

## Strange Bedfellows: IP Rights and Accounting in SBIR/STTR Grants

by Mike Martensen | Dec 2, 2021 | Government Contracts, Intellectual Property Due Diligence



The Small Business Innovative Research (SBIR) and Small Business Technology Transfer (STTR) programs (referred collectively hereafter as SBIR) directly target small innovative companies to participate in federally funded research and development. The SBIR program, established in the Small Business Innovation Development Act, requires agencies conducting substantial R&D to set aside funds earmarked for small business innovation efforts.<sup>1</sup>

Since its inception, the program has consistently surpassed expectations, leading to continual growth and funding. SBIR grants leverage the well-known fact that the majority of innovation is found in small, not large, companies. And, the more than \$50 billion of taxpayer money granted to small businesses has been pushed back into the economy with a more than 22:1 return.

### 3 Phases of SBIRs

SBIRs are broken into three phases. Simply stated, in phase I, the government pays the business to provide a concept addressing a governmental need or pain point. In phase II, the government likes the concept and provides money to develop a prototype (proof of concept). Finally, in phase III, the government engages with the small business and purchases additional products.

It seems natural to expect that in exchange for an SBIR grant the government should gain something in return. Indeed, the government does gain rights in the innovations fostered through such a grant, but an SBIR effort is unlike a similar transaction in the commercial sector.

In the commercial sector, the party funding the research and development typically owns all intellectual property (IP) rights. SBIR programs are, on the other hand, designed to enhance the value and support

the success of the underlying innovative small business. Consequently, the IP developed by a small business under an SBIR grant remains the property of that business. The government gains a license to the technology but the license is limited, and by law the government is required to make phase III awards (to the holder of SBIR data rights) to the greatest extent practicable.

## **Valuable Exclusivity in SBIR Rights**

Here is where the rubber meets the road. While the government gains certain rights in the data, the small business becomes the preferred sole source for delivering products embodying that technology for a substantial period of time. This exclusivity is why SBIR rights are strongly valued in the governmental marketplace.

SBIR grants provide the contract holder with SBIR data rights. First, recognize that SBIR data rights are distinguishable from patent rights. A patent protects innovative ideas, concepts, designs, or methods that are inventive. Data rights protect the disclosure of recorded and written technical information. They are an amalgamation of copyright and trade secret protection.

The government's ability to disclose SBIR data is substantially limited while data disclosed in a patent becomes public knowledge. The publishing of SBIR data in a patent terminates the government's nondisclosure obligation, which can be problematic if a company is pursuing both governmental and commercial markets.

A product in which the technology is easily reversed engineered once it is placed into the public domain is arguably best protected by a patent. In the commercial market, patents can provide a competitive advantage. A product in which the innovation is difficult to grasp even when holding the product in your hand is better left as a trade secret, i.e., an SBIR data right. But recognize that SBIR data rights are meaningless in the commercial market.

## **Developing an IP Plan**

A critical first step in IP planning is knowing your market and which rules best apply. Aspirations of commercializing (or financing) a product developed under an SBIR grant may necessitate seeking a patent. Yet the patent disclosure may terminate SBIR data rights, making it easier for the government to take the innovation and hand it to a competitor.

Recall that patents granted to government-funded "subject inventions" cannot be enforced against the government. While the government recognizes the contributions of small innovative companies, it also likes the stability and scope of large companies. From the government's point of view, a startup, despite having great technology, may not exist in five years, may be unable to ramp up production or might have growing pains that render delivery questionable. As lucrative as a phase III can be, it also comes with risks for those not properly prepared.

Each agency (DoD, HHS, DOE, DOA, NASA, etc.) manage its own SBIR program.<sup>2</sup> And while each agency provides its own regulations regarding IP rights, a major distinction is found between those grants issued by defense agencies and SBIR awards supplied by civilian agencies.

Civilian agencies define SBIR data, and indeed all of their IP rights, on performance of a contract.<sup>3</sup> The regulation goes on to state that the government shall possess limited rights in SBIR data and restricted rights in software first generated in performance of the contract.<sup>4</sup>

By contrast, defense agencies generally allocate IP rights based on funding. In the DoD world, the more that the government pays, the more rights the government gets. That is, except with respect to SBIR data rights. Here the DoD is aligned with the civilian concept of data rights, focusing on performance rather than funding.

## The Importance of Tracking Deliverables and Funding

As a company moves through the SBIR process, identifying and drafting deliverables "generated" under the contract and tracking (allocating) government funds used in that generation becomes more and more critical. Determining which projects or which technologies are privately funded or conceived or reduced to practice with private funds vs. governmental funds can paint vastly different futures. Having systems in place to track spending, workflow, billing, etc. becomes increasingly important.

Drafting and implementing an effective SBIR IP strategy requires understanding the legal landscape. It also requires executing sound accounting and business practices. To paraphrase Benjamin Franklin: Failing to plan, is a plan to fail.

### Resources:

1 Small Business Innovation Development Act of 1982 (P.L. 97-219). The STTR program, was created by the Small Business Research and Development Enhancement Act of 1992 (P.L. 102-564) to facilitate the commercialization of university and federal R&D by small companies.

2 A complete set of U.S. Government regulations scan be found at <https://www.acquisition.gov/content/regulations>.

3 FAR 52.227-20

4 FAR 52.227-14 states "These data ...will not ...be used purpose of manufacture nor disclosed outside the Government." "This computer software ...may not be used, reproduced, or disclosed by the Government...."

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