States domestically and abroad. The bill contains five titles which are briefly described below.

Title I merely sets forth the findings and declaration of purpose of the bill, and is not controversial.

Title II, also non-controversial, assigns advisory functions to OSTP and FCCSET to assure uniform implementation of the patent policy provisions and the development of policy in other areas of intellectual property such as rights in technical data, copyrights, etc.

Title III provides criteria for allocating property rights to inventions which result from Federally-sponsored research.

Chapter 1 of Title III is controversial and establishes criteria for allocating such invention rights between the Federal Government and the contractor. See Option 4 below for a more complete discussion of the public safeguards and Government rights which this chapter provides.

Chapter 2 covers inventions made by Federal employees and is an effort to codify the criteria of Executive Order 10096 issued by President Truman, and does not present real controversial matters. TVA, NSF, and ERDA presently are not required to follow the criteria of this Order.

Title IV provides all Federal agencies authority to protect (patent) Federally-owned inventions both domestically and abroad, and to license (both nonexclusively and exclusively) such inventions. Inasmuch as similar authority has already been provided ERDA and NASA to provide for effectual transfer of technology owned by the Government, this title is not considered controversial.

Title V contains three chapters, none of which contains controversial subject matter.

ANALYSIS

General

More often than not, before an invention reaches the marketplace and is made available for use by the public, it usually first requires additional development and marketing following the termination of the Federal contract. The discovery of penicillin and the fact that its production was open to all drug manufacturers did not assure its use to the public and to the war effort of World War II. To obtain its further development and production, it was necessary for the Federal Government to invest 20 million dollars in plant facilities. What happened in the case of penicillin normally does not occur under the existing R&D practices of the United States. Rather, private enterprise is expected to invest its own capital to further develop and market products for use by the public. Often this cost is 10 to 100 times the cost expended in conceiving or making the invention. The patent system assists in the effort of achieving commercialization by providing exclusive rights to entrepreneurs to invest, develop and market an invention, and hopefully, permits the entrepreneurs to recoup the investment prior to the expiration of the exclusive period provided by the patent.

Federal Patent Policy

Most authorities concerned with Federal patent policy agree that the policy should:

(1) meet the needs of the Federal Government. [The license to the Government for its own use is sufficient for this purpose.];

(2) take into consideration the equities of the contractor. [Normally, this can not occur when the Government acquires title to an invention and the contractor is immediately placed in the same situation as his competitors. For Fiscal Year 1975, only 235 companies

of the total of 1,133 companies performing R&D which have more than 1,000 employees performed Federal R&D. Of the 10,000 companies having less than 1,000 employees, even a smaller percent allegedly perform Federal R&D.];

(3) serve the public interests. [To serve such interests, an invention (first) must be conceived, (second), timely produced, and (third) made available at reasonable prices.]; and

add disclosure to ensure patenting.

(4) reduce the administrative burdens for both the Government and its contractors. [Contractor requests for waiver of title and the resultant often lengthy negotiations by the Federal agency, as well as seemingly unnecessary Federal licensing activities contribute to the administrative burden for both parties to the R&D contract. Such burdens lead to unnecessary overhead costs for the company and the Federal Government, and accordingly, do not serve the public interests, especially if they are counter-productive to early utilization of resulting inventions.].

This is one-sided and unacceptable.

OPTIONS

Five major options for allocating contractor invention rights and a brief discussion are set forth below.

<u>Option 1.</u> - Current policy of USDA, Postal Service, DOI, AEC(ERDA) and FHA(DOT) imposed by statute.

Federal Government acquires title to inventions made under Federally sponsored research and development contracts and grants, with the contractor retaining a nonexclusive license, revocable only if the Federal agency must issue an exclusive license to obtain further development and marketing of the invention under its licensing program.

<u>Discussion</u>

All of the statutes which provide for Option 1, except for the Postal Service, were enacted many years ago. As Congress debated the issue, and the Executive Branch issued more flexible policies, the concept of waiving title, under certain identified criteria, to the contractors developed. The strict title policy of Option 1 is therefore considered outmoded.

Option 2. - Current policy of NASA and ERDA imposed by statute. In addition, policy is followed by EPA and DOT for certain of their R&D programs, also imposed by statute.

Federal Government acquires title to all inventions, except where the contracting Federal agency waives title to the contractor after considering specified criteria to (i) facilitate early development and marketing of resulting inventions, (ii) obtain the participation of the best qualified contractors to perform the R&D for the agency, or (iii) otherwise serve the public interests.

Discussion

The policy of Option 2 constitutes the most recent expression of the Congress in providing statutory guidance to a major R&D Federal agency - namely, to ERDA in December 1974. While the criteria for waiving title to the contractor are specified, such criteria are applied on a case by case basis and may be liberally or strictly interpreted in accordance with philosophy and background of the Administrator or his designee. Option 2, therefore, negates any degree of uniformity. In addition, if this option were applied Government-wide, using available statistics, the administrative burdens could entail up to 30,000 advanced waiver requests, or 7,000 requests for waiver after the inventions are identified. Also, once waiver is granted, the contractor retains title (exclusive rights) for the full 17 year life of the patent. The current practices of NASA provide contractor waivers in almost 100% of the cases where the contractor is willing to invest capital to obtain its expeditious utilization. Under a liberal waiver policy - Option 2 may be considered more of a "giveaway" than Option 3, 4 or 5.

and hence is in conflict with 5 above.

As a result of the 1974 legislation, ERDA presently operates under the old AEC patent provisions, the new ERDA patent provisions, and the amendment to the Federal Procurement Regulations which implements the 1971 Presidential Patent Policy Statement. The resultant implementing regulations makes it difficult for the uninitiated to serve their employers.

Option 3. - Current policy of DOD, HEW, DOJ, NSF, VA, FCC, DOC, EPA, ACDA, HUD, Treasury, TVA, DOT, CIA, [The policy also is required to the R&D programs of USDA, AEC(ERDA) and DOI not covered by statute.] imposed by the 1971 Presidential Patent Policy Statement.

Federal Government either acquires title, waives title or defers allocation of rights question until an invention is identified. R&D categories for normal title acquisiton are defined specifically (waiver, however, may be provided for these categories). When these specified R&D categories are not present and the contractor has a nongovernmental commercial position, the contractor may retain title. In other cases, allocation of rights are deferred.

Discussion

The 1971 Presidential Statement on Government Patent Policy is followed by all agencies, which are not required to follow differing statutory criteria. As with Option 2, option 3 ~~provides a Government of men - not of laws.~~ Congress has always been aware of the 1971 Statement and its predecessor, the 1963 Statement, yet continued to legislate.

In addition, while there are only 19 statutes today, Congress may attach additional patent policy riders to bills in the future. Already, DOI and EPA must follow the patent provisions of ERDA in two of their programs, requiring two sets of regulations and implementing procedures.

Option 4. - Policy set forth in Chapter I of Title III of H.R. 6249

The Federal Government acquires title to all inventions where the contractor does not file a patent application, with a license to the contractor - very similar to Option 1.

Where the contractor files a patent application and declares his intent to further develop and market (commercialize) the invention, the contractor retains title to such inventions, with the Government acquiring the following rights:

(a) the right to a paid up, royalty free, nonexclusive license
 - (i) for its own use; and
 - (ii) where appropriate, the right to sublicense
   - (A) state and local governments, and
   - (B) foreign governments;

(b) the right to obtain reports from the contractor on the commercial use of the invention;

(c) the right to require the contractor to license responsible applicants, or to grant such a license itself if the contractor refuses, where the Federal agency determines that the contractor is not taking steps to expeditiously commercialize the invention;

(d) the right to require the contractor [applicable even when the invention has been commercialized by the contractor] to license responsible applicants, or to grant such a license itself if the contractor refuses, where such action is necessary:

(i) to alleviate health or safety needs;

(ii) to meet requirements for public use specified by Federal regulations which are not being satisfied by the contractor; and

(iii) because the contractor's exclusive rights have tended substantially to lessen competition or to result in an undue market concentration; and

(e) the right to require the contractor to license responsible applicants, or to grant such a license itself if the contractor refuses, ten years after making the invention or seven years after commercializing the invention, whichever comes first. [This right of the Federal Government, applicable only against large companies or big businesses, effectively reduces the 17-year period of exclusivity, provided by the patent, to approximately a five year period. Where the contractor is a small business firm, this right of the Government does not apply.]

Discussion

The policy of Option 4 establishes a Government of laws, not of men. Uniformity is assured. Administrative burdens are kept to a minimum. Contractor participation and the making of inventions and their utilization is enhanced. Competition following the seven year period is assured inasmuch as the large companies are required to license their competitors after 7 years of exclusivily practicing the invention.

X Except for the additional rights provided small business firms, the only ~~so-called "giveaway"~~ in Option 4 is the exclusive period retained by the contractor ~~commencing~~ ending ten years from the date the invention was made or seven years after first public use or on sale (commercialization) in the United States, whichever occurs first. The 10 and 7 year periods have been chosen since they reflected the normal time frame for a commercialized invention to return sufficient profits to permit recoupment of the contractor's investment. Shortening these periods to 7 and 5, or 5 and 3, year periods would further reduce the so-called "giveaway". However, to do so would probably raise the number of times contractors request an extension of this period to permit them to recoup their investment.

From a statistical point of view, the allocation of rights breakdown resulting from all Federal agencies operating under the policy would be as follows:

(1) With respect to title acquisition by the Government in all cases where the contractor does not file a patent application --- using current statistics, of a total of 7,000 inventions reported annually, the Government would acquire title to 6,000 inventions and contractors would retain title to 1,000; and

(2) With respect to title retention by the contractor in all cases where contractor files patent application and declares his intent to commercialize the invention --- [Unless a small business firm, the contractor must license others 10 years after making the invention or 7 years after placing the invention in the marketplace, whichever occurs first. In addition, all contractors must license patents if not commercialized.] Using current statistics, of the 1,000 patents on which the contractors would retain title, 800 of them will be available to competitors because of nonutilization. Therefore, exclusive rights would be retained, in effect, by the contractor in only 200 cases annually, and then for a limited period. These 200 would, of course, presumably be the most valuable ones of the original 7000.

In conclusion, Option 4 provides the contractor with additional incentives to participate in Federally sponsored R&D contracts, make inventions, and enhance their utilization. Furthermore, inasmuch as Option 4 provides the maximum uniformity and drastically reduces the administrative burdens for both the contractors and the Federal agencies, it is favored by a large proportion of Federal contractors and grantees. It does, however, still treat government financed inventions differently from privately financed inventions.

Option ~~5~~ 6. - Option ~~5~~ 6 is a variation of Option 4.

Federal Government acquires title to inventions made under Federally sponsored research and development contracts and grants, with the contractor retaining an exclusive license for a specified period of time to induce early development and marketing. After the contractor's exclusive period, the invention is made available to all interested licensees under the Government's licensing program.

Discussion

The policy of Option ~~5~~ 6 appears to involve the Federal Government unnecessarily, and does not permit prospective licensees, following the contractor's period of exclusivity, to obtain a true license package from the contractor. Such a package might include know-how, background patent rights, and counseling by the inventor - important features not always available from the Federal Government under its licensing program.

Instead, under this option, the Government normally is in a position to grant a license only to the naked patent. When the contractor owns title, as in Option 4, and is required to license - the licensee can obtain these important items in a true license package.

Option 5 is favored by a few uniformity advocates who believe title acquisition by the Government will refute the "giveaway" arguments possible under Option 4. Others argue that the period of exclusivity guaranteed the contractor by the retention of the exclusive license makes this option in terms of a "giveaway" equivalent to Option 4.

RECOMMENDATIONS AND DECISION

/_/ Option 1. - Dated and outmoded statutory authority.
Favored by Postal Service.

/_/ Option 2. - NASA and ERDA Policy.
Favored by Admiral Rickover. [The DOJ suggests maintaining the status quo; namely, to continue to operate under Options 1, 2, and 3, with a view of conducting further studies, especially as they relate to the experiences of ERDA. Otherwise, DOJ tends to bend toward Option 2.]

/_/ Option 3. - 1971 Presidential Statement on Government Patent Policy
Favored by TVA for its own programs, but is not opposed to H.R. 6249 being applicable to other Federal agencies. It is noted that if Option 4 were law, TVA could continue its present practices regarding patents without change.

/_/ Option 4. - H.R. 6249
Subject to minor substantive revisions, favored by DOD, HEW, NSF, VA, FCC, DOC, USDA, DOJ, DOT, NASA, EPA, ACDA, HUD, Treasury and CIA.

Favored by majority of industry, as well as universities and nonprofit institutions.

If the memorandum is signed, OFPP, OSTP, OMB and the Domestic Council probably should be added here.

/_/ opt 5

/_/ Option 6. - Modification of H.R. 6249
Favored by

[Query? Inasmuch as Option 5 is not favored by anyone at this time, should it be dropped from the memorandum?]