| Employment and Training Administration<br>Advisory System<br>U.S. Department of Labor<br>Washington, D.C. 20210 | **CLASSIFICATION**<br>Grants/Intellectual Property |
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**TRAINING AND EMPLOYMENT GUIDANCE LETTER No.** 31-04

**TO:** ALL STATE WORKFORCE LIAISONS
ALL STATE WORKFORCE AGENCIES
ALL ONE-STOP CENTER SYSTEM LEADS

**FROM:** EMILY STOVER DeROCCO
Assistant Secretary

**SUBJECT:** Payment of Royalties on Intellectual Property Created with Federal Grant Funds

1. Purpose. To advise states of the general principles that apply to the payment of royalties on intellectual property that was created using Federal grant funds.

2. References. The Copyright Act of 1976 (17 U.S.C. 101 et seq.); 29 CFR Part 97, "Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments;" and Office of Management and Budget (OMB) Circular No. A-87 (Revised), "Cost Principles for State, Local, and Indian Tribal Government."

3. Background. Recently, states have been asked by private entities to pay royalties for the use of computer software that was created using Federal funds. Under current Federal law, a state may not use Federal funds to pay royalty fees for any product developed with Federal funds unless the Department has, as discussed below, waived its rights to the product. This advisory discusses the basis for this position and provides additional guidance.

4. Discussion. In general, an entity that retains ownership of a product with an intellectual property component (such as a copyright) may require payments for the use of such products. The term commonly used to describe these payments is "royalties." Specifically, royalties are

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payments for the privilege of using another entity's patents, copyrights, secret processes and formulas, trademarks, and similar intellectual property. As the term is used in this advisory, royalties may include both one-time and periodic payments. Under Federal grant law, royalties are payable from grant funds only under specific circumstances.

A copyright in a product refers to a property right provided under Federal law to owners of original works of authorship, which include computer software, printed literature, sound recordings, visual works, and other original works of creativity. (See 17 U.S.C. 101, 102.) Where the recipient of a grant has created a product with Federal funds, it generally owns, and retains, the copyright in the product. As the owner of the product, the recipient generally has the exclusive right to reproduce, distribute, display, perform publicly, and modify the product, and may legally prevent others from exercising such rights. In addition, the grant recipient/copyright owner may exploit the product commercially by demanding royalties from others for the use of its product.

However, there is an important limitation on the grant recipient's copyright rights. Under Department of Labor regulations, the Department—

> reserves a royalty-free, nonexclusive, and irrevocable license to reproduce, publish, or otherwise use, and to authorize others to use, for Federal Government purposes:
>
> (a) The copyright in any work developed under a grant, subgrant, or contract under a grant or subgrant [funded by the Department]; and
>
> (b) Any rights of copyright to which a grantee, subgrantee or a contractor purchases ownership with grant support [from the Department]. [29 CFR 97.34.]

As a result, when a state uses Departmental grant funds to develop (or engage a vendor to develop) a product or to acquire ownership in a product, the Department automatically reserves the right to reproduce, publish, and otherwise use the work for Federal purposes. This reservation of rights applies unless the applicable grant provides otherwise. However, no Departmental grant is currently known to waive this right. In addition, the Department may authorize others to use, but *not* reproduce or publish the product, for Federal purposes. This principle of law is supported by Respect Incorporated v. Committee On the Status of Women, d/b/a Project Respect, 815 F. Supp. 1112, 1122 (N.D. Ill. 1993).

Unless this license of use is expressly waived by the Department under the terms of the particular grant under which the product was created, a second state seeking to use products created under that first grant may not use Federal funds to pay a royalty for the use of such products. Such a cost is not considered allowable under Departmental regulations. Specifically, 29 CFR 97.22 provides that whether a cost is allowable by a state grantee will be determined in accordance with OMB Circular No. A-87. That Circular provides that:

> Royalties on a patent or copyright or amortization of the cost of acquiring by purchase a copyright, patent, or rights thereto, necessary for the proper performance of the award are allowable unless:
>
> > (1) The Federal Government has a license or the right to free use of the patent or copyright. . . . [Attachment B, Section 38, as revised May 10, 2004.]

This rule essentially protects the Federal government from paying twice for the product/license. As a result, a state seeking to use a product previously developed with Department grant funds for Federal purposes (which includes administration of a Federal grant), should take appropriate steps to obtain a free copy. (See item "c." in "Action Required" below.)

Note that, while states may not use Federal funds to pay a royalty, they may use Federal funds to pay for other costs related to the acquisition of the product. For grant programs in general, costs are allowable if they are necessary, reasonable, and benefit the particular grant. Thus, allowable costs related to the acquisition of the product might, for example, include shipping costs for delivery, or costs for a service tied to the operation of the product, such as maintenance fees.

5. Examples.

a. A state used Federal unemployment insurance (UI) administrative grant funds to pay a vendor to develop computer software for administering that state's UI program. Under the state's contract with the vendor, the state retains ownership of this software and the vendor has the right to sell/license copies of the software to others. The vendor is required to pay the state a royalty on each sale it makes of the software. When a second state published a Request for Proposal for the development of similar software for use in its UI program, a responding vendor included in its bid the costs of using the first state's software, including the royalty fee that the vendor is required to pay to the first state.

In this case, the second state may not use Federal funds to pay royalty fees because the product - computer software – was developed with Federal funds. As noted above, an exception is if the Department has waived its rights to the product; no Departmental grant currently waives this right. However, the second state may use Federal funds to modify the computer software for its own use or otherwise enhance the software.

b. The Department contracted with a vendor to develop software to quickly and accurately assign occupational codes for job applicants and job openings. The vendor that developed this software – called AutoCoder - retains the copyright and is offering a modified version to the states under different names.

In this case, a state may not use Federal funds to purchase the original AutoCoder software. As discussed above, the Department reserves a royalty-free, irrevocable license to reproduce and "authorize for use" products developed with its grant funds. Since AutoCoder is such a product, a free copy of AutoCoder is available to all states. (See item "c." in "Action Required" below.) However, states may use grant funds to develop their own enhancements to AutoCoder or to purchase enhancements, and for services related to the product, such as updates or maintenance fees.

6. Action Required. State administrators should take the following actions:

a. Distribute this advisory to appropriate staff.

b. Have staff review any contracts requiring the payment of royalties for the use of a particular product. If the product was developed or purchased under a Federally funded grant, and if the Department has not waived its license for the use of such a product, states may not use Federal funds to pay a royalty for the use of the product.

c. If a vendor refuses to provide the product without the payment of royalties, states seeking to use the product for a Federal purpose should request a free copy of the product from the Department or the state for which the product was first developed or purchased, if that state holds either the copyright or the licensing rights.

7. Inquiries. Direct questions to the appropriate Regional Office.