Secretary of Energy Advisory Board

Recommendations Regarding the Application of "Other Transactions Authority" Within the Department of Energy

Report of the External Members The Laboratory Operations Board Industry Partnering/Technology Transfer Working Group

September 24, 2002

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U.S. Department of Energy

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BACKGROUND

The Laboratory Operations Board was charged with assessing the Department of Energy's policies and practices regarding industry partnering and technology transfer. In addition, they were directed to review the advantages and disadvantages to the Department as a whole of special contracting authority, such as "Other Transactions Authority" to enter into contracts with public agencies, private organizations, or individuals on terms that further basic, applied, and advanced research functions.

This latter charge resulted from provisions in the Floyd D. Spence National Defense Authorization Act for Fiscal Year 2001, Section 3163. The Act directed the Secretary of Energy Advisory Board to examine the advantages and disadvantages of providing the Administrator of the National Nuclear Security Administration with special contracting authority such as "Other Transactions Authority." At the request of Senator Bingaman, the assessment was expanded to encompass the entire Department.

DESCRIPTION AND USE OF "OTHER TRANSACTIONS AUTHORITY"

"Other Transactions (OT)" are contracts "other than" standard procurement contracts and financial assistance instruments such as cooperative agreements and grants to fund research and development projects including prototype projects.

Most laws applicable to procurements, cooperative agreements, and grants are not applicable to contracts negotiated under "Other Transactions Authority." Such agreements may be drafted essentially from a "clean sheet of paper" and utilize commercial practices employed by the private sector. They provide for more flexible terms and conditions than the standard financial management and intellectual property provisions typically found in standard contracts.

"Other Transactions" agreements are contract instruments not subject to the federal laws and regulations governing procurement contracts. As such, they are not required to comply with the Federal Acquisition Regulation (commonly known as FAR), its supplements, or laws that are limited in applicability to procurement contracts, such as the Truth in Negotiations Act and Cost Accounting Standards.

A number of Federal agencies already have "Other Transactions Authority" and have been using them successfully for some time. For example, the Departments of Defense, Transportation, and the National Aeronautics and Space Administration have this authority.

BENEFITS AND CONCERNS RELATED TO USE

Benefits

In general, there is widespread agreement that "Other Transactions Authority" provides benefits to the Government. The General Accounting Office (GAO) has reviewed the Department of Defense's implementation of "Other Transactions Authority" on three separate occasions.[1] In 1996, GAO concluded that "other transactions appear to have provided DOD a tool to leverage the private sector's technological know-how and financial investment. The instruments have attracted firms that traditionally did not perform research for DOD by enabling more flexible terms and conditions than the standard financial management and intellectual property provisions found in DOD contracts and grants. The instruments have contributed to reducing some of the barriers between the defense and civilian industrial bases." In 2000, GAO again reviewed DOD's "Other Transactions Authorities" and found that they "provided contractors more flexibility in the business processes and practices they employed than typically provided by standard contract provisions."

In 2000, the RAND Corporation assessed the experience of DOD's use of "Other Transactions Authority."[2] RAND conducted a detailed examination of about one-third of the total population of prototype projects that used "Other Transactions Authority." They found confirmation that the use of "Other Transactions Authority" yielded benefits to DOD. RAND's assessment found that the benefits are broader than the expansion of the industry base. Other important benefits were achieved. They include the following:

1) Significant new industrial resources were participating in DOD prototype projects because of the freedoms inherent in the OT process. RAND found that a new important industrial capability was being drawn from

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[1] *DOD Research: Acquiring Research by Nontraditional Means*, GAO/NSIAD-96-11 (March 1996); Report to the Chairman and Ranking Minority Member, Committee on Armed Services, Subcommittee on Readiness and Management Support, U.S. Senate, *Acquisition Reform: DOD's Guidance on Using Section 845 Agreements Could Be Improved,* GAO/NSIAD–00-33 (April 2000); Testimony of Jack L. Brock, Managing Director, Acquisition and Sourcing Management, and John B. Stephenson, Director, Natural Resources, and Environment, *Intellectual Property: Information on the Federal Framework and DOD's Other Transaction Authority*, GAO-01-980T, July 17, 2001

[2] *Assessing the Use of "Other Transactions Authority" for Prototype Projects*, Documented Briefing, RAND Corporation, National Defense Research Institute, March 2000

segments of major firms that had been focusing exclusively on commercial projects but, with the OT process in place, they were willing to apply their skills and products to DOD activities.

2) Because of the flexibility inherent in the OT process, there were a better use of industry resources and better management of risks and uncertainties that were inherent in either research and development projects or prototype development. Change and adaptability were built into the process. Flexibility inherent in OT agreements permits government and industry managers to make changes, beneficial to the project – as long as it did not affect program goals or overall costs – without costly and time consuming external reviews. This flexibility seemed to provide powerful opportunities to deal with inevitable problems and opportunities that arose during activities of that nature.

3) OT agreements could be written in terms that define the objectives as being general goals and, thus, were not stated in terms of detailed specifications. That allowed the managers, both government and private sector, to observe the evolution of knowledge during the process and adjust the final design or product to match the emerging knowledge base. In addition, goal oriented or milestone related incentives, instead of fixed, inflexible contract specifications, could be incorporated as an integral part of an OT agreement and utilized to guide the progress of the activity. Overall, more effort was devoted to product than to process.

4) OT agreements provided an opportunity to create innovative business relationships that were associated with a particular project requirement. For example, government and private sector managers could negotiate prior to an award yielding a more focused statement of work. Such interactions can suggest, for example, that the needs of the government may be better served by the creation of industry partnerships or consortia. OT agreements provided opportunities to establish such contractual arrangements that might otherwise be prohibited under standard Federal government contracting regulations.

5) An OT agreement can provide the government manager an opportunity to become directly involved in project activities down to the subcontractor level. Such provisions, giving visibility at that level of activity, gives the manager a much better understanding of the project's true status. The manager no longer has to rely solely on information the prime contractor chooses to make available to the customer. This enhanced information flow permits the manager to play a more active and potentially constructive role in the activity.

6) Use of an OT agreement leverages private investment through sharing of costs, risks and benefits and could yield more value per dollar of government resources invested. This was thought to be a difficult metric to quantify, but the RAND researchers believed that the assertions of government and private sector managers have validity because the logic and mechanisms underlying those claims appeared reasonable. Cited were several elements: reduced transaction costs; sharing of risks and costs; reduced overhead costs; and cost avoidance resulting from lesser amount of formal oversight and internal project reporting.

7) Although the RAND report noted risks to the government through the relaxation of some financial oversight and ownership of intellectual property requirements, they concluded that the immediate rewards substantially outweighed those risks. Specifically RAND found that "if the flexibility in negotiating intellectual property and financial audit clauses is removed from the OT authority, most if not all of the new industrial resources would again become unavailable to DOD."

Concerns

There are important the perceived benefits associated with using "Other Transactions Authority" for prototype development projects. However, there are some general concerns that should be noted if such authority is provided to the Department for use not only for prototype development projects but also for research and development activities and demonstration projects.

Those concerns are

1) Loss of Intellectual Property Rights and Lack of Traditional Cost Standards

With regard to intellectual property rights and lack of traditional cost accounting requirements, as noted, overall the RAND study found OT to be beneficial. However, the study also stated "because program management under OT can potentially remove the traditional oversight and accountability processes, critics have been concerned that DOD's interests might not be adequately protected. In particular, the lack of traditional cost accounting and auditing procedures could expose DOD to greater financial risk. Lack of ownership from intellectual property resulting from OT development activities could constrain future innovations or impose future costs on the government because of limits on licensing the technology. Similarly, the lack of technical data obtained under OT could adversely affect DOD's ability to support systems using that technology. These are serious concerns that should be addressed before OT is more widely applied."

2) Less Competition for Follow-on Procurements

There could be less competition for a follow-on procurement resulting from technology developed through an OT because the private OT parties may retain more data than usually would be available to the Government to disseminate to prospective offerors. The OT participants therefore may be in a better position to win any competition.

3) Less Public Access to Data

Hypothetically, for projects where there is the expectation of significant commercial payoff for products developed under OT agreements, it is possible that there will be less public access to data paid for by the Government if OT participants are able to retain more rights than usual to the intellectual property developed under an OT. Accordingly, this could also mean there would be less data available to stimulate commercialization of research resulting from OT.

4) Longer Negotiating Time

The time required to negotiate an OT agreement is often times more lengthy because both parties are working from a "blank slate." Considerable time is spent developing terms and conditions. An expectation with respect to this would be, given experience on the part of both government and private sector participants, that negotiation durations would become shorter over time with experience and the use of more "standardized" OT agreements.

5) Difficulty in Establishing Metrics to Measure Success

RAND found that it was difficult to establish metrics to measure the success of OT. RAND reported, "one important element of our research was to develop a set of metrics that would measure the relative effects of OT on program outcomes and OT's broader policy goals. While attempting to accomplish this, we were unable to develop any practical quantifiable metrics that others would find credible. The few quantifiable metrics we uncovered are either misleading (*e.g.*, the number of nontraditional contractors) or unverifiable (*e.g.*, cost avoidance). This result affects both the kind of information we can present and the kind of conclusions that can be drawn . . . Thus, we rely largely on qualitative information in this analysis—the judgments and opinions of experienced managers who have run both types of programs."

6) Unfavorable Terms for the Government/Training Requirements

DOD users of OT agreements have suggested that some OT agreements they worked with had terms and conditions less favorable to the Government than standard Federal Acquisition Regulations (FAR) terms and conditions. One

example given was the Government's inability to unilaterally request a change, as is permitted under the standard FAR Changes clause. Another problem was a negotiated term that expanded permissible excusable delays beyond those in the standard FAR termination clause. Under one agreement, the private company had the right to unilaterally stop performance. In another instance, the Government had difficulty obtaining title to a product because of the agreement between the private party and its subcontractor.

Arguably the Government should be able to negotiate the terms and conditions it needs for a given OT. However, these officials believed that because Government negotiators are used to taking for granted the unique provisions in the FAR that protect the Government (*e.g.*, the unilateral right to request changes for a project or terminate an agreement), they may not be careful enough in making sure that the Government is adequately protected and fully appreciate a different type of change or termination provision.

In this regard, the RAND study also noted that: "the quality of an Agreement is more closely associated with the skills and experience of the government and industry managers and contracting officers, than a traditional FAR-based contract." While the study did not cite this as a negative, it does, however, show the importance of having negotiators trained in negotiating commercial contracts serve as "Agreements Officers." The Department of Defense, Office of Procurement, for example, offers an extensive training program course for individuals involved in OT agreements. This course could be used as a basis for a similar one within the Department of Energy.

7) Proliferating Reporting Requirements

Because the use of OT agreements is relatively new, there appears to be a natural self-protective institutional effort to collect more information on the OT agreements in order to forestall potential criticisms concerning mismanagement, intellectual property give-aways, etc. DOD officials have noted that proliferating reporting requirements on the use of OT may offset any other administrative benefits to OT. According to these officials, every year there are new reporting requirements on the use of OT so ultimately OT may not result in overall savings regarding administrative requirements.

8) Possible Audit/Access Requirements

As noted, one of the key perceived benefits of OT has been the ability to utilize commercial audits and be free of Government intrusion into financial records. DOE may be asked about what type of access and audit policies it may issue regarding OT participants in the event it is granted OT authority.

RELEVANCE TO THE DEPARTMENT'S NATIONAL LABORATORIES

A more specific concern is the issue of whether the Department's National Laboratories should have the authority to negotiate "Other Transactions" agreements and, if so, under what circumstances.

There are a number of subordinate issues associated with the Department's National Laboratories having "Other Transactions Authority." They are:

1) Effects of Authority to Negotiate Intellectual Property Rights

A key attraction for companies interested in entering into DOD OT agreements has been the inapplicability to OT of the Bayh-Dole Act governing rights to intellectual property. This statute guarantees to non-profits, universities, and small businesses that make an invention under a Government funding agreement subject to the Bayh-Dole statute ownership of the invention regardless of whether the party contributed funds pursuant to the agreement. By Executive Order, the principles of Bayh-Dole invention ownership have been extended to all types of parties to government funding agreements, to the extent permitted by law. DOE and the National Aeronautics and Space Administration are the two agencies having separate statutes whereby Bayh-Dole does not extend to all types of contractors. Thus, right now if a DOE National Laboratory enters into an agreement with a Bayh-Dole subcontractor (*e.g.*, non-profits, universities, or small businesses) and the subcontractor makes an invention under the agreement, the subcontractor owns the invention.

However, if the agreement between the DOE National Laboratory and the subcontractor were considered to be an OT, the Bayh-Dole Act would not apply. This would mean the power to determine who owns the rights to an invention pursuant to an agreement might be in the hands of the entity awarding the agreement; *i.e.*, the agreement would determine the rights to the invention. Although theoretically, a small company seeking to work with a laboratory could negotiate intellectual property rights with the laboratory, the ability to negotiate intellectual property rights would give the laboratory a negotiating leverage advantage it would not otherwise have if the agreement were not an OT.

Flexibility to negotiate intellectual property rights pursuant to an OT also means that ancillary intellectual property right provisions will be negotiable; *e.g.,* DOE or National Laboratories would have the ability to negotiate the Government license for a subject invention as well as a time limit as to when Government march-in rights may be exercised. If DOE National Laboratories were granted OT authority, they would have the ability to negotiate these rights with subcontractors. Again, DOE may wish to consider whether any limits should be placed on such authority to ensure that small businesses are treated fairly by the laboratories.

2) Types of Agreements DOE National Laboratories May Negotiate

If DOE National Laboratories are granted OT authority, it may be useful to consider the range and type of financial agreements that could conceivably benefit the missions of DOE laboratories. Put another way, it may be asked what OT authority would enable DOE National Laboratories to accomplish that cannot now be accomplished.

3) Exercise of Authority

Another question is how DOE National Laboratories might exercise OT authority. For example, right now if DOE National Laboratories issue a subcontract for research and development, the laboratory does not obtain rights to a subcontractor's invention. If a laboratory had OT authority, the question may arise whether the laboratory would be free to negotiate rights on behalf of the laboratory.

4) Limitations on Negotiating Authority

When considering whether DOE National Laboratories should have OT authority, other issues may include whether it would be useful and appropriate to place certain limitations on the negotiating authority; *e.g.*, based on type of project, dollar amount, intellectual property transfer questions and DOE Headquarters Contracting Officer review requirements.

5) Reporting Requirements

If DOE National Laboratories are granted OT authority, it is likely that some type of reporting requirements will be necessary in order to judge whether and under what circumstances the authority has proved useful. Since DOE National Laboratories already are concerned about the level of reporting requirements, it may be useful to determine a priori what reporting requirements would be warranted for OT.

RECOMMENDATIONS

The Industry Partnering/Technology Transfer Working Group of the Laboratory Operations Board has reviewed this issue and has weighed the pros and cons of the use of "Other Transactions Authority" by the Department of Energy and its National Laboratories.

None of the concerns raised above are "show stoppers" and the potential benefits appear to far outweigh any disadvantages. We believe that the concerns, as noted, can be appropriately addressed by the Office of Procurement & Assistance Management working in conjunction with Office of General Counsel, Program

Offices, and the National Laboratories in the development of guidelines for use of such authority.

Therefore, based on the evaluation, we recommend the following:

1) **The Working Group recommends that the Department of Energy would benefit from special contracting authority such as "Other Transactions Authority."** The Working Group believes that, as discussed, there are important benefits for the Department and other public agencies and/or private organizations and individuals to be derived from the use of innovative contracting vehicles such as "Other Transactions Authority." **The contracting vehicle should be limited to research and development programs, prototype development, and demonstration projects.**

2) **The Working Group further recommends that the National Laboratories also be given the right to utilize "Other Transactions Authority."**

3) **The Working Group can see no reason to limit the application of "Other Transactions Authority" to only the National Nuclear Security Administration to the exclusion of the rest of the Departmental complex.** It appears to have equal validity for use by all elements of the Department of Energy and we would so recommend.

4) The Working Group is aware of the fact that currently the Department does not have authority to enter into "Other Transactions Authority" arrangements. It understands, however, that Congress is in the process of conferencing on the Energy Policy Act of 2002 (H.R. 4) in order to reconcile differences between the Senate and House Bills. The Senate version of H.R. 4 contains, in Section 1410, provisions related to " Other Transactions Authority" while the House Bill does not. The language in Section 1410 would provide the Department with the authority to "enter into other transactions with public agencies, private organizations, or persons on such terms as the Secretary may deem appropriate in furtherance of basic, applied, and advanced research functions now or hereafter vested in the Secretary."

   The Working Group endorses the provisions regarding "Other Transactions Authority" in the Senate Bill and recommends that the Department express its support for it during the ongoing Conference.

5) **The Working Group recommends**, should authority be forthcoming as a result of enactment of the Energy Policy Act of 2002, **that the Department's Office of Procurement & Assistance Management develop guidelines** similar to those developed by the Under Secretary of Defense for Acquisition and Technology (January 2001**) to provide a framework for implementation**. The Working Group further recommends that such implementation guidelines be developed in conjunction with the Office of General Counsel, Program Offices, and the National Laboratories. The Guidelines should specifically address the issues raised in the discussion above entitled "Relevance of Other Transactions Authorities to DOE Laboratories."

6) Further, the **Working Group recommends** that the Department emphasize the importance of **targeting a substantial portion of any "Other Transactions Authority" agreements to small and medium sized businesses** in recognition of the innovative role they play in cutting edge research and development in partnering with the National Laboratories. OT agreements should not, however, be limited solely to small and medium-sized businesses.

7) The **Working Group recommends that the Department develop appropriate training programs** to ensure that contracting officials possess suitable background and training in negotiating Other Transaction Authority agreements in order to assure that the government's rights are protected. Such training is available from other federal agencies having authority to enter into OT agreements. Taking advantage of such training programs should facilitate and make more effective the department's activities in this area.

8) Finally, the **Working Group recommends** that, after the Department has utilized "Other Transactions Authority" for a period of three to five years, **an assessment be conducted to evaluate the effectiveness of "Other Transactions Authority" in assisting the Department in carrying out its missions.**