THE FACULTY MEMBER AS AN ENTREPRENEUR

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I. INTELLECTUAL PROPERTY ISSUES

When a faculty member's research activities lead to an invention, the question arises: "Who owns the invention?" While universities and faculty alike often assume that the university, as the employer, owns all faculty research that occurs on campus, the law does not necessarily support that result. Similarly, depending upon the university's policies and the faculty member's conduct, the mere fact that an invention is conceived of while the faculty member was engaged in "private consulting" does not necessarily mean that the faculty member owns the fruits of his research.

Intellectual property battles may arise in a number of contexts. In addition to disputes between faculty and universities, disputes also arise between private companies and universities where the faculty member has assigned his invention rights to a private company as part of a consulting agreement. Further, when a professor participates in a "start-up" company, with the use of university resources, disputes often arise between the professor's start-up company and the university.

Depending upon the particulars of the faculty member's relationship with her university vis-à-vis the private company to which she has a relationship, the faculty member may align herself with either the university or the private company. While the cases and statutes discussed below concern disputes between faculty and universities, the principles apply equally to disputes between outside businesses and universities.

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A. Case Law Supports the Faculty Member's Ownership Rights

Despite the increase in entrepreneurial activities on the part of faculty throughout the country, there are very few cases which directly address the issue of faculty inventions.[1] The seminal case in the area of ownership of employee-generated inventions is a 1933 United States Supreme Court case, *United States v. Dubilier*, 289 U.S. 178 (1933). *Dubilier*, which involved non-academic employees, is often cited by commentators who urge universities to implement policies which are more entrepreneur-friendly.[2]

In *Dubilier*, two laboratory employees conducted research on airplane radios for the Bureau of Standards of the U.S. Department of Commerce. In the course of employment-related research, one of the employees became interested in a project which was not work related: "the subject of substituting house lighting alternating current for direct battery current in radio apparatus." *Id.* at 184. In the next two years, the two employee researchers invented three products applying the alternating current concepts to broadcast reception and power amplification in loudspeakers. The Court stated that because these employees were not hired to invent, the employer received only a "shop right"—a royalty-free license to use the invention. The Court further held the: "employer in such a case has no equity to demand a conveyance of the invention, which is the original conception of the employee alone, in which the employer played no part." *Id.* 188-89.

Dubilier is still the leading case on the issue of employee ownership rights to employee inventions. For example, in a more recent case, *University Patents, Inc. v. Kligman*, 762 F. Supp. 1212, 1219 (E.D. Pa. 1991), the court followed *Dubilier* and explained: "The general rule is that an individual owns the patent rights in the subject matter of which he is an inventor even though he conceived of the subject matter or reduced it to practice during the course of employment." The fact that an employee uses the "time and facilities of the employer" does not change this rule. According to the court in *Kligman*, and other cases outside the academic setting where courts have dealt with employee inventions, there are two exceptions and one limitation to

[1] The term "inventions" includes both patentable and non-patentable creations that are not subject to protection under the copyright laws.

[2] *See e.g.*, Pat k. Chew, Faculty-Generated Inventions: Who Owns the Golden Egg?, 1992 *Wis. L. Rev.* 259 ("Golden Egg"); Sunil R. Kulkarni, All Professors Created Equally: Why Faculty Should Have Complete Control Over The Intellectual Property Rights In Their Creations, 47 *Hastings L.J.* 221 (1995) ("All Professors Created Equally").

this rule. The first exception is where the employee is "a party to a contract" that confers ownership rights on the employer. Although an employer should seek to obtain a *written assignment* from employees at the time employment is commenced, the court in *Kligman* held that an assignment of patent rights may be *implied* where an employee acts consistently with a written patent policy. In *Kligman*, Dr. Kligman disclosed a prior invention—not the subject of litigation with the university—as required by the university's Invention Disclosure policy, which Dr. Kligman contended was created on his own time. In doing so, the court held that a factual question existed as to whether Dr. Kligman recognized the applicability of the patent policy to later discoveries—which were the subject of the litigation—which he created with the use of university resources.

The second exception is where an employee is "hired to invent" something in particular, then the inventions related thereto are the property of the employer. In the academic setting, most professors are hired to teach and do general research in areas substantially of their own choosing. Moreover, courts have construed the "hired to invent" exception narrowly. Thus, the "hired to invent" exception is probably not applicable in most academic settings.[3] The one limitation to the general rule is the "shop right" exception referenced above. Where an employee uses the time or facilities of his employer, the employer may have a non-exclusive and non-transferable royalty-free license to use the employee's patented invention. *Id.* at 1219-20.

Applying the principles set forth in the leading cases to inventions that arise out of private consulting by faculty, it is clear that absent a contract—written or implied—which confers ownership rights upon the university, a faculty member should retain ownership in her inventions. Similarly, without a contract to the contrary, private companies may assert ownership rights to inventions created by a faculty member who has assigned her ownership rights to inventions to the private company. Some states have statutes that affect ownership

[3] *See* Golden Egg at 267-68; All Professors Created Equally at 232-33. However, one case supports the proposition that professors are customarily hired to invent. *See Speck v. North Carolina Dairy Foundation*, 319 S.E. 2d 139 (N.C. 1984) (The North Carolina Supreme Court used common–law principles to find that Dr. Speck was hired to invent, so the invention belonged exclusively to the university and Speck had no valid royalty claims.). *Speck* has been widely criticized, especially with regard to the court's implication that university professors are usually "hired to invent." *See e.g.,* Golden Egg at 289-304; All Professors Created Equally at 233, n. 64; Christopher G. Browning, Jr., The Souring of Sweet Acidophilus Milk: Speck v. North Carolina Dairy Foundation and the Rights of University Faculty to Their Inventive Ideas, 63 *N.C. L. Rev.* 1248, 1258 (1985). *See also, Yeshiva Univ. v. Greenberg,* 255 A.D.2d 576, 681 N.Y.S. 2d 71 (1998) (research assistant who was hired to conduct research on Alzheimer's disease had no ownership rights in the discovery she made of PHF-1, an antibody which can detect specific genetic markers which are associated with Alzheimer's disease.)

rights. For example, as discussed further below in Section 2., Connecticut, North Dakota and Ohio have recently enacted laws that delineate faculty ownership rights of universities and their employees to faculty-generated inventions.[4] Other states have statutes which limit all employers' rights to obtain assignment of their employee's inventions that are the product of "private" activity. For this reason, as discussed further in Section III, many universities have policies and/or written agreements which define what activities are "private" and which spell out the circumstances in which faculty may retain an ownership interest in their inventions.

B. Connecticut, North Dakota and Ohio's Statutes Limit Faculty Ownership Rights

By statute, the Connecticut State University system and the University of Connecticut:

> shall be entitled to own . . . any invention . . . in which such invention is conceived in the course of performance of customary or assigned duties of the employee inventor . . . or in which the invention emerges from any research, development or other program of the university, or is conceived or developed wholly or partly at the expense of the university, or with the aid of its equipment, facilities or personnel.

Conn. Gen Stat. §§ 10a-98 b and 110b (1999).

When an invention belongs to a Connecticut university under section 10a-110b, the faculty member still receives royalties of a minimum of 20 % of the net proceeds from the invention. Conn. Gen. Stat. §§ 10a-98c and 110c.

North Dakota has a statute that provides that the "respective state institution of higher learning" retains patents on "inventions resulting from research sponsored by a state institution of higher learning and conducted by faculty . . . ." N.D. Cent. Code § 47-28-01. The faculty member receives royalties of at least 30 % on university-sponsored research. N.D. Cent. Code § 47-28-02.

Pursuant to the Ohio statute, Ohio state colleges and universities retain all rights to inventions "which result from research or investigation conducted in any . . . research facility

[4] As the U.S. Supreme Court's decision in *Dubilier* involved federal common law rights, these statutes should be valid even to the extent that they are inconsistent with *Dubilier*.

of any state college or university." The faculty member only has a right to income from such research if the same is authorized by the board of trustees. ORC Ann. 3345.14.

While the North Dakota and Ohio statutes appear to limit university ownership of faculty inventions to only those inventions that are directly related to university research, the Connecticut statute seems to impose greater restrictions on faculty ownership. For example, if a professor has a private consulting engagement on an issue which is closely related to an issue that the professor is researching "partly at the expense of the university," it would appear that the Connecticut statute would confer sole ownership upon the university.

C. The Bayh-Dole Act Supports University Ownership in Government-Sponsored Research

The federal Patent and Trademark Act of 1980, commonly referred to as the Bayh-Dole Act, governs ownership rights in inventions which are the result of government-sponsored research. This Act allows the university to elect title to faculty inventions within two years. If the university does not make this election, the government may claim title or allow the faculty member to petition the government for ownership.

D. Several States Have Statutes Supporting Faculty Ownership of Inventions Created on Their "Own" Time

As mentioned above in Section A, the courts have stated that a written assignment is the best means for an employer to obtain ownership of employee inventions where an employee invents something he was not "hired to invent." However, several states have statutes which prohibit written assignments which seek to provide employer ownership of inventions which employees create on their "own" time. California, known for its pro-entrepreneurial environment has had such a statute in place for 20 years, a relatively long period of time in this area. California's statute regarding employee ownership of inventions provides:

> (a) Any provision in an employment agreement which provides that an employee shall assign, or offer to assign, any of his or her rights in an invention to his or her employer shall not apply to an invention that the employee developed entirely on his or her own time without using the employer's equipment, supplies, facilities, or trade secret information except for those inventions that either:

> (1) Relate at the time of conception or reduction to practice of the invention to the employer's business, or actual or demonstrably anticipated research or development of the employer; or
>
> (2) Result from any work performed by the employee for the employer.
>
> (b) To the extent a provision in an employment agreement purports to require an employee to assign an invention otherwise excluded from being required to be assigned under subdivision (a), the provision is against public policy of this state and is unenforceable.

Cal. Lab. Code § 2870.

While on its face, the California statute may be construed as supportive of a faculty member's right to retain ownership in inventions created in her private consulting capacity, there are some risks to such an interpretation. First, the statute states that only inventions which are "developed *entirely* on his or her own time" are excluded from employer assignment agreements. Second, even where the faculty member develops an invention on "her own time," employer assignment agreements are permissible if the invention relates to "demonstrably anticipated research" or if the invention results from "any work performed by the employee." Depending upon the nature of the private consulting agreement, the faculty member might not find refuge in the California statute.

Other states that have statutes similar to California's include: Delaware (19 Del. C. § 805), Illinois (765 ILCS 1060/2), Kansas (K.S.A. §4-130), Minnesota (Minn. Stat. § 181.78), North Carolina (N.C. Gen. Stat. § 66-57.1), Utah (Utah code Ann. § 34-39-3), and Washington (Rev. Code Wash. (ARCW) § 49.44.140).

Utah's statute is the most favorable to employees. The statute provides that an employment agreement may not require assignment of an invention that is either created entirely on the employee's own time or that is "not an employment invention." Thus, even if the invention relates to an issue the employee is researching for the employer, the Utah statute, unlike the other state statutes cited above, would still void any agreement purporting to assign the employee's rights in the invention to the employer. The Utah statute does, however, permit assignment agreements which are supported by consideration "which is not compensation for employment." Utah Code Ann. § 34-39-3.

II. EMPLOYMENT LAW ISSUES

A. Potential *Qui Tam* Lawsuits

As some faculty members at state universities have earned literally millions of dollars through their entrepreneurial activities, university watchdogs, some of whom are also professors, have raised concerns that the university has been deprived of its share of the profits. Under the federal False Claims Act's *qui tam* provision, 31 U.S.C. 3730(b), a private party may bring a claim on the government's behalf for damages caused by another party's false claims. In a recent case, *United States ex rel. Cantekin v. University of Pittsburgh*, 192 F.3d 402 (3rd Cir. 1999), the court allowed a professor to proceed with a *qui tam* claim against another professor in the Otolaryngology Department of the University of Pittsburgh's medical school, on the grounds the defendant professor failed to disclose on his National Institute of Health (NIH) grant application that he had received several million dollars from various pharmaceutical companies

California and Florida allow private parties to file *qui tam* suits. *See e.g.*, Cal. Gov't. Code § 12650; Fla. Stat. § 68.083[5]. While there do not appear to be any published decisions involving *qui tam* claims brought against university professors who allegedly misappropriated publicly-funded university resources for their own personal gain in connection with private consulting or start-up companies, there have been lawsuits filed with such allegations. The typical fact pattern involves a state university professor that has an ownership interest or other relationship with a company. The professor is accused of circumventing the university's outside research and disclosure policies by conducting research on the company's behalf and not allowing the university to have an interest in the profits generated by the professor's discoveries. Further, the professor will be accused of not paying the university for the use of its facilities, personnel, and other resources. These claims can run into the multi-million dollar range.

One example of a *qui tam* lawsuit involving a public university is the case brought by Dr. Charles Richardson, a professor at U.C. San Francisco, against another professor, Dr. Dennis Magono and Magono's foundation, Ischemia Research and Education Foundation. The lawsuit claimed Magono misused U.C.'s name, staff and resources to perform multi-million dollar drug-

[5] Other states have false claims statutes too, but they are limited to the area of health-related claims.

testing contracts with drug companies. Without admitting liability, the Foundation agreed to pay $25 million to settle the lawsuit. U.C. San Francisco received $19 million of the settlement proceeds.[6]

B. Potential Liability Under "Joint Employer" Theories

When a faculty member has an outside consulting business that utilizes university employees, the university may be exposed to liability for a myriad of claims, including discrimination and sexual harassment, under a joint employer theory. In examining whether an employer-employee relationship exists, courts generally apply a "common law employee" test. The common law test looks to the law of agency to determine whether an employment relationship exists, and considers the hiring party's **right to control** the manner and means by which the individual in question accomplishes the work.[7] Factors relevant to this inquiry include:

- the extent of control the employer may exercise over the details of the work
- whether the individual is engaged in distinct occupation or business
- the kind of occupation the individual is doing, and whether it is typically the kind of work done under the direction of a supervisor
- the skill required
- whether the employer provides equipment, tools, and place of work
- the method of payment, by time or job
- whether the employer withholds social security or other taxes from the individual's compensation
- whether the employer provides leave or benefits
- whether the individual is covered by workers' compensation
- the manner in which the relationship may be terminated

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[6] "UC To Get Millions As Suit Is Settled; Doctor's Foundation Was Accused Of Cheating UCSF," *San Francisco Examiner*, January 31, 1997, P. A-1.

[7] *Nationwide Mutual Ins. Co. v. Darden*, 503 U.S. 318, 323-34 (1992) (quoting *Community for Creative Non-Violence v. Reid*, 490 U.S. 730, 751-52 (1989)).

- whether the work is an integral part of the employer's business
- whether the individual is permitted to do the same type of work for other companies
- whether the individual may delegate the work
- whether the individual is an employee with employees of his or her own
- whether the individual is required to make a capital investment
- whether the work affords the individual an opportunity for profit or loss depending on the individual's abilities
- the intention of the parties in creating the relationship[8]

The fact that an individual is an employee of one organization does not preclude a finding that the individual may also be an employee of another organization. In reality, if not on paper, both organizations may be "joint employers" of a single individual. "Where it appears that more than one entity is involved in controlling an individual's employment situation, courts have recognized the concept of multiple 'employers' . . . ."[9]

The joint employer test was first developed under the National Labor Relations Act (NLRA), in the context of contractual relationships with primary contractors and subcontractors, and has been used in varying forms by courts interpreting other federal statutes as well. The test focuses on the extent of control over the terms and conditions of an individual's employment that the organization has retained in contracting with an independent company for the supply of labor.[10]

There are a number of possible ramifications if a employer is found to have misclassified its workers. They include:

- ***Liability for Overtime Pay, Compensation and Employee Benefits***
- ***Liability for Job-Related Injuries Suffered by the Employee***
- ***Tax Penalties***

[8] *EEOC* Interpretations § 605, App. H (CCH EEOC Compliance Manual ¶2182).

[9] *Pemrick v. Stracher*, 67 F. Supp. 2d 149 (E.D.N.Y. 1999).

[10] *NLRB v. Browning-Ferris Indus., Inc.*, 691 F.2d 1117, 1122 (3rd Cir. 1982); *see NLRB. v. Jewell Smokeless Coal Corp.*, 435 F.2d 1270, 1271 (4th Cir. 1970) (citing *Boere v. Greyhound Corp.*, 376 U.S. 473 (1964)).

- ***Benefit Plan Disqualification***
- ***Claims for Wrongful Discharge, Discrimination and Harassment***

To avoid claims under a joint employer theory, universities may implement policies which prevent faculty from hiring any university employee in connection with any outside business interest. However, this type of policy may discourage faculty from exploring and developing outside business interests. To the extent a university chooses to have a less restrictive policy, it should clarify that the faculty member may not utilize the university's name in connection with an outside business. Further, the university should have a policy that any university personnel hired by faculty for an outside business should have duties which are separate and distinct from that personnel's university duties.

Agencies such as the IRS may reclassify workers that an employer thought "belonged" to a different employer or whom the employer contends was an "independent contractor." Although the risk of reclassification of workers on examination by an agency cannot be eliminated, universities can take several steps to minimize the risk of reclassification:

- Draft a written document to be signed by both parties that spells out the relationship. The document should make it clear the hiring organization does not have the right to control the procedures for accomplishing the contracted services.

- Consider reciting the worker's obligation to pay income and self-employment taxes.

- Whenever possible, the worker should invest his/her own resources in the work being performed.

- The worker should have responsibility for hiring, supervising, training and paying assistants.

- If the worker must rely on the university's facilities, such as office or classroom space, an agreement should be made specifying what will be provided and how much the worker will pay for such facilities.

- Service should be paid for by project (when an invoice is received) and not on an hourly, weekly or monthly basis.

- Deadlines should be set specifying when the work should be completed.

- The worker should formalize his or her own business by filing an assumed name certificate, having letterhead and business cards printed and opening a bank account in the business's name.

- Form 1099s should be filed reporting the compensation paid to each worker.
- Classify workers performing similar work similarly.
- Classify a worker consistently to the extent possible.

III. NEED FOR COHERENT UNIVERSITY POLICIES

To address the various issues raised by entrepreneurial faculty, many universities have developed policies that deal specifically with ownership rights and limitations on outside consulting activities. Below are excerpts from a representative sample of current university policies.

Stanford University Research Policy Handbook

Document 4.3

- "[T]he basic principle of this policy statement is that there needs to be a limitation upon the time that a Stanford faculty member may spend in consulting."
- Re Moonlighting: "Faculty members may pursue a variety of endeavors for financial profit that are not directly related to the person's field or discipline . . . Such endeavors may only be pursued after the full-time commitment to Stanford has been fulfilled."
- Re Number of Permissible Consulting Days: "The maximum number of consulting days permissible for a member of the Academic Council on a full-time appointment is 13 days per academic quarter."
- Re Responsibility of Faculty Members: "The University has the right, and indeed the obligation, to protect itself from losses due to excess consulting and to seek reimbursement from the faculty member for salary and benefits covering time spent on consulting beyond the limits provided for by this policy . . . ."
- Re Use of University Facilities or Services: "The facilities and services of the University may not be used in connection with compensated outside work, except in a purely incidental way."

University of Pennsylvania Patent Policy

- "The University wishes to share the economic benefits of inventions or other intellectual property with the creators of such works in a way that is consistent with the research and educational mission of the University obligations to regulatory authorities, research sponsors and licensees."

- Re Outside Employment or Consulting Agreements: C.2 "If a faculty member . . . contemplates a consulting relationship with a company that sponsors research for that individual at the university, the proposed consulting agreement shall be disclosed to the IPA [Intellectual Property Administrator] . . . ." C.4 "Faculty members . . . . acting as independent consultants to outside companies . . . do so at their own risk and are not protected by the University."

University of California Policies

- Re Outside Professional Activities of Faculty Members: "Regents Standing Order 103.1(b) states that faculty members shall not allow outside employment to interfere with primary University duties . . . A full-time faculty member . . . may not engage in compensated outside professional activity for more than 39 days during the academic year."

M.I.T. Policies

- Re Significant Use of M.I.T.-Administered Resources: "M.I.T. does not construe the use of office, library machine shop or Project Athena personal desktop work stations and communication and storage servers as constituting significant use of M.I.T. space or facilities, nor construe the payment of salary from unrestricted accounts as constituting significant use of M.I.T. funds, except in those situations where the funds were paid specifically to support the development of certain materials."

University of Minnesota Board of Regents Policies

- Re Restrictions on Service Activities: "In general, it seems proper to restrict service activities if they may: (1) interfere with a faculty member's ability to carry out contractual responsibilities; or (2) make use of University resources or facilities.

Each of the above-referenced universities also requires their faculty to sign written acknowledgements of their agreement to comply with their university's patent-related policies. Further, these universities have policies which specify what percentage of net proceeds relating to faculty inventions covered by the agreements belong to the faculty member and what percentage belongs to the university. As mentioned above in Section I., to avoid disputes with faculty after an invention is created, universities should adopt comprehensive patent-related policies and require all faculty to sign an acknowledgement of an agreement to comply with these policies as a condition of employment. Set forth below are the royalty policies for distribution of net proceeds at the above-referenced universities.

Stanford—1/3 to inventor; 1/3 to inventor's department; 1/3 to inventor's school.

University of Pennsylvania—30% to inventor; 15% to inventor's research activity share; 15% to inventor's department; 17.5% to inventor's school; 17.5% to research foundation; 5% to intellectual property fund.

University of California—35% to inventor; 15% to inventor's campus/laboratory; 50% to school.

M.I.T.—1/3 to inventor; 2/3 to Departmental Pool (1/2 to M.I.T. General Fund and ½ to Laboratory/Department).

University of Minnesota—If there is a patent application filed, 1/3 to Office of Patents and Licensing, 1/3 to unit from which the development came; 1/3 to developers; if no paten application is filed, 25% to the Office of Patents and Licensing and 75% to developers.

Other universities not included in this Article, such as Columbia University, have policies that have different royalties for net proceeds over a certain amount. At Columbia, the inventor receives royalties of 40% for the first $100,000, and 20% thereafter.

IV. CONCLUSION

The options for faculty in the private sector have been growing at a seemingly exponential rate. To retain the best and the brightest, universities will want to have policies that are "pro-entrepreneur," while at the same time "pro-academia." Similarly, in encouraging faculty to be entrepreneurial, university policies should protect the university from potential *qui tam* and joint employer liability claims. With these proactive policies in place, universities should meet their objectives of faculty retention, maintaining ownership of university-related inventions, and limiting liability for third-party claims.