

The Phase III Triple Crown: When SBCs, Primes and the Government Ride Together

Navy Opportunity Forum | Reston, Virginia | June 4, 2013

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Overview

- Phase III is a most unique SBIR right and status
- Phase III offers:
 - SBIR Data protection from disclosure in SBIR contracts and subcontracts, and "roll-over" of SBIR Data Rights
 - Sole source federal contracts, sparing federal agencies and prime contractors the burdens of competitions and protests
 - Phase III Preference rights
 - Opportunities for SBCs to establish markets
- Proper Phase III administration ("Phase III Process") involves 1) proper **identification** of the Phase III requirement, 2) **handling** it properly, and 3) **marking** the SBIR Data, all in accordance with the law

The Need for Phase III Collaboration

- Not all understand Phase III rules and opportunities
- Notwithstanding this lack of familiarity -- SBIR Phase III rights and rules are law and cannot be ignored
- The Phase III Process works best when all ***stakeholders*** – **small business concerns (SBCs)**, **prime contractors** and **federal contracting officials** – are committed to knowing, understanding, and implementing the Process
- The Phase III Process creates rights for SBCs, obligations for primes contractors and federal officials, and opportunities for all three stakeholders

Phase III Identification, Handling & Marking

- The identification, handling, and marking steps in the "Phase III Process" involve complex regulations
 - Identification involves knowing the definition of a Phase III and applying it so that each party knows when they are dealing with one – and is complex for some procurements
 - Handling Phase IIIs involves all parties knowing Phase III SBIR Data Rights, the Preference for Phase IIIs, and sole-source rights
 - Marking is vital to preserving SBIR Data Rights and helping federal agencies to manage SBIR Data – but becomes complex when non-SBIR Data is also involved
- When the Phase III Process works, it produces successful outcomes for all parties involved – agencies, SBCs, and large prime contractors

The Basis for Phase III Rights

- SBIR Phase III rights and obligations are set forth in:
 - The SBIR Reauthorization Act of 2011 (Act)
 - The August 6, 2012 SBA SBIR Policy Directive (Directive)
 - FAR clause 52.227-20, and
 - DFARS clause 252.227-7018
- All of these sources of Phase III rights – including the Directive – are laws and have the force of law
 - The Directive was implemented pursuant to lawmaking procedures
- Each party involved in the Phase III process must know and understand all of these laws

Identification of an SBIR Phase III

- **Identification:** The first step is: "What is an SBIR Phase III?"
- SBIR Phase III refers to:
 - "[W]ork that derives from, extends, or completes an effort made under prior SBIR funding agreements, but is funded by sources other than the SBIR Program."
- This definition is from Section 4(c) of the Directive
- A commercial contract can be a Phase III
- While the SBA Policy Directive applies only to federally funded work, a commercial contract can "roll over" SBIR Data Rights under subsequent SBIR funding agreements

Identification of Phase IIIs

- **"Derives from"** is a very broad test that refers to work that traces back to SBIR efforts performed under prior SBIR funding agreements
 - These prior SBIR agreements can be prior Phase I, II, or III contracts, grants, or other funding vehicles
 - "Derives from" is at the most basic level of the prior SBIR work – not the application, data, or reports, but the basic SBIR hypothesis that was tested for feasibility in Phase I
- **"Extends"** means the work can be for *other applications* not researched or performed in prior SBIR efforts
- **"Completes"** means commercialization of the prior SBIR research into a commercial product or application
- These are three different tests because of the word **"or"**

Identification of Phase IIIs

- "[B]ut is funded by sources other than the SBIR Program" means that funds from the agency set aside for the SBIR Program (used for Phases I and II) cannot be the source of funding
- Thus, a Phase III many times looks like a regular procurement:
 - A Phase III can be funded by procurement, O&M, construction, research, *or any other type of agency funds* (except SBIR Program funds)
 - It can be any type of contract, including a subcontract, and result from a competition

Identification of Phase IIIs

- This concept can be confusing
- For instance, contracting officials are conditioned that the nature of a contract is dictated by its funding:
 - A construction contract is funded by construction funds
 - An operation and maintenance contract is funded by O&M funds
 - A research contract is funded by research funds
- For Phase IIIs, the CO is asked to accept that a Phase III SBIR contract is funded by ***non-SBIR funds***
- Many acquisition officials conclude that because the work in question is not funded by Phase I or II funds, it cannot be an SBIR contract
- However, ***the very fact*** that it is ***not*** funded by SBIR funds makes it a Phase III

Identification: A Phase III Can Be of Any Type

- A Phase III can be for *any* type of activity
- The fact that the work is not for research does not mean it cannot be a Phase III
- The Directive states that: "Phase III work may be for products, production, services, R/R&D, or any such combination." (Sec. 4(c)(4))
- A subcontract can be a Phase III and a Phase III can be a subcontract (Sec. 4(c)(5) states this expressly)
 - In fact, a Phase III can be any type of contract or funding vehicle
 - It can be a purchase order under an IDIQ or GSA Schedule contract, a grant, a subgrant, a subcontract, or any other type of federally funded agreement

Identification: Phase IIIs Can Result From Competition

- If an SBC wins a *competition* for work that "derives from, extends, or completes" that firm's work under a prior SBIR funding agreement, **then the new funding agreement is a Phase III and must be accorded all SBIR rights.** Sec. 4(c)(2)
- A Phase III can result from a competitive procurement if it derives from, extends or completes prior SBIR effort
- If an SBC offers its SBIR technology in a Broad Agency Announcement ("BAA") competition, and wins, the resulting contract award is a Phase III (Sec. 4(c)(2))
- The solicitation in that case does not call for Phase III work if it simply requested solutions to a generally described problem – ***but the award is a Phase III***

Identification: A Phase III Can Result From a Competition

- The law (and definition of a Phase III) makes the award in such a case a Phase III because the *work proposed* derives from, extends or completes prior SBIR work
- The solicitation is not law and cannot supersede the Phase III status the law affords the award
- A solicitation cannot incorporate SBIR Data
- If the solicitation, unlike the BAA, which solicited a solution to a generally described problem, incorporates SBIR Data to describe the requested work, then the *solicitation itself* defines Phase III work and requires the agency to afford an SBIR Preference prior to issuance to the SBIR developer (See *Directive, Section 4(c)*)

Identification: Phase IIIs Are Flexible

- A Phase I can go straight to a Phase III
- A Phase III can follow another Phase III
- A Phase III can be for any amount
- A Phase II and a Phase III can be awarded at the same time, but from different funds
- A Phase III can be a modification to a Phase I or II – the Phase III is the amendment funded with non-SBIR funds
- A Phase III can be other than the agency that awarded the Phase I, II, or prior Phase III
- Size standards do not apply to Phase IIIs – Phase IIIs are exempt from the 500 employee size standard and the affiliation rule

Handling a Phase III

- Once a Phase III is identified, the law requires that it be provided SBIR rights
- The Directive states: "A Phase III award is, by its nature, ***an SBIR award***, has SBIR status, and ***must be*** accorded SBIR data rights..." (*Directive, Sec. 4(c)(c)*)
- At the point of identification of the work as a Phase III, the agency or prime contractor must accord the solicitation or work SBIR status and SBIR rights and obligations attach to it
- Thus, once a Phase III is identified, the law "kicks in" and SBIR rights and obligations flow from there

SBIR Rights & Obligations

- The Government may award a Phase III on a sole-source basis
- The SBC receives a "Preference" – the Government must afford a Phase III Preference to the SBIR developer of the technology to perform the Phase III work
- The Government receives a royalty-free right to use the Phase III SBIR Data worldwide
- The Government cannot disclose Phase III Data
- The SBC receives the benefit of the nondisclosure obligation, SBIR Data Rights, SBIR Data "roll-over" rights, and the Preference

SBIR Data Rights – What Are they?

- Agencies have a broad duty to protect SBIR Data
- Agencies ***receive a royalty-free license*** in technical data generated under SBIR awards "for Government use," but may not disclose SBIR technical data "outside the Government" – especially to the SBC's competitors -- during the protection period
- Under the DFARS clause, DOD may disclose SBIR technical data to support contractors – those firms that signed a nondisclosure agreement with DOD and cannot bid on contracts involving the technology or data
- SBIR firm retains ***ownership rights*** to data generated by the SBC in the performance of an SBIR award

Phase IIIs Receive SBIR Data Rights

- Phase IIIs must include the SBIR Data Rights Clause – the agency or prime contractor must insert the clause
- Under the SBIR Data Rights Clause:
 - Agencies must protect all proprietary information, and must refrain from disclosing all information generated under an SBIR funding agreement, except for limited purposes
 - Protections under the Directive are "for not less than 4 years" — but under the DFARS, 5 years under clause 252.227-7018
- According to Section 8 of the Directive, Phase III contracts "roll-over" SBIR Data protection periods of prior SBIR contracts to the Phase III protection period
- SBCs should provide notice to contracting officers on prior SBIR contracting notifying them of the "roll-over"

SBIR "Roll-Over Rights"

- "Roll-over" rights are a valuable Phase III right
- SBIR Data Rights "roll over" to the end of the protection period of the *latest* SBIR contract
- Because of Phase IIIs, SBIR protection can theoretically be perpetual – keep rolling over SBIR Data Rights protection periods with new contracts
- *Provide notice* of subsequent awards to agencies from which you have received prior SBIR funding agreements, and the new protection period, so that the prior funding agencies are aware that your rights have "rolled over" in prior SBIR funding agreements to the new date

SBIR Data Rights Are Non-Negotiable

- SBIR technical data rights are non-negotiable
- Agencies may not in any way make issuance of an SBIR award, including a Phase III, conditional on data rights
- Agencies may not diminish or remove SBIR Phase III technical data rights during contract administration
- Transfer of technical data rights to the agency or any other party must be in a writing that can only be executed *after* the SBIR award is signed
- *SBA must immediately* report to Congress any attempt or action by an agency to condition, exclude or diminish SBIR data rights

Preserving Non-SBIR Data Rights

- SBC's must affirmatively act to preserve rights in **non-SBIR** data – most commonly developed at private expense
- Such data receives rights more restrictive than SBIR rights:
 - **IDENTIFY** data developed at private expense and not developed under the SBIR contract that the SBC may bring to the contract
 - **ASSERT** rights to the data
 - Describe the **BASIS** for the assertion
 - Provide the **NAME/COMPANY** asserting rights
- This four-column chart appears in the SBIR DFARS clause
- Failure to identify and assert rights to non-SBIR technical data submitted under a contract can result in forfeiture of rights in privately developed (non-SBIR) data

Handling Non-SBIR Data

- Identify technical data developed at private expense, developed outside of SBIR funding agreements, or brought to the contract, sufficiently so the Government can ascertain where SBIR Data generated under the contract starts and ends
- If the agency requests more than the title to the program or a general description, then you can provide it later
- For data from patents, cite the "data developed in connection with [list the patent number]," but do not merely list the patent itself – patents are not data
- Describe copyrighted materials (sketches, drawings, engineering plans), by title (if it exists) or other description
- Describe other trade secret data

Data Developed at Private Expense

- Pre-existing, non-commercial data developed at private expense is ***not*** SBIR Data, even if delivered under an SBIR contract – if it was not generated under the SBIR contract
- Deliver and mark data developed at private expense with the Limited Rights legend (or with the Restricted Rights legend for non-commercial computer software)
- If you must deliver it, then mark it with the Restrictive or Limited Rights legend to indicate that it was *not generated* under the SBIR contract, and therefore, is not SBIR Data
- Restrictive or Limited Rights data that cannot be separated from SBIR Data must be marked with a Restrictive/Limited rights legend because such data can never be disclosed

Mark Your Data

- SBCs must **mark** all SBIR data (generated under an SBIR contract) with the data rights legends contained in:
 - DFARS 252.227-7018 for defense agency contracts; and
 - FAR 52.227-20 for non-defense (civilian) agencies
- Use the exact wording from those clauses
- Annotate the date to indicate the "roll-over" – "...subject to Section 8 of the SBA SBIR Directive of August 6, 2012"
- "Mark it or lose it" when it comes to data rights
- There is no deadline in the DFARS or FAR clause for marking – you can "cure" a failure to mark – re-submit your deliverable with the SBIR marking on it
 - If any disclosure took place while it was unmarked, you have no recourse, but no disclosure can be made after your submission

The Prime Contractor's Role in Phase IIIs

- A large contractor that awards a Phase III subcontract must ***insert*** the SBIR clause into its subcontract
- The large prime does not flow down the clause because it does not have it in its prime contract – but the law requires the clause in a Phase III SBIR subcontract – so ***it is inserted, not flowed down***
- The prime contractor need not fear a reaction from the customer agency for this – the answer is that the law requires the SBIR clause in an SBIR contract
- The prime contractor benefits because its prime contract now will produce technical data that is non-disclosable to others –giving them an advantage in re-procurements
- The prime can also take credit for Phase III success stories with SBC subcontractors or purchased firms

Prime Contractor Rights

- Prime contractors can also benefit from purchasing SBIR firms or their technologies
- Size standards/affiliation rules do not apply to Phase IIIs
- Agencies can procure sole-source work that derives from, extends, or completes prior SBIR work from these large contractors that have purchased SBIR firms
- They can also purchase individual SBIR technology lines
- SBIR Data in such acquisitions provide large primes an advantage in re-procurements of their programs – the Government cannot disclose SBIR Data to competitors
- The Government also cannot incorporate this SBIR Data from subcontracts into solicitations – the Data becomes an edge in re-procurement competitions for the prime

Phase III Sole Source Rights

- The Phase III sole-source rights are the Government's not the SBC's -- this is widely misunderstood
- The Government has the absolute right to issue Phase III sole-source contracts (*Directive, Sec. 4(c)(3)*)
- The Justification and Approval merely needs to state that the work "derives from, extends, or completes prior SBIR efforts and is funded with non-SBIR funds"
- This saves countless hours of competitive procurement and protest time and effort – Phase III awards cannot be successfully protested
- Prime contractors also can award Phase III subcontracts on a sole-source basis

The Phase III Preference

- The SBC's related right is the Preference Right
- SBCs do not have a legal right to sole-source awards
- The Preference means that Phase III defined work must go to the SBIR developer "to the greatest extent practicable" (*SBIR Reauthorization Act, Sec. 5108, Dir, Sec. 4(c)(7)*)
- SBA has said that the Preference Process involves the agency asking: 1) "Is the SBIR firm available?; and 2) Is it capable of performing the work?"
- A "Yes" answer to both questions raises a compelling case for a **sole-source contract**, and the agency risks acting unreasonably if it fails to consider such an award

Are Phase IIIs a "Slippery Slope" for Agencies?

- Some agency officials are concerned that Phase IIIs are a "slippery slope" – once awarded, future contracts will derive from the initial Phase III and "it will never end"
- Such a view is unjustified:
 - The SBC developed the technology – SBIR law protects SBIR inventions just as the patent laws protect technology inventions
 - It is the law -- Congress wants it that way
 - If the SBC is completing the work on time and within budget, the agency could ask for nothing more from anyone else
 - SBCs are commonly cheaper and more efficient than large firms
 - The most common critics of Phase III sole-source contracts are larger firms with out-moded approaches and methods that Phase IIIs replace – Phase IIIs encourage large firm innovation

Summary – Winning the Triple Crown

- Phase IIIs are a win, win, win for all stakeholders
- **SBCs** win with sole-source contracts, markets for their products, and technical data protection
- **Agencies** win by complying with the law, issuing sole-source contracts that avoid burdensome competition and protests, introduction of new, faster, better, cheaper and more reliable innovations into their missions, and being able to report successful Phase IIIs to Congress
- **Large primes** win by assisting customer agencies with Phase III subcontracts, complying with law, and protecting Phase III Data from disclosure to competitors
- **The Triple Crown goes to all when they ride together**

The Phase III Triple Crown: When SBCs, Primes and the Government Ride Together



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