UNITED STATES DEPARTMENT OF COMMERCE
Associate Under Secretary for
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Washington, D.C. 20230
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23 MAY 1988

Honorable Robert Bedell
Administrator for Federal
Procurement Policy
Office of Management and Budget
Washington, D.C. 20503

Dear Mr. Bedell:

The Department of Commerce has found at least three situations in which the Department of Energy has erroneously denied nonprofit contractors their right under Section 202(a) of Title 35, United States Code, to elect to take ownership of inventions made under federal funding arrangements. In each case, DOE claims that "exceptional circumstances" exist within the meaning of that section which justify an allocation of patent rights to the Government. DOE's determinations are questionable on several grounds:

- DOE's determinations are based in large measure on the need to prevent nuclear proliferation. In practice, any legitimate interest which DOE may have in controlling nuclear proliferation can be served through existing invention screening procedures and does not justify denying nonprofit and small business contractors their right to elect to own federally-financed inventions.

- DOE uses exceptional circumstance determinations under Section 202(a)(ii) as a means of preventing commercialization of certain technologies. Such determinations should be used to deny contractors their right of election only when the Government itself plans to fully fund and promote an invention or to bring about its commercialization through actions that do not rely on patent incentives, such as requiring its use through regulation.

The Department of Commerce has broad responsibilities under Chapter 38 of Title 35 for ensuring the proper implementation of federal patent policy, including that of precribing uniform regulations and patent clauses. It is also responsible under Section 202(b)(1) of Title 35 for (i) advising you whenever the Department believes that an agency has made improper exceptional circumstance determinations and (ii) recommending corrective action. Pursuant to Section 202(b)(2), you are authorized to issue regulations describing classes of situations in which exceptional circumstance determinations may not be made. Guidelines for a suggested regulation are contained below.

Under the provisions of Section 202(a) of Title 35, nonprofit organizations and small businesses may elect to retain title to inventions which they conceived or first reduced to practice under a federal funding agreement if they make their election within a reasonable time after disclosing the invention to the agency. The agreement may provide for an allocation of rights to the Government in "exceptional circumstances" when an agency determines that the purposes of Chapter 38 of Title 35 would be better served by restricting or eliminating the contractor's right to elect to take title. Such determinations are to be forwarded to the Secretary of Commerce within thirty days of the award of the applicable funding agreement (35 USC 202(b)(1)).[1]

DOE's contracts for the operation of its laboratories typically require the contractor to assign to the Government all rights to inventions in a technical field or task with respect to which DOE determines that "exceptional circumstances" exist. If an invention occurs within such a field, it is known as an "Exceptional Circumstances Subject Invention" and title goes to the Government unless the contractor obtains a waiver thereof from DOE.

As should be immediately apparent, the more broadly one describes a technical field (e.g., "technologies subject to export regulations"), the more inventions are swept in; the more inventions that are swept in, the more often the contractor must seek a waiver. The net effect is a reversion to the old approach of case-by-case waivers that the right of election was designed to supplant.

By requiring the contractor to seek a waiver in the case of any invention in a broadly defined technical field, a federal agency can effectively shift its burden of justifying why an invention should not go to the contractor onto the contractor to justify why it should. Contractors then have to consider their overall relationship with the agency, may then conclude that it is not worth jeopardizing that relationship, and the result is to leave title to the invention with the Government by default. The "right of election" can, under such circumstances, become illusory.

Accordingly, if the "right of election" is to have any meaning, technical fields must be defined with precision, be narrowly tailored, and the existence of exceptional circumstances surrounding that field must be clearly demonstrated. In at least three instances, DOE has failed to demonstrate adequately the existence of exceptional circumstances.

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[1]. The Department has no record of having received any of the funding agreements in question.

One of these pertains to DOE's uranium enrichment program (Tab A). A second pertains to its civilian high-level nuclear waste and spent nuclear fuel storage and disposal program (Tab B). The third (Tab C) would have allocated rights to the government in the case of any technology which is subject to classification, which is sensitive under Section 148 of the Atomic Energy Act, or which is subject to export control under DoD Directive 5230.25, but DOE, recognizing the overreach of this approach, replaced the reference to the DoD Directive with a reference to that part of the Critical Technologies List devoted to nuclear-related technology associated with the production and use of nuclear fission or fusion energy for both peaceful and military applications (Tab D).

Such uses of the Critical Technologies List to take inventions from university contractors would have serious economic consequences. For example, under the original DOE proposal important discoveries such as monolclonal antibodies used in the detection of Sickle Cell Anemia and cancer would be taken as "exceptional circumstances" inventions by DOE. Even under DOE's subsequent narrowing of the Critical Technologies List, inventions related to high-field superconductors would be owned by DOE -- not the contractor. Such attempted uses of "exceptional circumstances" by agencies fundamentally undermines the law.

A central theme running through each of these determinations is that Section 202(a)(ii) of Title 35 constitutes a basis for allocating ownership rights to the government as a means of discouraging or limiting the commercialization of federally funded research. That is, DOE's view is that if a good case can be made that a technology should not be commercialized for public policy reasons, the best way to achieve that will generally be to assert ownership rights.

Thus, the uranium enrichment determination is based on the proposition that "for public policy reasons such as nuclear proliferation, the technology is considered too sensitive to be utilized with private sector ownership." The Waste/Spent Fuel Determination is based on the idea that it is not yet "desirable ...to have industry commercialize the technology." The initial Classified/Sensitive Technologies Determination states that "(i)nventions covered by this exceptional circumstances determination are inherently inventions in which it is in the public interest to <u>discourage</u> commercial utilization" (emphasis in original). The appeal limited the scope of the latter but not the principle that "exceptional circumstance" determinations were useful tools for preventing commercialization of certain technologies.

We are not, in this action, challenging the principle that it is important to control nuclear proliferation or that to do so, the commercialization of certain carefully defined technologies may

have to be discouraged or limited. Rather, we are challenging (i) DOE's view that is generally necessary to allocate invention rights to the government to achieve this end, and (ii) that Section 202a(ii) provides a justification for taking ownership rights for purpose of retarding the commercialization of any technology. Authority for that purpose must be found elsewhere.

Turning first to the question of the necessity of allocating rights to the government versus the contractor, we would begin by noting that this is not the first time OMB has considered the relationship of invention rights to the protection of legitimate national interests. At Tab E you will find a copy of a memorandum from Mr. Alton G. Keel, Jr., formerly OMB's Associate Director for National Security and International Affairs, dismissing DOE's argument that federal policy on ownership of patent rights affects its ability to protect national security interests. As Mr. Keel explained, there are procedures to ensure that inventions affecting national security are properly screened and if these procedures are inadequate, that is where the problem lies. In Mr. Keel's words:

> "Government policy on ownership of patent rights does not affect its ability to prevent disclosure of patent applications for reasons of national security regardless of the source of research funds. Where research is done under Government auspices, particularly research expected to have national security implications, both the funding agencies and the performing organizations have the responsibility of ensuring that the work is conducted under the appropriate security conditions. If patentable technologies result from that research, the PTO national security screening process takes over. As part of that process, the funding agencies inform the PTO about potentially classifiable technologies."

These same procedures (see 35 U.S.C. 181 et seq.) are applicable to DOE and the interests which it is charged with protecting. Unless OMB no longer subscribes to Mr. Keel's view or can distinguish between ownership as a means of protecting security interests and ownership as a means of protecting nonproliferation objectives, the reasoning in Mr. Keel's memorandum should be dispositive of the present issue.

DOE's opinion at Tab D, on the other hand, asserts that ownership is necessary, but does not explain why. What DOE is in effect trying to do - and what Mr. Keel evidently recognized - is free itself from the obligation of defining its interests with precision and reviewing individual inventions to see how its interests are affected. Instead, it wants to get around the burden of classification by simply asserting ownership in as many fields of technology as it can, shifting the burden to the contractor to argue that commercialization should be allowed to proceed in a given case.

In other words, protection of nonproliferation interests should be accomplished the same way national security interests are protected: review the invention and place a secrecy order on it if appropriate to do so. DOE's practice of telling contractors that anything they invent across a whole range of areas will go to the government unless they are willing to go through a laborious and time-consuming process of trying to convince the Government otherwise can only reduce the incentives for inventing and reporting the same in the first place, thus retarding the development and commercialization of new technologies while achieving little, if anything, of positive value.

Particularly ironic is DOE's attempt to achieve this result by transforming a statute that is intended to promote the commercialization of federally funded research into a new authority for controlling sensitive technology without having to classify it, something it was never intended to be.

Chapter 38 of Title 35, which aims at promoting the commercialization of federally funded technologies by giving universities and small businesses the right to own inventions made under federal contract, was enacted after many years of Congressional disappointment that so few of the inventions owned by the government were ever commercialized. It recognized that the best way to achieve commercialization of federally funded inventions is to leave the invention in the hands of the people who understood it best (i.e., generally the contractor who developed it) and to ensure that they have the proper incentives to bring it to the marketplace, which will generally be ownership. Accordingly, it gave universities and small businesses the right to elect to take ownership of inventions made by them under federal financing, a principle which President Reagan subsequently directed them to extend to inventions made by other contractors as well.

Section 202(a) creates four bases for the government to to deny contractors the right to take ownership. One of these, the one at issue here, authorizes the Government to deny the contractor the right to take ownership "in exceptional circumstances when it is determined by the agency that restriction or elimination of the right to retain title to any subject invention will better promote the policy and objectives of this chapter."

The policy and objective of the chapter is to promote commercialization. The plain meaning of the language is clear: ownership rights do not have to go to the contractor if, in an exceptional case, there is a better way to get the invention commercialized. As Senate Report 96-480 (Tab F), accompanying S. 414, explained at pages 32-33:

> "It is expected that the "exceptional circumstances" exception will be used sparingly. An example of a situation in which it might be used is when the funding agreement calls for a specific product that will be required to be used by regulation. In such a case, it is presumed that patent incentives will not be required to bring the product to the market.
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> "Similarly, if the funding agreement calls for developmental work on a product or process that the agency plans to fully fund and promote to the marketplace, then use of this exception might be justified...." (emphasis added).

Clearly, the intent of the exceptional circumstances provision is to ensure that the right of election does not itself become a device for retarding commercialization. It is designed to foster commercialization by allowing the Government to allocate title to itself in support of its own efforts to bring the invention to the marketplace or because development of a market will be accomplished without recourse to patent incentives. Its use as a means of retarding commercialization should be rejected.

In what is perhaps the most strained and dubious argument of all, DOE justifies its actions on the grounds that the House Report accompanying H.R. 5003, a predecessor bill to Public Law 98-620, made it clear that certain of its programs were viewed as "exceptional circumstances."

A copy of the House Report on which DOE relies is attached at Tab G. As you will note, Title III of H.R. 5003, to which the DOE-cited report language pertains, would have created a special set of rules for contractors other than nonprofit contractors and small businesses. It would have permitted an agency to retain title when it "determines, on a case-by-case basis, that there are exceptional circumstances" thus avoiding the requirement that the circumstances be those which "better promote the policy and objectives of this chapter." The "better promote" requirement would have continued to apply to nonprofits and small businesses. Most important of all, it refers to language that was never enacted into law. In other words, DOE has justified its position by using a Congressional explanation of a proposal that was never enacted; that even if enacted would not have applied to nonprofit and small business contractors; and that if enacted would have used very different language for the class of contractors it would have covered.

Moreover, it is difficult to believe that Congress would have been careful in limiting the security (Section 202(a)(iii)) and weapons-related (Section 202(a)(iv)) bases for allocating rights to the government with such precision, while allowing Section 202a(ii) to become a catch-all, which is the practical effect of DOE's interpretation.

Finally, we are mystified by DOE's assertion at Tab A that the General Accounting Office "endorses" its reasoning that its exceptional circumstance determination is justifiable in order to promote future commercialization by avoiding "fragmentation of rights." Enclosed at Tab H are the relevant portions of the cited GAO Report which are applicable to DOE's determinations. DOE is certainly correct in that GAO acknowledges the possibility that to transfer technology to the marketplace an agency may have to transfer rights to an entire process. However, GAO's report (1) dismisses this argument as a justification for taking rights when there is really no intention to commercialize, and (2) notes that even if commercialization is the objective, an agency has an obligation to carve out appropriate fields of use (see Tab H, particularly pages 7-10 and pages 10-11 marked "Appendix I" at the top).

In simple terms, GAO refused to allow DOE to use procommercialization language to hide what was really its anticommercialization intentions.

In short, DOE has converted a statute aimed at promoting the commercialization of federally funded research into a basis for limiting the commercialization of nonclassified technologies. It is using Chapter 38 to free itself of the safeguards of the invention screening/classification process. It is shifting the burden, which it should bear, of justifying why commercialization of a particular invention should be limited to the contractor to explain why commercialization should be allowed to proceed. It is misreading legislative history and relevant GAO reports.

If no corrective action is taken, DOE will have successfully converted the right of election into the old case-by-case waiver approach.

Accordingly, we request that the Office of Federal Procurement Policy, pursuant to the authority vested in you by Section 202(b)(2) of Section 35 of the United States Code, issue a regulation prohibiting allocation of patent rights to the government as an "exceptional circumstance" under Section 202(a)(ii) in any case in which the agency has failed to provide clear evidence of its intent to commercialize the relevant technology and a detailed plan for achieving commercialization.

Sincerely,

Barry C. Beringer

Barry C. Beringer
Associate Under Secretary
for Economic Affairs

Enclosures