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UNIVERSITY OF CONNECTICUT

Office of the Executive Vice President for
Administration and Chief Financial Officer
Treasury Services
John D. Sullivan, MBA, CFA
Manager of Treasury Services

To: Scott Jordan – Executive Vice President for Administration and Chief Financial Officer
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From: John D. Sullivan, CFA
Manager of Treasury Services

Date: November 12, 2015

RE: TAX-EXEMPT COMPLIANCE: PRIVATE USE OF UCONN 2000 FINANCED PROJECTS

Review of Potential Private Activity/Use

We appreciate continued assistance in keeping us informed on private activity/use related to any UCONN 2000 debt financed assets by forwarding any documents concerning any private use of any tax-exempt bond funded asset including leases, management contracts, private payments, provisions of services (e.g. utility or other services), Technology incubation and cooperative ventures to the Office of Treasury Services.

It is best if the EVPA/CFO's Office of Treasury Services and the University's Tax Counsel to review such potential uses prior to entering into an agreement. Please continue to forward these contracts, leases, management use agreements and other types of uses to Treasury Services for review and inclusion in the tax-exempt compliance process. Please note the nomenclature is not determinative of the IRS interpretation of private use. Even if private use is safe harbored, the University must report the private use in its tax-exempt analysis.

Once again our goal is to accommodate the University wishes within the tax-exempt debt regulatory compliance framework.

Private Activity/Use/Payment/Tracking & Analysis

UConn's Executive Vice President for Administration and Chief Financial Officer signs the tax regulatory certificate and the ability to issue tax-exempt debt is at the heart of the UCONN 2000 program. The IRS has many complicated regulations and requirements that we must comply with in order for the debt to remain tax-exempt. This memo is intended to provide a brief overview of the private activity/sponsored research tax-exempt compliance use of UCONN 2000 debt funded assets by other entities. Basically, we need to know what private activity/use is going on with UCONN 2000 assets so we can be sure that we do not exceed the IRS limits on private use. For example, generally speaking a bond is only tax exempt if 10% or less of bond proceeds are used for any related private business use and 10% or less of principal or interest costs of the bonds are paid off with private funds.

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Private Activity/Use

Private activity/use can be thought of as the use of any tax-exempt debt funded asset by any private entity. Some examples of possible private activity/use are: a food restaurant leasing space in the Stamford Campus, a private company managing one of the UConn Parking garages, or an entity occasionally using space in a building on terms other than those available to the general public. We rely on UConn & UConn Health departments including, Office of Research, Office of Sponsored Program Services, Planning Architectural & Engineering Services, General Counsel, and/or the Attorney General's Office to forward private activity/use information to us usually in the form of leases, management contracts, and agreements for UConn owned assets. For these and any other private activity/use of a UCONN 2000 debt funded asset, we need to know about it to conform to the tax-code exceptions and to update our Tax-Compliance questionnaires that are filed with Tax Counsel and the State.

Another type of Private activity/use is related to research, such as a private or federal entity having use of research space/assets at the University. Some of the reporting for this type of private activity has flowed from the Office of Research and Office of Sponsored Program Services. Often UConn internal policies may meet the IRS safe harbors.

Please note that some uses considered to be private activity by the IRS are not intuitive, such as the use of UConn tax-exempt funded assets by other tax-exempt entities such as the UConn Co-Op and the U.S. Government. The sale of an asset that was funded with tax-exempt debt can also be considered private activity. For example if one provides certain tax-exempt debt funded services such as water, sewer, or electricity to private entities, it could be considered private activity.

IRS Compliance is Important – Downside Risk

While the IRS tax-exempt debt rules and regulations are complicated, it is important to comply with them. The downside risk is onerous, and in these circumstances, an ounce of prevention is worth a pound of cure. For example, failure to comply can result in the loss of tax-exemption on the University's debt in arrears which can engender bondholder lawsuits for damages, regulatory penalties, indenture non-compliance, credit rating downgrades, adverse impacts nationally for UConn debt in capital markets, loss of international reputation, inability to sell new debt, adverse audit reports, increased debt service costs, and the State's revocation of the ability to issue debt, and other collateral damage, etc.

Treasury Services IRS Compliance Program

Fortunately, Treasury Services has a program in place for compliance, including the use of allowed private activity percentages and safe harbors that if followed, meet the IRS requirements and regulations.

Attached for your informational use please find:

1.) The Treasury Services Private Activity Tax-Exempt Compliance Procedures

2.) The Safe-Harbor Management Contract Guidelines

3.) The Safe-Harbor Guidelines For Research Agreements

Percentage of Bond Proceeds Available for Private Activity is Restricted

Certain small percentages of bond issues can be used for related and unrelated private activity ("bad use"). Because of the complicated nature of the IRS regulations, and other factors, such as Connecticut General Statues and the indentures, that we must follow, the application of these allowed percentages needs to be considered case by case for each use and each debt issue.

Safe Harbors

The IRS allows safe harbors for private activity that does not use up the restricted percentages. If possible it may be best to maximize the University's use of these safe harbors. It may be the case that most of the University's present and planned private activity and research use already meets the guidelines. Additionally, it is respectfully offered for your consideration, that perhaps many University contracts can incorporate the IRS safe harbor requirements without losing the business and other opportunities that the University wishes to achieve. If so, this could free up the limited "bad use" options available to us.

Thank you for your assistance in making the UCONN 2000 program a successful one!

If you have any questions, comments, or suggestions or if I may be of any assistance, please do not hesitate to contact me at 860-486-5907.

JDS/kjm
Enclosures

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TAX-EXEMPT COMPLIANCE QUESTIONAIRES: PRIVATE ACTIVITY AND PRIVATE RESEARCH USE OF UCONN 2000 TAX-EXEMPT DEBT FINANCED ASSETS

TREASURY SERVICES TAX EXEMPT DEBT PRIVATE ACITIVITY/USE COMPLIANCE PROGRAM

In order to meet the stringent IRS regulations the Tax-Exempt Questionnaires request certain information that includes the actual and/or expected private activity use or research use of any bond funded asset. Fortunately, the IRS does allow such private activity or research use if they meet certain IRS "safe harbors". If the safe harbors are not met, only a small percentage of the University's tax-exempt bond funded assets may be used for private activity or research use.

Fortunately we have a program in place for compliance, including the use of allowed percentages by the IRS and safe harbors, that if followed meet the IRS requirements and regulations.

The General Tax-Exempt Private Activity/Use/Payments Compliance Program Steps Are:

(1) The University should try to make use of the attached safe harbors where possible including those for sponsored research. General University policies that incorporate these safe harbors will go along way towards meeting the IRS regulations.

(2) Information for each UCONN2000 Project is provided to Treasury Services including private activity and sponsored research uses, such as contracts, square footage, the use of space, leases, payments, etc.

(3) Treasury Services analyses the information, and shares it with tax (bond) counsel for their analysis.

(4) Bond Counsel updates their records accordingly and may supply a tax-exempt compliance letter when requested. This is required for State contract approval in many instances.

(5) Treasurer Services produces a Tax-Exempt Questionnaire for each UCONN 2000 project for signature of the CFO, etc. and filing with bond counsel. These forms serve as the basic document for the University's Tax Regulatory Certificate/Agreement/Certificate, and also meet certain State filing requirements.

(6) Tax-Counsel relies on the questionnaires to produce the Tax Regulatory Certificate/Agreement which is a prerequisite for any UCONN2000 tax-exempt debt can be issued. This serves as the compliance document to meet the Internal

Revenue Service regulations and requirements. It is generally attested to by UCONN and the State Treasurer.

(7) The TRA is an essential document behind tax-counsel granting a tax-exempt opinion which allows the University to issue bonds that are exempt from federal taxes.

(8) This is a reiterative process as the information changes and projects are added or reallocated.

(9) The University's senior management signs the Tax Regulatory Certificate/Agreement and other tax-exempt debt documents and are ultimately responsible for them. Treasury Services relies on other areas of the University to provide the required information.

RELATED INFORMATION:

Private Activity/Use: Private activity and private use, can be thought of as the use of any tax-exempt debt funded asset by any private entity. For example if a food restaurant leases space in the Stamford Campus, or a private company manages a UCONN Parking garage, both can be considered private activity. Also if a private entity has use of research space at the University that can be considered private use. Some uses considered to be private activity by the IRS are not so intuitive, such as the use of UCONN tax-exempt funded assets by other tax-exempt entities such as the UCONN Co-Op and the U.S. Government. Also, for example if one provides certain tax-exempt debt funded services such as water, sewer, or electricity to private entities, you can have private activity/use.

Downside Risk of Failure to Comply with IRS Rules: The IRS regulations are quite complicated. Failure to follow them can have onerous consequences such as: the loss of tax-exemption on the University's debt in arrears which can engender bondholder lawsuits for damages, regulatory penalties, indenture non-compliance, credit rating downgrades, adverse impacts nationally for UCONN debt in capital markets, loss of international reputation, inability to sell new debt, adverse audit reports, increased debt service costs, and the State's revoking of the ability to issue debt, and other collateral damage, etc.. The downside risk is onerous, and in these circumstances, an ounce of prevention is worth a pound of cure. Fortunately we have developed a compliance system that includes certain "safe harbors" that if met automatically satisfy the IRS requirements.

Safe Harbors - The University can meet IRS requirements by meeting the safe harbors for private activity use and research use in the attached "The Safe-Harbor Management Contract Guidelines" for private activity, and the "Safe Harbor Guidelines for Research Agreements".

For projects that do not meet the safe harbor guidelines, there is a threshold on the amount of private activity use and/or research use that is permitted with tax-exempt bond funded assets. However, it may be that most of the University's present and planned private activity and research use already meet the guidelines. If so, this would free up the limited amount of allowable "bad" use for where it is unavoidable.

Contact people should be made aware that "safe-harbors" and other exceptions to the IRS requirements exist for private use and research use, and that they should not enter into any agreement that would jeopardize the tax-exemption of the UCONN 2000 Bonds. Consequently, as people enter into agreements, etc. and provide the information to fill out the questionnaires, they should be cognizant of any private use or research use that meets these safe-harbors or other exemptions to the IRS requirements.

Allowable Percentages: If they do not meet the safe harbor guidelines, certain small percentages of bond issues can be used for related and unrelated private activity. Because of the complicated nature of the IRS regulations any such application of percentages should be uniquely considered for each use and each bond issue by Treasury Services and tax-counsel.

Safe-Harbor Management Contract Guidelines

General Rule.

A contract for the management, services rendered at or incentive payment in respect of, a bond-financed facility that meets the safe-harbor guidelines summarized below would be permitted. Conversely, a contract that does not meet such guidelines would generally not be permitted. All contracts must be reviewed on a case-by-case basis.

Permitted Compensation Arrangements.

The compensation paid to the service provider must be reasonable and no compensation may be based, in whole or in part, on a share of net profits from the operation of the facility. Reimbursement of the service provider for actual and direct expenses paid by the service provider to unrelated persons is not by itself treated as compensation. Compensation based on (a)(i) a percentage of gross revenues or adjusted gross revenues of a facility or (ii) a percentage of expenses from a facility, but not both, (b) a capitation fee or (c) a per unit fee is generally not considered to be based on a share of net profits. A productivity reward equal to a stated dollar amount based on increases or decreases in gross revenues (or adjusted gross revenues), or reductions in total expenses (but not both increases in gross revenues (or adjusted gross revenues) and reductions in total expenses) in any annual period during the term of the contract, generally does not cause the compensation to be based on a share of net profits. "Adjusted gross revenues" is defined to mean all gross revenues of all or a portion of a facility, less allowances for bad debt and contractual and similar allowances.

If the compensation agreements of a management contract are materially revised, the requirements for compensation arrangements are retested as of the date of the material revision and the management contract is treated as one that was newly entered into as of the date of the material revision.

The types of compensation arrangements permitted to be entered into are as follows:

(a) 95% periodic fixed fee arrangements, wherein at least 95% of the compensation for services for each annual period during the term of the contract is based on a periodic fixed fee which is a stated dollar amount for services rendered for a specified period of time. The stated dollar amount may automatically increase according to a specified objective external standard that is not linked to the output or efficiency of a facility, *e.g.*, the Consumer Price Index and similar external indices that track increases in prices in an area or increases in revenues or costs in an industry are objective external standards. A fee shall not fail to qualify as a periodic fixed fee as a result of a *one-time* incentive award during the term of the contract under which compensation automatically increases when a gross revenue or expense target (but not both) is reached if that award is a single stated dollar amount. The term of the contract, including all renewal options, must not exceed the lesser of 80% of the reasonably expected useful life of the financed property and 15 years.

(b) 80% periodic fixed fee arrangements, wherein at least 80% of the compensation for services for each annual period during the term of the contract is based on a periodic fixed fee. The term of the contract, including all renewal options, must not exceed the lesser of 80% of the reasonably expected useful life of the financed property and 10 years. A one-time incentive award during the term of the contract similar to the award described above is permitted under this option as well.

(c) 50% periodic fixed fee arrangements, wherein either at least 50% of the compensation for services for each annual period during the term of the contract is based on a periodic fixed fee or all of the compensation for services is based on a capitation fee or combination of a periodic fixed fee and a capitation fee. A capitation fee is a fixed periodic amount for each person for whom the service provider or the State and local governmental unit assumes the responsibility to provide all needed services for a specified period so long as the quantity and type of services actually provided to covered persons varies substantially; *e.g.*, a fixed dollar amount payable per month to a medical provider for each member of a health maintenance organization plan for whom the provider agrees to provide all needed medical services for a specified period. A capitation fee may include a variable component of up to 20% of the total capitation fee designed to protect the service provider against risks such as catastrophic loss. The term of the contract, including all renewal options, must not exceed five years. The contract must be terminable by the State and local governmental unit upon reasonable notice without penalty or cause, at the end of the third year of the contract.

(d) Per-unit fee arrangements, wherein all of the compensation for services is based on a per-unit fee or a combination of a per-unit fee and a periodic fee. A per-unit fee is defined to mean a fee based on a unit of service provided specified in the contract or otherwise specifically determined by an independent third party, such as the administrator of the Medicare program or the State and local governmental unit; *e.g.*, a stated dollar amount for each specified medical procedure performed, car parked or passenger mile is a per-unit fee. Separate billing arrangements between physicians and hospitals generally are treated as per-unit fee arrangements. The term of the contract, including all renewal options, must not exceed three years. The contract must be terminable by the State and local governmental unit on reasonable notice, without penalty or cause, at the end of the second year of the contract term.

(e) Percentage of revenue or expense fee arrangements, wherein all of the compensation for services is based on a percentage of fees charged or a combination of a per-unit fee and a percentage of revenue or expense fee. During the start up period, however, compensation may be based on a percentage of either gross revenues, adjusted gross revenues or expenses of a facility. The term of the contract, including renewal options, must not exceed two years. The contract must be terminable by the State and local governmental unit on reasonable notice without penalty or cause, at the end of the first year. This type of contract is permissible only with respect to contracts under which the service provider primarily provides services to third parties (*e.g.*, radiology services to patients), and management contracts involving a facility during an initial start up period for which there have been insufficient operations to establish a reasonable estimate of the amount of the annual gross revenues and expenses (*e.g.*, a contract for general management services for the first year of the operations).

Renewal Option.

A renewal option, for purposes of the foregoing, is defined to mean a provision under which the service provider has a legally enforceable right to renew the contract. Thus, for example, a provision under which a contract is automatically renewed for one year periods absent cancellation by either party is not a renewal option, even if it is expected to be renewed.

Cancellation Penalty.

A cancellation penalty is defined to include a limitation on the State and local governmental unit's ability to compete with the service provider, a requirement that the State and local governmental unit purchase equipment, goods or services from the service provider, and a requirement that

the State and local governmental unit pay liquidated damages for cancellation of the contract; compare a requirement effective on cancellation that the qualified user reimburse the service provider for ordinary and necessary expenses or a restriction against the State and local governmental unit hiring key personnel of the service provider is generally not a contract termination penalty. Another contract between the service provider and the State and local governmental unit, such as a loan or guarantee by the service provider, is treated as creating a contract termination penalty if that contract contains terms that are not customary or arm's length, that could operate to prevent the State and local governmental unit from termination the contract (*e.g.*, provisions under which the contract terminates if the management contract is terminated or that places substantial restrictions on the selection of a substitute service provider).

No Relationship with State and Local Governmental Unit.

The service provider must not have any role or relationship with the State and local governmental unit, that, in effect, substantially limits the qualified user's ability to exercise its rights, including cancellation rights, under the contract, based on all the facts and circumstances. This requirement, amongst others, is satisfied if (a) not more than 20% of the voting power of the State and local governmental unit in the aggregate is vested in the service provider and its directors, officers, shareholders and employees; (b) overlapping board members do not include the chief executive officers of the service provider or its governing body or the State and local governmental unit or its governing body; and (c) State and local governmental unit and the service provider under the contract are not related persons. A related person means, generally, a member of a controlled group, or any person having a 50% ownership or voting interest in the subject entity.

Safe-harbor Guidelines for Research Agreements

Revenue Procedure 97-14:	Revenue Procedure 97-14 provides the safe-harbor guidelines for research agreements involving the use of facilities financed with proceeds of tax-exempt bonds.
Consequence of Failure to Comply with Guidelines:	If the guidelines are met, a research agreement is considered not to create any impermissible private activity. Conversely, if the guidelines are not met, impermissible private activity may be considered to be created. If the research agreement causes the applicable private activity limits to be exceeded and no remedial action is taken to cure the violation, interests on the bonds may become subject to federal income taxation retroactive to the date of issue of the bonds.
Certain Caveats:	All facts and circumstances must be analyzed in determining whether private activity is created by any research agreement. Private activity will result from research agreements with respect to bond financed property if the nongovernmental sponsor is treated as the lessee or owner of such property for federal income tax purposes.
Basic Research Requirement:	The research agreement must be for "basic research." Basic research means any original investigation for the advancement of scientific knowledge not having a specific commercial objective. For example, product testing supporting the trade or business of a specific nongovernmental person is not treated as basic research.
Definition of Sponsor and Qualified User:	A sponsor means any person, other than a qualified user, that supports or sponsors research under a contract. A qualified user means any state or local governmental unit or a section 501(c)(3) organization if the financed property is not used in an unrelated trade or business of such section 501(c)(3) organization. The federal government, including any federal agency or instrumentality, is not a qualified user.
Two Permitted Arrangements:	*Corporate Sponsored Research.* Under this arrangement, the research agreement must provide that any license or other use of the resulting technology by the sponsor of the research be on the same terms and for the same price as UConn or the State would enter into with any unrelated, non-sponsoring party. The sponsor must pay a competitive price (*i.e.*, fair market price) for its use. The price paid for that use must be determined at the time the license or other resulting technology is available for use. Although UConn or the State need not permit persons other than the sponsor to use any license or other resulting technology, the price paid by the sponsor must be no less than the price that would be paid by any non-sponsoring party for those same rights.

Cooperative Joint-Industry-Governmental Research. Under this arrangement, the agreement must provide that:

(a) multiple, unrelated industry sponsors agree to fund governmentally performed basic research;
(b) UConn or the State determines the research to be performed and the manner in which it is to be performed (*e.g.*, selection of the personnel to perform the research);
(c) title to any patent or other product incidentally resulting from the basic research lies exclusively with UConn or the State; and
(d) the multiple, unrelated industry sponsors are entitled to no more than a non-exclusive, royalty-free license to use the product of any such research.

Special Rule for Federally-Sponsored Research:

Applicable federal government contracting principles may require with respect to a research agreement with the federal government that:

(a) federal agencies receive a non-exclusive, royalty-free license in certain intellectual property developed or discovered in the course of performing research (*e.g.*, technical data, software and patents) on behalf of any federal agency;
(b) UConn or the State retains publication rights in any such property and the right to use such property in any future work performed for other clients without requiring the approval of the federal government; and
(c) UConn or the State may register copyrights and trademarks and apply for patents with respect to such property, without federal government consent.

Such agreement is treated as meeting the safe-harbor guidelines of Rev. Proc. 97-14 if:

(a) the agreement is for basic research;
(b) the research under the agreement enters the public domain;
(c) the use of the property by any federal agency is on the same terms and for the same price (determined at the time property is available for use) as UConn or the State would enter into with any unrelated, non-sponsoring party (*i.e.*, if a non-exclusive, royalty-free license is granted to federal agencies, the same must be granted any unrelated, non-sponsoring party); and
(d) neither any federal agency nor any other client is granted ownership of such property.

Rev. Proc. 2007-47

Rev. Proc. 2007-47, 2007-29 I.R.B. 108, 2007 WL 1816829 (IRS RPR)

Internal Revenue Service (I.R.S.)
IRS RPR

Revenue Procedure

Released: June 26, 2007
Published: July 16, 2007

26 CFR 1.141-3: Definition of private business use.

(Also: §§ 103, 141,145; 1.141-3, 1.145-2.)

This procedure sets forth conditions under which a research agreement does not result in private business use under section 141(b) of the Code. Rev. Proc. 97-14 modified and superseded.

SECTION 1. PURPOSE
The purpose of this revenue procedure is to set forth conditions under which a research agreement does not result in private business use under § 141(b) of the Internal Revenue Code of 1986 (the Code). This revenue procedure also addresses whether a research agreement causes the modified private business use test in § 145(a)(2)(B) of the Code to be met for qualified 501(c)(3) bonds. This revenue procedure modifies and supersedes Rev. Proc. 97-14, 1997-1 C.B. 634.

SECTION 2. BACKGROUND
.01 *Private Business Use.*

(1) Under § 103(a) of the Code, gross income does not include interest on any State or local bond. Under § 103(b)(1), however, § 103(a) does not apply to a private activity bond, unless it is a qualified bond under § 141(e). Section 141(a)(1) defines "private activity bond" as any bond issued as part of an issue that meets both the private business use and the private security or payment tests. Under § 141(b)(1), an issue generally meets the private business use test if more than 10 percent of the proceeds of the issue are to be used for any private business use. Under § 141(b)(6)(A), private business use means direct or indirect use in a trade or business carried on by any person other than a governmental unit. Section 150(a)(2) provides that the term "governmental unit" does not include the United States or any agency or instrumentality thereof. Section 145(a) also applies the private business use test of § 141(b)(1) to qualified 501(c)(3) bonds, with certain modifications.

(2) Section 1.141-3(b)(1) of the Income Tax Regulations provides that both actual and beneficial use by a nongovernmental person may be treated as private business use. In most cases, the private business use test is met only if a nongovernmental person has special legal entitlements to use the financed property under an arrangement with the issuer. In general, a nongovernmental person is treated as a private business user of proceeds and financed property as a result of ownership; actual or beneficial use of property pursuant to a lease, or a management or incentive payment contract; or certain other arrangements such as a take or pay or other out-put-type contract.

(3) Section 1.141-3(b)(6)(i) provides generally that an agreement by a nongovernmental person to sponsor research performed by a governmental person may result in private business use of the property used for the research, based on all the facts and circumstances.

(4) Section 1.141-3(b)(6)(ii) provides generally that a research agreement with respect to financed property results in private business use of that property if the sponsor is treated as the lessee or owner of financed property for Federal income tax purposes.

(5) Section 1.141-1(b) provides that the term "governmental person" means a State or local governmental unit as defined in § 1.103-1 or any instrumentality thereof. Section 1.141-1(b) further provides that governmental person does not include the United States or any agency or instrumentality thereof. Section 1.141-1(b) further provides that "nongovernmental person" means a person other than a governmental person.

(6) Section 1.145-2 provides that §§ 1.141-0 through 1.141-15 apply to qualified 501(c)(3) bonds under § 145(a) of the Code with certain modifications and exceptions.

(7) Section 1.145-2(b)(1) provides that, in applying §§ 1.141-0 through 1.141-15 to § 145(a) of the Code, references to governmental persons include § 501(c)(3) organizations with respect to their activities that do not constitute unrelated trades or businesses under § 513(a).

.02 *Federal Government rights under the Bayh-Dole Act.*

(1) The Patent and Trademark Law Amendments Act of 1980, as amended, 35 U.S.C. § 200 *et seq.* (2006) (the "Bayh-Dole Act"), generally applies to any contract, grant, or cooperative agreement with any Federal agency for the performance of research funded by the Federal Government.

(2) The policies and objectives of the Bayh-Dole Act include promoting the utilization of inventions arising from federally supported research and development programs, encouraging maximum participation of small business firms in federally supported research and development efforts, promoting collaboration between commercial concerns and nonprofit organizations, ensuring that inventions made by nonprofit organizations and small business firms are used in a manner to promote free competition and enterprise, and promoting the commercialization and public availability of inventions made in the United States by United States industry and labor.

(3) Under the Bayh-Dole Act, the Federal Government and sponsoring Federal agencies receive certain rights to inventions that result from federally funded research activities performed by non-sponsoring parties pursuant to contracts, grants, or cooperative research agreements with the sponsoring Federal agencies. The rights granted to the Federal Government and its agencies under the Bayh-Dole Act generally include, among others, nonexclusive, nontransferable, irrevocable, paid-up licenses to use the products of federally sponsored research and certain so-called "march-in rights" over licensing under limited circumstances. Here, the term "march-in rights" refers to certain rights granted to the sponsoring Federal agencies under the Bayh-Dole Act, 35 U.S.C. § 203 (2006), to take certain actions, including granting licenses to third parties to ensure public benefits from the dissemination and use of the results of federally sponsored research in circumstances in which the original contractor or assignee has not taken, or is not expected to take within a reasonable time, effective steps to achieve practical application of the product of that research. The general purpose of these rights is to ensure the expenditure of Federal research funds in accordance with the policies and objectives of the Bayh-Dole Act.

SECTION 3. DEFINITIONS

.01 *Basic research,* for purposes of § 141 of the Code, means any original investigation for the advancement of scientific knowledge not having a specific commercial objective. For example, product testing supporting the trade or business of a specific nongovernmental person is not treated as basic research.

.02 *Qualified user* means any State or local governmental unit as defined in § 1.103-1 or any instrumentality thereof. The term also includes a § 501(c)(3) organization if the financed property is not used in an unrelated trade or business under § 513(a) of the Code. The term does not include the United States or any agency or instrumentality thereof.

.03 *Sponsor* means any person, other than a qualified user, that supports or sponsors research under a contract.

SECTION 4. CHANGES

This revenue procedure modifies and supersedes Rev. Proc. 97-14 by making changes that are described generally as follows:

.01 Section 6.03 of this revenue procedure modifies the operating guidelines on cooperative research agreements to include agreements regarding industry or federally sponsored research with either a single sponsor or multiple sponsors.

.02 Section 6.04 of this revenue procedure provides special rules for applying the revised operating guidelines under section 6.03 of this revenue procedure to federally sponsored research. These special rules provide that the rights of the Federal Government and its agencies mandated by the Bayh-Dole Act will not cause research agreements to fail to meet the requirements of section 6.03, upon satisfaction of the requirements of section 6.04 of this revenue procedure. Thus, under the stated conditions, such rights themselves will not result in private business use by the Federal Government or its agencies of property used in research performed under research agreements. These special rules do not address the use by third parties that actually receive more than non-exclusive, royalty-free licenses as the result of the exercise by a sponsoring Federal agency of its rights under the Bayh-Dole Act, such as its march-in rights.

SECTION 5. SCOPE

This revenue procedure applies when, under a research agreement, a sponsor uses property financed with proceeds of an issue of State or local bonds subject to § 141 or § 145(a)(2)(B) of the Code.

SECTION 6. OPERATING GUIDELINES FOR RESEARCH AGREEMENTS

.01 *In general.* If a research agreement is described in either section 6.02 or 6.03 of this revenue procedure, the research agreement itself does not result in private business use. In applying the operating guidelines under section 6.03 of this revenue procedure to federally sponsored research, the special rules under section 6.04 of this revenue procedure (regarding the effect of the rights of the Federal Government and its agencies under the Bayh-Dole Act) apply.

.02 *Corporate-sponsored research.* A research agreement relating to property used for basic research supported or sponsored by a sponsor is described in this section 6.02 if any license or other use of resulting technology by the sponsor is permitted only on the same terms as the recipient would permit that use by any unrelated, non-sponsoring party (that is, the sponsor must pay a competitive price for its use), and the price paid for that use must be determined at the time the license or other resulting technology is available for use. Although the recipient need not permit persons other than the sponsor to use any license or other resulting technology, the price paid by the sponsor must be no less than the price that would be paid by any non-sponsoring party for those same rights.

.03 *Industry or federally-sponsored research agreements.* A research agreement relating to property used pursuant to an industry or federally-sponsored research arrangement is described in this section 6.03 if the following requirements are met, taking into account the special rules set forth in section 6.04 of this revenue procedure in the case of federally sponsored research --

(1) A single sponsor agrees, or multiple sponsors agree, to fund governmentally performed basic research;

(2) The qualified user determines the research to be performed and the manner in which it is to be performed (for example, selection of the personnel to perform the research);

(3) Title to any patent or other product incidentally resulting from the basic research lies exclusively with the qualified user; and

(4) The sponsor or sponsors are entitled to no more than a nonexclusive, royalty-free license to use the product of any of that research.

.04 *Federal Government rights under the Bayh-Dole Act.* In applying the operating guidelines on industry and federally-sponsored research agreements under section 6.03 of this revenue procedure to federally sponsored research, the rights of the Federal Government and its agencies mandated by the Bayh-Dole Act will not cause a research agreement to fail to meet the requirements of section 6.03, provided that the requirements of sections 6.03(2), and (3) are met, and the license granted to any party other than the qualified user to use the product of the research is no more than a nonexclusive, royalty-free license. Thus, to illustrate, the existence of march-in rights or other special rights of the Federal Government or the sponsoring Federal agency mandated by the Bayh-Dole Act will not cause a research agreement to fail to meet the requirements of section 6.03 of this revenue procedure, provided that the qualified user determines the subject and manner of the research in accordance with section 6.03(2), the qualified user retains exclusive title to any patent or other product of the research in accordance with section 6.03(3), and the nature of any license granted to the Federal Government or the sponsoring Federal agency (or to any third party nongovernmental person) to use the product of the research is no more than a nonexclusive, royalty-free license.

SECTION 7. EFFECT ON OTHER DOCUMENTS

Rev. Proc. 97-14 is modified and superseded.

SECTION 8. EFFECTIVE DATE

This revenue procedure is effective for any research agreement entered into, materially modified, or extended on or after June 26, 2007. In addition, an issuer may apply this revenue procedure to any research agreement entered into prior to June 26, 2007.

SECTION 9. DRAFTING INFORMATION

The principal authors of this revenue procedure are Vicky Tsilas and Johanna Som de Cerff of the Office of Associate Chief Counsel (Financial Institutions & Products). For further information regarding this revenue procedure, contact Johanna Som de Cerff at (202) 622-3980 (not a toll-free call).

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