NERF License Rights:
Factors to Consider When Exercising NERF Pilot Program Authority

INTRODUCTION

This guidance document provides a discussion of factors for consideration when contemplating the commitment of non-exclusive royalty-free (NERF) license rights to University inventions under a sponsored research agreement. As each campus/Laboratory has a wide range of options to choose from when offering such rights to a sponsor, this guidance document addresses topics of relevance to both the C&G Office and Campus Licensing Office (CLO). Many of the topics discussed herein fall within the authorities of both the campus C&G and CLO functions. As such, consultation between the C&G Office and CLO is strongly encouraged when crafting appropriate NERF rights under a sponsored research agreement.

The organization of this guidance document progresses from a general discussion on how to evaluate the sponsor's purpose and need for a NERF to a more detailed discussion of the individual components of a NERF. Here is a "roadmap" to help guide you through the topics and content within this document:

Anatomy of a NERF
(a brief discussion of non-exclusive licenses)

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Purpose of a NERF
(discussion of determining if a NERF is appropriate)

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NERF Form & Function
(discussion of the various forms a NERF can take and how best to use it)

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Other NERF Elements
(discussion of various legal, academic, and commercialization issues to consider when contemplating NERFs)

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Alternatives to a NERF
(other choices available as well as narrowing the NERF rights)

While the material in this guidance document is best absorbed through a sequential reading of the document, each individual section can also serve as an independent subject matter reference source for the more experienced C&G Officer and CLO professional.

ANATOMY OF A NERF

Background

Each campus/Laboratory is authorized to provide a sponsor of research the first right to negotiate a license to patentable inventions conceived and first reduced to practice in the University's performance of a sponsored research project. The license rights may consist of an exclusive or non-exclusive right to such future inventions. In exchange for these rights, the sponsor is typically required to meet certain performance criteria (due diligence) in order to ensure the timely development of the University's invention for the public benefit along with some form of fair consideration (usually financial in nature) back to the University based upon the commercial value the sponsor derives from its use of the invention. The sponsor's market strategy will usually be the primary factor in determining the type of license needed by the sponsor ranging from exclusive rights to non-exclusive rights to merely the freedom to practice the invention. An exclusive license excludes all parties other than the sponsor from practicing the University invention. A non-exclusive license, however, merely provides assurance that the University will not initiate an infringement suit against the sponsor for certain specified rights to the subject invention. A nonexclusive license does not preclude the University from practicing the invention or from licensing others to practice the invention. The University may grant numerous nonexclusive commercial licenses to different companies for the same invention. A NERF is one type of a non-exclusive license. So how does a NERF differ from the typical non-exclusive license offered by the University?

To state the obvious, a NERF is a non-exclusive license right whereby a licensee is not required to share a portion of any proceeds received from the cumulative use or sale of a product (also known as a running royalty) that falls within the claims of the licensed patent. License fees or other payments required under the terms of the license that do not result from the sale of a licensed product, method, or service are separate and distinct from a running "royalty" payment by the licensee. In granting a sponsor certain NERF license rights to future inventions, the C&G Officer should consider the following criteria:

(1) what purpose will the NERF license serve;

(2) the form and function of the NERF rights a sponsor will acquire under the research agreement; and

(3) other elements that may influence the campus/Laboratory in framing such NERF rights.

Let's consider each of these in greater detail.

(1) Purpose

The first determination a campus/Laboratory will need to make is what purpose does the NERF serve in the researcher's overall research agenda. In an ideal world, the campus/Laboratory would know the scope and utility of an invention and how it serves the researcher's long-term research objectives prior to negotiating the sponsor's future rights to that invention. Such rights should complement rather than constrain the researcher's long-term research objectives.

Inventions, however, are a serendipitous future outcome of a research endeavor. As a result, the C&G Officer is asked to articulate appropriate rights to an invention that is yet to be created without the benefit of knowing the purpose of the invention or how best to frame the sponsor's rights to such invention in a manner consistent with the needs of the inventor, the University, and the sponsor. Knowing the long term objectives of the researcher, however, can help the C&G Officer frame the invention rights discussion with the sponsor and determine whether a NERF right is consistent with the researcher's objectives. While a research/internal use NERF right will satisfy the needs of some sponsors (predominately non-profits and the federal government), most commercial entities that sponsor research at the University will require some form of commercial rights for the use of any resulting inventions.

Any commercial rights should be consistent with the research objectives of the research program. For example, if the goals of the research program are focused on "value engineering" – to develop open industry standards and protocols (i.e., IEEE) or establish a leadership position in a particular area of technology (i.e., microwave communications, nanochip design, etc.) – then a NERF could be an appropriate vehicle for meeting these objectives as it provides unrestricted access to the invention with the goal of achieving adoption of the technology by as many users as possible. In contrast, if the goals of the research program are focused on "applied technology development" – to develop or improve established technologies employed by commercial entities – then a NERF may not be the best choice as the sponsor is the predominant beneficiary of the research effort and the University should share in any commercial benefits realized by the company through the use of reasonable and non-discriminatory license terms under a royalty-bearing license.

It is in the best interest of the University, the C&G Officer, and the CLO to engage the researcher in these types of discussions early-on in a research program in order to understand (and in some cases help delineate) the purpose and goals of the research program. This will simplify the task of developing an invention rights strategy for use in future sponsored research agreements and license agreements addressing any resulting inventions.

In addition, the campus/Laboratory should also evaluate the impact a NERF license right could have on its implementation of a technology development strategy for a particular invention. To illustrate this point, a campus provided a company with a NERF right under the terms of a Material Transfer Agreement (MTA). The researcher later disclosed a new potentially patentable algorithm created in the performance of the MTA. A medical device company approached the campus with an interest in licensing the invention and supporting further research at the campus on the algorithm-based technology. When the medical device company learned about the NERF right to the MTA provider (which was a competitor of the medical device

company), it decided not to pursue the license and sponsored research agreement with the campus.

(2) Form and Function

The next decision a campus/Laboratory will need to make is what type of NERF is appropriate for a specific situation. The following options represent a cross-section of choices that a campus/Laboratory might consider when contemplating the inclusion of a NERF rights provision in a sponsored research agreement:

(1) Research-Only NERF:
This type of NERF would restrict the sponsor's use of the University invention to an investigatory utilization of the University invention in a research setting. This type of NERF leaves greater possibilities for the campus/Laboratory to license other entities for both research and commercial applications. For example, this type of NERF could be used in a multi-party collaboration (i.e., consortia) involving participants from both academia and industry. All parties would have the right to use any resulting inventions for research purposes only. Any right to make or sell a commercial product or service that falls within the claims of the University patent would require the negotiation of a separate commercial license. The campus/Laboratory may choose to further limit the scope of the research NERF by limiting the term of the license to the duration of the research project. This permits the consortia membership to practice such University inventions in order to complete the project tasks but requires a separate license should a consortia member wish to continue the practice of the University invention beyond the performance period of the research project.

A research NERF to other academic institutions and non-profits should limit the institution's use to education and research purposes. A research NERF to a commercial entity is difficult to distinguish from a non-commercial NERF, particularly when the research use is the commercial use (i.e., in the case of a "research tool" used to develop or manufacture a commercial product), unless there is a way to clearly isolate the company's "research" use from its product development activities. An internal use NERF to a commercial entity may be a better choice when the company's internal "research" activities are linked with its product development activities.

(2) Internal Use NERF:
This type of NERF is an extension of the research NERF with the added ability to practice the University invention in an applied research/industrial setting that does not involve the direct manufacture or sale of a licensed product or service. For example, this type of NERF license could be used where the purpose of the sponsor's use involves the evaluation or monitoring of processes that may improve manufacturing efficiencies. Because the distinction between internal use and commercial use is artificial at best, how one defines the boundary between internal use and commercial use can be problematic. For example, providing a pharmaceutical company with an internal use NERF to a research tool for drug discovery applications is equivalent to a commercial use since the

company's use of the research tool could result in the creation of a new drug product. In contrast, providing a company that develops diagnostic kits for the detection of diseases with an internal use NERF whereby the research tool would be used to test the efficacy of the diagnostic kits falls presumably within the framework of non-commercial use. This option should only be considered after careful evaluation of the facts and circumstances where such use is being considered and in consultation with the CLO. An internal use NERF may grant the company the right to make and use the invention but should explicitly exclude the right "to sell or offer for sale" any products or services that use the invention.

(3) Commercial NERF:
This type of NERF license is the one most frequently requested by a commercial sponsor as it provides the sponsor with commercial use rights of a University invention. The sponsor would have the right to "make, use, and sell or offer for sale" the invention, including incorporation into any products or services that fall within the claims of the resulting University patent. This would satisfy a commercial sponsor's "freedom to operate" requirement as it permits them to pursue their chosen product markets without restrictions. The use of this NERF option should be limited to only those sponsors engaged in the manufacture or sale of commercial products or services. This is not an appropriate choice for use with non-profit sponsors or other academic institutions.

While a commercial NERF lacks a running royalty provision, the campus/Laboratory should consider whether other forms of consideration are justified based upon the likely value of the commercial license to the sponsor and whether such a license is consistent with the research project objectives and goals (i.e., value engineering versus applied technology development). The campus/Laboratory may consider incorporating any one or combination of the following forms of consideration into a commercial NERF license, when appropriate:

- *Reimbursement of University's Patent Costs* – As a minimum financial obligation on the part of the sponsor, the campus/Laboratory should strongly consider a requirement for the sponsor to reimburse the University for its unreimbursed patent costs. This can be structured on a pro-rata basis when the campus/Laboratory anticipates multiple licensees, though this is burdensome from an accounting perspective. If the sponsor refuses to accept such an obligation, the campus/Laboratory should include a provision in the sponsored research agreement stating that the University is not obligated to file for patent protection on any inventions made under the research agreement. The University should avoid situations where it must spend public funds to obtain a patent for the benefit of an individual company, with no consideration being provided back to the University.

- *Issue Fee* - The licensee pays a fee to the University upon final execution of the license agreement or pursuant to a pre-agreed upon schedule. The fee amount generally should reflect the value of the invention at the time it is made available

to the licensee. Normally, such fees can range from a few thousand dollars to a quarter of a million or more. For small companies or start-ups, the issue fee may be partially postponed until sufficient investment capital is secured, or may be replaced in part by the University's acceptance of equity in the company (see Equity below).

- *Annual Maintenance Fee* - The licensee makes a fixed annual payment to the University. Such fees may serve as a form of diligence in that their payment represents a continuing interest in and financial commitment of the licensee to the licensed invention.

- *One-Time License Fee* – Some companies do not want to incur an ongoing and sometimes procedurally burdensome obligation to provide financial consideration during the term of a license but are willing to provide a one-time payment for the purchase of a "paid-up" license to a University invention. In such cases, the CLO may consider valuing the invention, once it is disclosed, over its lifetime to arrive at an appropriate one-time fee to be paid by the sponsor when the license is executed by the parties.

- *Equity* - This option may be particularly useful in working with small or startup companies that may find it difficult to commit significant cash outlays for both developmental and licensing costs (but should not be used to offset royalty rates). The campus/Laboratory should consult Business & Finance Bulletin G-44 on Accepting Equity (http://patron.ucop.edu/ottmemos/docs/ott02-01.html) for additional guidance in this area.

- *Other* - The campus/Laboratory may negotiate or identify other forms of consideration to the University for access to University inventions other than those described above. Research equipment, other forms of research support (as a due diligence requirement under the NERF), and other unique exchanges of value may be appropriate forms of consideration. The campus/Laboratory should note, however, that such non-standard forms of consideration fall outside the royalty-sharing provisions of the University Patent Policy and all project participants and relevant stake holders should be advised accordingly if such terms are incorporated into the sponsored research agreement.

Please note that many companies subscribe to the belief that a "NERF" is actually a fully paid-up, no cost license. This differs from the University's working definition of a NERF as discussed above under "Commercial NERF", i.e., that there will be no running royalties, but there could be other forms of financial consideration. Unless the campus/Laboratory intends on providing a sponsor with a fully paid-up, no cost NERF, the C&G Officer should clearly articulate the University's expectation regarding a "commercial NERF" right under the sponsored research agreement by including a statement that the sponsor will be required to provide some form of financial consideration for the NERF. Any discussions with the sponsor as to what constitutes an

acceptable form and amount of financial consideration should involve a representative from the CLO.

(4) Fully Paid-Up, No Cost NERF:
This type of NERF is a fully paid-up, no-cost license where the sponsor provides no financial consideration to the University for the license. This is the least desirable NERF option that a campus/Laboratory should consider. Under this option, the campus/Laboratory assumes all financial risk associated with the patenting and licensing of the invention. Should the campus/Laboratory choose to pursue patent protection, the campus/Laboratory will have to use campus/Laboratory funds until such time that the campus/Laboratory can find other licensees that will reimburse the University for all past and future patent costs.

One situation whereby the University is more likely to agree to give a company free access to inventions is under a Material Transfer Agreement where the company provides a proprietary material that cannot be obtained elsewhere. Even then, the free license should extend only to those inventions that are dependent upon the provided material (necessarily uses or necessarily incorporates), limited to the provider's ability to make, use, and sell the provided material, or limited to internal research purposes. In these situations, the University often feels that having access to the proprietary material is sufficient valuable consideration for the NERF.

Should the campus/Laboratory choose to utilize this option, the campus/Laboratory should ensure that the associated files contain appropriate documentation addressing the University Principles of fair consideration, public benefit (see additional discussion below), and informed participation. Such documentation could include a memo to the file from the CLO describing the fair consideration received by the campus/Laboratory (in lieu of financial compensation by the sponsor), the manner in which the public benefit is preserved, and a special investigator acknowledgement form signed by the project participants (or equivalent notice and acknowledgement by email).

When contemplating the form and function of any NERF rights offered to a particular sponsor, the campus/Laboratory may want to factor the following additional criteria into its decision-making process:

- Whether the sponsor is paying the full cost of the research;
- To what degree the sponsor holds a dominating patent position in a given area of technology together with whether the NERF is limited to inventions that are dominated by such patent(s);
- To what extent will the NERF impact the University's opportunity for additional sponsored research in the technology area and the licensing of any resulting inventions to non-sponsoring parties; and
- Whether the sponsor has funded other projects at the campus/Laboratory (or the University) in the same field, and at what level of funding.

(3) Other Elements to Consider When Granting NERF Rights to a Sponsor

The final step is for the appropriate campus/Laboratory authorized personnel to craft specific provisions in the sponsored research agreement and resulting NERF license agreement (if appropriate) tailored to the objectives and goals of the campus/Laboratory and the affected research program.

MEANS OF GRANTING NERF RIGHTS

All NERFs, regardless of the form, should be limited to patentable inventions conceived and first reduced to practice in the performance of the research project. A sponsor's right to a NERF can be structured under a sponsored research agreement in one of the following ways:

- *First Right to Negotiate* – The standard practice of the University is to offer a sponsor of research a time-limited first right to negotiate a license to inventions conceived and first reduced to practice in the performance of the research project. This provides the sponsor with a prioritized position as the first potential licensee to enter into negotiations with the University for a license to the University's invention. Even in the case of a NERF, this is the preferred approach as it leaves the details of the license agreement to a point in the future once the scope of an invention is known and appropriate terms can be negotiated by the CLO.

- *Will/Shall Grant* – Many times a sponsor will require a higher level of assurance from the University that a license will actually be issued once an invention is made. While this still defers the actual grant of a license until such time as the invention actually exists, it creates an affirmative obligation on the University to actually grant such a license. Some sponsors will attempt to make a distinction between "will" and "shall" with regards to the degree the University is obligated to grant such a license. From a legal perspective, no such difference exists and the use of either term is equivalent in this context. While this is not a preferred option to offer a sponsor, it is a possible solution when a sponsor demands an actual grant of a license (see below) under the terms of the sponsored research agreement.

- *Hereby Grants* – Some sponsors demand an outright upfront grant of a NERF license to future inventions at the onset of the research project. The use of "hereby grants" effectively turns the sponsored research agreement into a license agreement. As such, the agreement is now subject to an additional set of legal and policy standards. Research agreements are negotiated in the contract & grant office, which generally does not have the authority to enter into license agreements (similarly, the CLO does not have the authority to enter into research agreements). Even with the delegated licensing authority, the CLO must still secure the review and approval of the Office of General Counsel (OGC) before entering into a license agreement. There are several terms that OGC absolutely requires in each of the University's licenses to provide certain protections for the University - without which, the license will not be approved. These include the following:

  - no use of the University's name without prior approval,

- a disclaimer of warranty,
- appropriate indemnification of The Regents,
- a limitation of liability, and
- a statement of no implied license to other University inventions.

Also, the University must ensure that the terms of such agreements support the University's obligations to the State, comply with Federal law and regulation, serve the public interest, and meet certain business standards. When faced with this scenario, the C&G Officer should either modify the provision to a first right to negotiate (or as a last resort to a "will or shall grant" as discussed above), or have the sponsor work with the CLO in crafting an appropriate NERF license document that can be attached to the sponsored research agreement and exercised at such time when an invention actually exists. The latter option allows the University to incorporate terms that accommodate the various issues, concerns, and legal obligations of the University into a final license agreement and to administratively track the license obligations associated with a particular invention. The C&G Officer should avoid an outright grant provision if at all possible, and if it is truly unavoidable, must first consult with and get concurrence from the CLO and secure any necessary approvals.

- *Non-Assert Provision* – While this is not a grant of rights in the traditional sense, some sponsors may attempt to insert a "non-assert" provision under the intellectual property rights section in a sponsored research agreement. The sponsor will claim that it does not want to bother with having to come back and negotiate a separate license agreement and simply wants the University to agree that it will not assert its rights in University inventions against the sponsor. A "non-assert" provision is equivalent to a fully paid-up, no cost NERF thereby affording the sponsor the freedom to operate it desires. This is an unacceptable substitute for a NERF license for the following reasons:

  - It is not a license agreement but a binding legal obligation that the University (and usually any University licensees of the invention) will not assert its patent rights in a particular invention against the sponsor;
  - It does not require the sponsor to take an affirmative action (i.e., a written election to the University) in order to exercise this right;
  - The University does not retain the legal protections afforded the University under a commercial license agreement for a sponsor's commercial use of a University invention (i.e., warranty, limitation of liability, indemnification, use of the University's name, etc.);

- The University cannot enforce due diligence over the sponsor to ensure the invention is developed in a timely manner for the benefit of the public;

- There is a higher risk for future conflicting obligations since no actual license document exists, making it difficult to administer and track in order to prevent future conflicting obligations; and

- It is difficult to require any fair consideration back to the University.

The C&G Officer should consult with the CLO and UCOP/OTT when a sponsor insists on including a "non-assert" provision in the sponsored research agreement as the campus/Laboratory will require an approved exception to University Patent Policy before using such a provision.

PUBLIC BENEFIT

As a standard practice, the University includes diligence provisions in all exclusive license agreements to ensure that University-generated inventions are developed and deployed to the marketplace by the licensee in a timely manner. It is not in the best interest of the University or the public to allow an invention to languish due to a lack of commitment of the licensee, a licensee's business strategy to "shelve" the technology to protect its competing product lines, or inadequate technical or financial resources. One of the major concerns with granting a NERF license is that the licensee either can't or won't develop the invention in a timely manner for the public benefit or lacks any incentive to do so. The very existence of the NERF may act as a deterrent to other potentially interested parties. Possible ways for the University to address public benefit under a NERF license include:

- requiring diligent development;
- narrowly limiting the range of inventions or the field-of-use to which the NERF applies;
- requiring some form of non-royalty remuneration such as an annual fee; or
- addressing the problem directly.

The practice of addressing public benefit under a non-exclusive license varies from campus/Laboratory to campus/Laboratory and may be accomplished in the following ways:

- *Diligence* – Diligence provisions under a non-exclusive license may seem less important than under an exclusive license as the University can, in theory, non-exclusively license the same invention to other companies. There are no guarantees, however, that the University will find other companies interested in a license to the invention, particularly when the sponsor already has a royalty-free license and the sponsor may ultimately be the only licensee for that University invention. How does the University maximize the benefit to the public in such non-exclusive license situations without some de minimis due diligence obligations on the part of the sponsor/licensee?

Appropriate diligence provisions are specific to each invention, may vary widely from case to case, and are left to the discretion of the campus/Laboratory as how best to implement under a non-exclusive license to ensure the public benefit principle is adequately addressed. The ideal sponsored research agreement will provide a clear pathway for the inclusion of diligence requirements in any resulting license agreement by stating such license will include diligence requirements. In the license agreement itself, diligence would be case-specific. Diligence can even be used by the campus/Laboratory to address socially relevant issues such as compensation to indigenous cultures that contributed to the research activity leading to the invention (i.e., indigenous plants or local medicinal folklore) and preferred drug pricing for third world countries.

Clear diligence provisions ensure that the University retains the ability to manage its technologies as public assets for the benefit of the public regardless of the type of license. Diligence provisions therefore should be sufficiently definitive so that both parties to the license agreement can tell whether they have been achieved. Further, the license should provide a remedy for lack of diligence, such as cancellation of the license, or a reduction/limitation of rights (i.e., narrowing the field-of-use).

- *Scope of Inventions/Field-of-Use* – The University can also serve the public interest by limiting the sponsor's NERF to certain inventions or certain fields-of-use, especially for those inventions with multiple applications within the research field of endeavor. For example, if the sponsor provided proprietary material, proprietary equipment, or secured patent protection in the area, the NERF could apply to only those inventions that require use of the material, equipment, or patents. Since any resulting inventions cannot be licensed to other parties without the sponsor's cooperation, the public benefit is not obviated. Alternatively, rather than limiting the range of inventions, the campus/Laboratory could limit the NERF license itself to just the extent necessary to make, use or sell the proprietary material or equipment, or just to the extent necessary to practice any dominating patent(s). Similarly, there are certain industry sectors that are based on and flourish with a model of broad non-exclusive access to technologies to ensure its freedom to operate within a certain technology sector. In such industries, such as the information technologies and electrical engineering sectors, the public interest can be served by a NERF licensing strategy. When implementing any approach to limit the scope or field of a sponsor's rights to University inventions under a sponsored research agreement, the C&G Office should consult with the CLO.

- *Consideration as Diligence* – As discussed in Section 2 (Form & Consideration) above, a royalty-free license can have other means of financial consideration, such as an annual fee. In many cases, the fee itself acts as a means of diligence, since each time the licensee pays the fee, it has to assess whether it is still sufficiently interested in the invention to justify payment of the fee.

- *Maximizing Invention Utilization* – For those inventions with applications across many fields-of use, the University can preserve its ability to achieve the maximum public utilization of such inventions by including an exclusive grant-back provision to the University under the NERF license that allows the University to license any unused rights to other third parties. This could be structured to allow the sponsor sufficient time (as determined by the campus/Laboratory) to develop a market for an invention (potentially limited to certain fields-of-use), whereby failure to do so within the prescribed time frame results in such rights reverting back to the University.

FAIR CONSIDERATION

Many sponsors will inquire whether "royalty-free" means a fully paid-up, no-cost license where the sponsor provides no financial consideration to the University or whether the sponsor is required to provide some form of financial consideration other than a "running royalty" on the sale of licensed products. Many sponsors will simply assume the former. To address this question, one must view University inventions as public assets created using public funds, supplies, equipment, facilities, and staff time.

The University, as a public trust, has a responsibility to manage its assets for the public benefit. Therefore, the University has an obligation to receive fair consideration in exchange for the grant of commercial licensing rights to a sponsor. The level and form of fair consideration should reflect the relative risks and rewards of the commercial pursuit. Such consideration may vary widely based on case-specific factors that include (1) the reimbursement of the University's patent costs, (2) payment of one or more types of license fee(s), (3) applicable running royalty payments, equity, or other forms of consideration, as well as (4) the nature of the invention itself, the amount of development necessary to bring it to market, and the size and profitability of the market. As an alternative, several campuses employ a patent cost reimbursement and a reasonable annual or one-time fee strategy when negotiating NERF rights under a sponsored research agreement to help provide fair consideration for the NERF.

Under the authority of the NERF Pilot Program, C&G Officers can, in consultation with the CLO and University project participants, determine the basis for appropriate consideration under a specific NERF Pilot Program project. One possible option could include the right for a sponsor to negotiate a non-exclusive commercial license with no running royalty, but with some other form of consideration. Any such determination of fair consideration should be based upon the specific set of circumstances and should be consistent with University Policy on Principles Regarding Rights to Future Research Results in University Agreements with External Parties (August 26, 1999) and OTT Operating Guidance Memo No. 00-05, University Licensing Guidelines (December 1, 2000). It is important to emphasize that the rationale used by the campus/Laboratory in determining the appropriate fair consideration for each NERF Pilot Program project should be documented in the appropriate University files.

TRIGGERS

How does the sponsor go about exercising its right to a NERF under the sponsored research agreement? When granting NERF rights under a sponsored research agreement, the C&G Officer should ensure that the obligation to initiate the NERF license process falls on the sponsor

rather than an automatic license agreement issued by the University. The University should require the sponsor to act in order to obtain the NERF rights obligated under the sponsored research agreement. The intellectual property provisions of the sponsored research agreement should require the sponsor to provide written notification (within the election period provided under the terms of the agreement) to the University that the sponsor elects to exercise its right to negotiate a NERF license (or to receive such license depending upon the terms of the agreement) to a particular University invention. The agreement language should indicate that if the sponsor fails to provide a written election notice to the University within the election period, then the University has no further obligation to negotiate such a license with the sponsor and is free to seek other licensing opportunities. Adherence to a formal election and notification process preserves the University's ability to track its license obligations associated with a particular University invention through the campus administrative processes used to issue and monitor license agreements and avoid future conflicts of obligation when licensing the same invention to others. It also makes it more likely that a sponsor will elect only those inventions that it intends to actually make use of.

SUBLICENSING RIGHTS

Sublicensing rights are not implied in the granting of a nonexclusive license absent a specific provision granting such rights. Sublicensing rights under a nonexclusive license are usually not granted by the University for the very fact that the sponsor can then sublicense its rights to other commercial entities in competition with the University's efforts to find other non-exclusive licensees to the same invention and causing the University to lose control over its own IP. The University occasionally encounters such a request where a commercial sponsor expresses concern about its ability to license affiliates that are part of the company's organizational structure. The campus/Laboratory may consider including a sublicensing rights to affiliates provision if there are no specific concerns and if "affiliates" is appropriately defined. The word "affiliates" has no specific legal or business meaning, and could reach to a company's casual relationships - in which case the campus/Laboratory would have no way of knowing to whom the obligations extend. The word "subsidiaries" would be a better choice of terminology, since that has a specific business definition. However, many companies would want to include not only subsidiaries, but parent companies as well. In such cases the C&G Officer should consult with the CLO for appropriate language to address this issue should it arise in the sponsored research agreement negotiations with the sponsor.

The campus/Laboratory should ensure that a provision permitting sublicensing to affiliates does not place any limitations on the University's ability to execute a proper license since the licensing situation can get very complicated when affiliates are included. An example would be a royalty-free internal use only license where the invention turns out to be a drug screening method. This may be appropriate for a company that sells screening tools since they would still need a commercial license to profit from the internal use of the University invention, but it may not be appropriate for an affiliated company in the business of drug discovery, because they could very well profit from the internal use of the University invention (in this latter case, the University would typically license the method to the company for some combination of upfront and annual fees).

The campus/Laboratory could further limit any sublicensing rights under a NERF by including additional requirements such as University approval of a selected sublicensee prior to execution of sublicense, sublicensing for research purposes only, collection of royalties on license and sublicenses at the same negotiated rate, or University prior approval of sublicense terms.

LEGAL INTEGRITY

It is the responsibility of the negotiating University official to carefully and thoroughly review the circumstances of every disclosed or potential invention to protect the interests of the inventor and the University by avoiding conflicting obligations to sponsors of research. Grants of certain nonexclusive rights to sponsors must only be promised after serious consideration has been given to potentially conflicting obligations to other supporters of research, including providers of biological materials. Some factors to be considered include the scope of work to which rights have been committed; potentially overlapping scope with other related projects; the use of project budget consideration to identify the potential involvement of other sponsors; and the NIH policy on "Sharing Biomedical Research Resources" issued on December 23, 1999.

ALTERNATIVES TO A NERF

When a sponsor requests a NERF, it is important to first determine if a NERF is actually needed to accommodate the sponsor's concern. For example, when queried, the sponsor may be concerned that it will take several years to determine if the invention is useful to their product line. In such cases, the campus/Laboratory may consider offering the sponsor the right to take a longer term option to the invention with reasonable fees that reflect the unknown utility of the invention. Often, the NERF requested by a sponsor may not even provide the relief a sponsor is seeking, such as the sponsor's right to enforce a resulting patent against infringing activities by third parties.

Once the campus/Laboratory determines that a NERF really is necessary to meet the sponsor's objectives and is appropriate to grant under the circumstances (i.e., also meets the objectives and goals of the research program), care should be taken in drafting the actual language to assure the potential risks of a NERF are mitigated to the greatest extent possible. For example, a commercial NERF should not be the subject of an outright grant of rights in the research agreement, and should be granted only "to the extent legally permissible."

There are also several ways to mitigate the effect of a NERF on the University mission and licensing activities if the sponsor insists on retaining a NERF right to future inventions made in the performance of the research agreement. To limit the impact of having to provide such NERF rights to the sponsor, the campus/Laboratory should consider the following:

- Limit the NERF to a specific field of use that covers the sponsor's actual business interests, rather than a broad NERF that covers all fields. With a narrow field of use,

the sponsor gets the assurances it seeks to cover its legitimate business interests, but the campus/Laboratory can still pursue other licensing opportunities in other fields, including an exclusive license right if needed;

- For MTAs, limit the NERF to those inventions that necessarily use or necessarily incorporate the material or compound provided for use in the research project. As an alternative, limit the rights to a license to make, use and sell the provided material under inventions that are directly related to the material.

- Limit the time period during which the sponsor may elect to secure a NERF, rather than allowing the sponsor the right to elect a NERF at any time during the 20 year term of the patent;

- Structure a grant-back provision to the University that allows the University to license any unused rights to other third parties. This could be structured to allow the sponsor sufficient time (as determined by the campus/Laboratory) to develop a market for an invention, whereby failure to do so within the prescribed time frame results in such rights reverting back to the University;

- Include a commitment for the sponsor to actively develop the invention in exchange for the NERF. As an alternative, the campus/Laboratory can request that the NERF be terminated if the invention is not either used in a commercial product or under active development by the sponsor after a fixed period of time (such as five years) or upon a trigger event (such as a third party expressing interest in developing the technology on an exclusive basis).

ADDITIONAL RESOURCES

See attached "NERF Quick Reference Guide"