National Academy of Sciences
Government-University-Industry Research Roundtable

INTERNATIONAL RESEARCH: LEGAL ISSUES AND AGREEMENTS

July 27, 2010
Washington, DC

Jamie Lewis Keith, Vice President and General Counsel, University of Florida
William F. Ferreira, Attorney at Law, Hogan Lovells US LLP

Threshold Issue: What Nature and Duration of Legal Relationship Is Warranted?

- Need To Avoid A Legal Partnership With Joint/Several Liability For Other's Debts, Contracts, Torts
- What are the programmatic goals of the endeavor? Feasibility?
  - → Do the foreign entity and U.S. institution have the same objectives, realistic expectations re: outcomes, equivalently important interests at stake?
  - → Who will fund? What are the risks and how will they be allocated?
- What foreign jurisdiction is involved? Does the foreign government expect to have an MOU with us? Are there good reasons to pursue one?
- What activities will be undertaken abroad by the U.S. institution?
- Will the foreign jurisdiction's "doing business" (research, education, consulting/advisory services) registration requirements be triggered, regardless of type of relationship?
- Will foreign tax filings and/or payments be required, regardless of type of relationship?
- Are the foreign jurisdiction's laws and processes predictable?
- How stable is the political context of the foreign jurisdiction?
- Are we negotiating with a legally and politically authorized representative?

OPTIONS: JOINT CREATION OF NEW CORPORATION

- ***U.S. Institution and Foreign Government or University Create A New Corporation In The Foreign Jurisdiction***
  - Best for True, Sustained Joint Ventures Funded By Foreign Government With Significant Activities In Foreign Jurisdiction

- ***Advantages***
  - Credibility and Substance
  - Some Foreign Registration Requires Involvement of Local Entity
  - Limited Liability For U.S. and Foreign Incorporators
  - Easy For Foreign Government To Fund

- ***Disadvantages***
  - Corporate Formalities Apply: With Costs and Feasibility Concerns
  - Must Address Governance, Ownership, Capitalization
  - Local Law Applies: Registration, Taxation, Other
  - Public U.S. Institutions May Be Restricted or Prohibited To Create or Operate—Depends on State Law

OPTIONS: SERVICE BLOCKER CORPORATION

- U.S. University Alone Creates (and Controls) A New Corporation Under U.S. Jurisdiction's Laws---or Under Foreign Jurisdiction's Law If Required By That Jurisdiction For The Contemplated Endeavor

- Tax and Liability Driven:
  - Insulates the U.S. University's Income and Assets From Taxation and Liability In The Foreign Jurisdiction
  - The New Corporation's Income and Assets Are Exposed

- ***Advantages***:
  - Avoids Tax Imputation To U.S. University
  - Limited Liability To New Corporation

- ***Disadvantages***:
  - Corporate Formalities Apply (e.g., by faculty)
  - Perception That U.S. University Has Limited Commitment to Project

OPTIONS: COLLABORATION OF EXISTING OR NEW FOREIGN ENTITY WITH U.S. UNIVERSITY

- Best For Foreign Government-Funded Collaboration With U.S. University Where Permanence, Formality Of Jointly Owned Corporation Isn't Warranted
  - Foreign University– Or If None Is Suitable, A New Foreign Entity Created By The Foreign Government or Industry--Is The Collaborator
  - Important That U.S. University Neither Is An Incorporator, Nor has Representatives on the New Entity's Governing Board (U.S. University's nominees are appointed by the foreign entity and serve individually)

- ***Advantages***
  - Politically Easier For Foreign Government to Directly Fund Its Jurisdiction's Entity, Rather Than The U.S. University or Its Service Blocker Corporation
  - Less Complicated/Restrictive Than Adhering To Corporate Formalities
  - Independence, Self-Control Of Collaborating Institutions Preserved
- ***Disadvantages***
  - Still Must Know/Obtain Workable, Reliable Pass-Through Funding Terms
  - Tension Between Foreign Entity and U.S. University Re: Funding and Roles
  - "De Facto" Partnership Risk If Contract AND Public Presentation Aren't Clear

OPTIONS: FOREIGN CAMPUS/Research Institute of U.S. UNIVERSITY

- Best When Permanence, Autonomy Are Warranted
- Seriously Assess Imperative/Feasibility, Weigh Risks/Benefits
  - Foreign Law Must Allow U.S. University's Independent Campus
    - →Different levels: operation of program vs. facilities
    - →If U.S. property ownership/leasing not permitted—May a local entity own or lease hard assets, contractually license use to U.S. University?
  - Foreign Jurisdiction's Laws (HR, Environmental, Registration, Taxation, Realty/Leasing, Research, Etc.) Apply—Expertise Needed, Often Requires Contracting With Local Operator:
    - →How will compliance risk/liability be allocated contractually?
    - →Would directing the research program, not operating the facility, not hiring the local employees be adequate?
    - →U.S. University should maintain autonomy over research (and academic) program as with its other campuses, approval of key personnel, and approval of selection and design of hard assets
  - Must Secure/Assure Ability to Meet Financial Obligations and Needs of the Foreign Campus

*Some information provided by Mary Joe Dively of Carnegie Mellon

OPTIONS: FOREIGN CAMPUS/Research Institute Of U.S. UNIVERSITY

- ***Advantages***:
  - Opportunities to Bridge Cultures
  - U.S. University Need Not Change Legal Structure or Observe Separate Corporate Formalities
  - Foreign Activities May Conform As Much As Possible To Principles, Policies and Procedures of U.S. Campus

- ***Disadvantages***:
  - Complexities of Operating Outside U.S.—Distance, Different Legal Regimes, Different Cultures
  - Must Segregate Research Performed At Foreign Campus Due to U.S. Government Funding Requirements
  - Must Address, Likely Equalize Compensation and Employment Terms For U.S. Faculty and Staff Working In Foreign Locale
  - Foreign Registration/Licensing and Entity and PersonalTaxation Apply
  - Separate Accounting and Auditing of Financial Records for Foreign Campus

Some information provided by Mary Jo Dively of Carnegie Mellon

OPTIONS: U.S.–Foreign JOINT DEGREE GRANTING PROGRAMS

- Best When U.S. University Conducts Most Teaching in U.S. -- But Seeks To Broaden Offerings -- Foreign Government Funds Joint Academic Program – And Foreign University Seeks To Broaden Offerings –And Sufficient Common And Complementary Curriculum Exists

- ***Advantages***: Enhances Academic, Research, Cultural Opportunities of Both Universities
  - No Need for Complexities of a Foreign Campus
  - Foreign Government Funding Made Available to US University Through Foreign University
  - Allows Joint Degrees Without Either University Compromising Standards

- ***Disadvantages***:
  - Requires Universities of Reasonably Comparable Stature and Compatible Programs/Standards
  - Complexities and Need for Infrastructure and Coordination
    - Students Separately Admitted to/Graduate From Each University's Program Under Its Usual Standards/Processes
    - Students Receive Fellowship/Funding from Joint Program Funding and Joint Degrees
    - Faculty Appointed to Both Universities -- Must Qualify Under Standards of Each
    - Distance Technology Required for US University Faculty to Teach Its Students at Foreign University Without Foreign Physical Presence
    - Very Difficult To Deliver On Promise Of U.S. Faculty Presence Abroad For Extended Period

MANAGING RISKS: REPUTATIONAL

- University's Reputation Is Its Most Valuable Asset
- Protect Reputation Where Name is Associated With An Endeavor Not Controlled By University
  - Specify How Name Is Associated With Endeavor
  - Provide Veto, Termination, Other Means to Prevent/Stem Damage
- Identify Greatest Sources of Reputational Risk Early and Plan to:
  - Establish Realistic Objectives, Expectations Re: Performance/Foreign Presence/Outcomes

    →Be Clear In Contract--No Guarantees And U.S. University Cannot Translate Its Experience For Foreign Implementation-Foreign Entity Must
  - Understand Interests and Stakes – Is Endeavor Sensible Politically?
  - Manage Compliance With Governing Research/Academic/Legal Standards
  - Specify Easy Exit Strategies (E.g., Automatic Termination – Action to Continue)
  - Position to Avoid Success vs. Failure Characterization

MANAGING RISKS: GOVERNING LAW AND LANGUAGE

- As a Practical Matter, Foreign Governments will Require Their Law To Govern
  - U.S. Public Institutions May Require As Well – Silence Is Option

- Areas to Consider Carving Out?
  - U.S. Export Controls and Trade Sanctions Apply
  - Law of Jurisdiction Where An Activity Occurs Governs Activity

- Make sure English is the Governing Language For The Contract and All Dispute Resolution

- Parties Should Agree That Court Of Competent Jurisdiction May Enforce Arbitration Provision and Decision

MANAGING RISKS: TERMINATION OF CONTRACT AND ENDEAVOR

- TERMINATION
  - Sole Remedy (Plus Payment For Surviving Obligations)
  - Without Cause (Avoid Public Declarations of Fault)
  - If Economically or Programmatically Infeasible
  - If Failure to Agree on Material Actions In Governance Of Entity Or Program
  - If Necessary For Export/Trade Sanction Compliance
  - Lead Times:
    - Try for 1 Year Advance Notice For Planning Purposes, Unless Sooner Necessary For Legal Compliance Or Force Majeure
  - Consider 1 Year Pilot Requiring Action to Extend, Otherwise Automatically Ending
  - Plan For Evacuation Of People and Abandonment Of Assets
  - Address Non-cancellable Obligations – Funding Must Survive Termination To Cover
    - Not only Formal Encumbrances But Other Commitments
  - May Need Security (Neutral Country Bank Demand Letter of Credit) For Substantial, Long-term Financial Obligations And Major Assets

MANAGING RISKS: TAX LIABILITY

Foreign Jurisdiction Tax Filings, Liability Re: Entity; Revenues to U.S. University; Individuals Employed By U.S. University or Its New Entity

- Not a U.S. Law Question
  - Governed by Foreign Jurisdiction and Tax Treaties—Need Expert
- Exposure Aggravated If there is a “Permanent Establishment” Or Time Limits In-Country Are Exceeded
  - Avoid If Possible: Foreign Bank Account, Office, Substantial Presence or Activity Requiring Foreign Registration, Exceeding In-Country Time Limits
- U.S. University or Entity Tax Liability
  - Tax-Exempt Status May Not Be Recognized or Available In Foreign Country
- Evaluate Up Front The Effect of Accounting, Tax Filing Obligations (Even Without Tax) and Tax Liability On Adequacy of Funding
  - Quantify, Mitigate, Allocate (Foreign Funder Pays or Grosses Up Funds)
- Individual Tax Liability – Determine and Address
  - Individuals Involved May Incur Additional Personal Tax Liability, Possibly A Portion of U.S. University Compensation Will Be Taxed
  - Individual reporting requirements (e.g., FBAR)

MANAGING RISKS: DISPUTE RESOLUTION

- Recognize That Changes In Political Control In The Foreign Jurisdiction May Profoundly Affect Value and View Of Endeavor There
- Always Create an Escalation Path, Involving Discussion, Resolution Efforts Among Senior Officials Of Internal Organizations First
- Make Sure that Arbitration Venue and Arbiters will be Familiar with Foreign Law Considerations and Governing Law of Contract If Different
- If Necessary, Use Binding Arbitration as Dispute Resolution Mechanism – Rather Than Enforcement In Court
  - Neutral Forum Best (E.g., London, Singapore, Switzerland)
  - Consider Rules that Govern (E.g., UN, International Chamber of Commerce Commercial Rules)
  - Will Still Need To Be Able To Enforce Arbitration Provision and Decision In Any Court Of Competent Jurisdiction and Agree To Venue For That Purpose

MANAGING RISKS: PAYMENTS

- PAYMENTS
  - In Advance Or “Escrow” 6 Months Contingency Funds From Sponsor
  - In USD or Indexed to Provide Equivalent Amount – Protect Against Currency Fluctuations
  - Allow Adjustment in Scope Of Work and Excuse Performance If Funding Is Inadequate
  - Be Clear Whether Fixed Price or Cost Reimbursable
    - Each Option has Risks/Benefits
  - Agree On Level of Detail Required in Invoices and Reports – Conform To U.S. Government or Institution Conventions To Avoid Significant Administrative Burden

MANAGING RISKS: PAYMENTS

- Consider And Plan Up Front To Address Any Foreign Jurisdiction Restrictions On Currency Transfers In USD Out of Country -- Or In To Country
- Consider Any Foreign Jurisdiction Special Prohibitions (E.g., No "State Aid" To Distort EU Market With "Claw Back")
- Carry Forwards: When Determined, How Measured
  - Does Award Allow Categorical Re-Allocation of Budget Without Sponsor Approval Or At What Level? By Whom?
- Is There a Withholding Pending Audit?
- Impact of Tax Liabilities

MANAGING RISKS: INTERNATIONAL EMPLOYMENT

- Foreign Employment Law
  - Applies to local nationals and U.S. personnel assigned to positions overseas
  - Basics of international employment
    - Very protective of employee rights
    - "Vested" rights
  - "Independent Contractor trap"
  - Complications of income tax withholding, local social security contributions, mandatory benefits, etc.

- Visas
  - Lawful entry ≠ lawful work

MANAGING RISKS: U.S. COST RECOVERY

- Don’t Compromise Your Core (U.S. Government) Research Funding
  - U.S. Government’s “Most Favored Nation” status with respect to structure and administration of international program
  - F&A recovery on foreign subawards
  - Disposition of assets upon wind down of operation
  - Beware of conflicts of commitment (excessive time commitments to foreign endeavors)

MANAGING RISKS: Financial Regulatory Compliance

- **Obligations To Federal Sponsors**
  - Financial compliance and cost principles
  - Property management
  - Local procurement

- **Subawards/Subrecipients**
  - Meaningful flow-down of federal sponsor obligations
  - Subrecipient monitoring
  - Foreign subrecipients unfamiliar with federal research compliance infrastructure
  - A-133 applies to foreign subrecipients? Technically no, but other federal audit requirements may apply

MANAGING RISKS: Financial Regulatory Compliance

Recent "Audit of Overseas Grant Controls"

Audit of a university's extensive federal research operations abroad

- **Finding #1:** Procurement noncompliance
  - Check procurement sources
- **Finding #2:** Subrecipient Monitoring
  - Oversight and training required
- **Finding #3:** Lack of documentation
  - Time and effort reporting
  - Records of taxes paid, pending exemption
  - Records retention policy

MANAGING RISKS: AUDITS

- Is an Audit Necessary? When?
  - Fixed Price Should Not Require vs. Cost Reimbursement
  - Who Does It? When? What Are the Terms of Engagement?

- Audit Fees Should Be Covered By the Project or, Preferably, a Separate Agreement
  - If In Project Account, Separately Budget As Additional Funding Over Programmatic or Institutional Administrative Costs

MANAGING RISKS: HUMAN AND ANIMAL RESEARCH

- **Human subjects research at foreign sites**
  - Applicability of US and foreign regulations
  - Pfizer case
- **Patient care issues**
  - Licensing and credentialing of health care professionals
  - Treatment of patient records; privacy
  - Storing and dispensing medications
  - Disposal of biohazards and other waste
- **Animal research at foreign sites**
- **Shipment of tissues/samples (biological materials)**
  - Highly regulated activity
  - USDA/CDC/Dept of Commerce Permits

MANAGING RISKS: U.S. REGULATIONS: Antiboycott and FCPA

- **Antiboycott Laws**
  - Arab League's economic boycott of Israel
  - Boycott participating countries: *Kuwait/Lebanon/Libya/ Qatar/Saudi Arabia/ Syria/United Arab Emirates/Yemen*

- **Foreign Corrupt Practices Act (FCPA)**
  - Prohibits payments to foreign officials to influence those officials in order to secure/retain business
  - Collaboration with foreign officials should be carefully managed.

MANAGING RISKS: FCPA

- **Misperceptions about the FCPA**
  "The FCPA does not apply because…"
  - No contact with elected government officials
    - Consider "instrumentality" of a foreign government
  - No presence in the foreign country
    - Consider "willful blindness" to subawardee
  - No "obtain" or "retain" any business
    - Consider "improper advantage"
  - Compliance policies and procedures are voluntary
    - Consider training/education

MANAGING RISKS

- **Learning from others**
  - Failure to investigate overseas partners
  - Failure to maintain control over international venture
    - Failure to supervise investigators and administrators
    - Failure to apply internal controls
  - Failure to take local law into account
  - Failure to take U.S. law into account
  - Failure to gauge reliability of lead personnel overseas
    - Who am I getting information from?

MANAGING RISKS: U.S. REGULATIONS: Export Controls/Trade Sanctions

- Analyze Up Front The Likely Applicability of Export Controls and Trade Sanctions To Activities, Equipment, Materials, Technical Information Involved In Endeavor With Particular Foreign Collaborators And Foreign Country
  - If ITAR Applies, All Countries Require A License For An Export, Exports To Some Countries Are Prohibited
  - EAR Depends On What Is Exported, Where And To Whom
  - Trade Sanctions/OFAC Depends On Sanction For Each Country

- Contract For International Research Should:
  - Acknowledge Possible Applicability of Export Controls and Trade Sanctions
  - Excuse Performance And Permit Termination If Necessary To Comply
  - Require Notice Before Technical Information or Any Items/Materials Are Exchanged (To Allow U.S. Institution To Analyze Exports/Sanctions)

MANAGING RISKS: U.S. REGULATIONS: Trade Sanctions

- OFAC Sanctions May Apply and Prohibit, *Regardless of Discipline Involved*:

-- Paying (E.g. Compensation, Honoraria) To– Contracting With-- Sanctioned Countries (currently *Cuba, Iran, Syria, Sudan, N. Korea, Balkans Region, Belarus, Burma, Ivory Coast, Congo, Iraq, Liberia, Zimbabwe*), Their Nationals, or Sanctioned Entities-Individuals (U.S. or Foreign)

-- Attending—Planning-- International Conferences In/With Sanctioned Countries, Their Nationals, or Sanctioned Entities-Individuals (U.S. or Foreign)

-- Travel to, Surveys In--Services or Bringing Even Office Laptops, Cell Phones, PDAs to Sanctioned Countries, Their Nationals or Sanctioned Entities-Individuals (U.S. or Foreign)

-- Editing/Joint Authoring Articles in/of/with Nationals of Sanctioned Countries or Sanctioned Entities-Individuals (Foreign or U.S.)

- December 17, 2004 OFAC General License for Cuba, Sudan and Iran Allows Most Editing/Joint Authorship with Nationals of these Countries (But Not the Governments or Government Employees) (31 C.F.R. 515, 538, 560)

  State Universities Are Not the Government For this Purpose.

MANAGING RISKS: U.S. REGULATIONS: Export Controls

- Export Controls May Apply/Be Violated:

  -- When Standard Office Laptop Computer, Cell Phone, PDA is Hand-Carried or Shipped to OFAC-Sanctioned Countries —OR *anywhere abroad* to Entities/Persons on OFAC Prohibited, State Department Terrorist, EAR Entities, Denied Persons, Unverified Persons, General Order No. 3 Lists or to terrorists or weapons of mass destruction or long range missile or nuclear programs-- Without a License--*Regardless of Field of Work* (See Fundamentals Slides re: Lists)

  If OFAC Countries Are Not Involved, Standard Office Laptop Computers, PDAs, Cell Phones With *Only* Standard Office Software and *Non-technical Subjects* (i.e., *Both* No Proprietary Data/Encryption *and* No Non-public Technical Research Results) May Be Taken Abroad If They Are Kept In Your Custody and Control and You Return With Them. (More Leeway May Be OK, But Hard To Confirm Against All Required Lists and Hard To Ensure Prohibited Entities/Individuals Cannot Gain Access.)

  -- When Technical Research Equipment—Specialized Computers—*Any* Biological Samples—*Any* Computer with Confidential Technical Research Data--or Encrypted or Proprietary Software--Are Hand-Carried, Shipped or Left Abroad Without a License

MANAGING RISKS: U.S. REGULATIONS: Export Controls

When Otherwise Fundamental Technical Research Occurs Not Only On Campus in the U.S—But Also At a Corporate <u>or</u> Foreign Collaborator's Site -- And The Research At the Collaborator's Site Is Not Covered By the Fundamental Research Exclusion

- When Sponsors Provide Technical Information *Marked As Export Controlled—*<u>Or</u> *Proprietary/Confidential Information*--- to University Researchers/Staff Who Then Share the Information With Anyone Abroad <u>or</u> <u>With Foreigners in U.S.</u> (Even on Campus)
  - Beware of Nondisclosure Agreements—Contract Should Require The Owner of Confidential Technical Information To Inform You Whether Export Controls Apply and Confirm With Experts *Before* Receiving the Information
  - Contract For Foreign Research Should Require Notice Before Technical Information Is Exchanged To Enable U.S. Institution To Analyze
- When Technical Information Is Emailed, Sent, Disclosed In Meetings or Lectures Abroad—Unless The Information Was Created In Open, Fundamental Research On A U.S. University Campus <u>OR</u> Is Already Published or In the Public Domain

MANAGING RISKS: U.S. REGULATIONS: Export Controls

If Exclusive Material Transfer Agreements or IP Licensing Agreements Impose Publication/Access-Dissemination Restrictions and the Materials and/or Related Technologies/Technical Data are Controlled – Deemed Exports (in U.S., even *on campus)* and Exports (*abroad)* Apply

When Tech Transfer Disclosures are Made Abroad Before a Patent Issues (Becomes Public)--Except When Directly Related to Applying for a Foreign Patent

- When the University Has Reason to Know that Sponsors or Collaborators are Violating Controls (15 CFR 736.2(b)(10))

MANAGING RISKS: INTELLECTUAL PROPERTY

- Contract Should Identify How Ownership Is Determined---Specify Cost and Revenue Sharing for IP Developed Under the Collaboration
  - Joint Ownership If People or Facilities Of Both Involved
  - Sole Ownership Where Developed Using the Facilities and Personnel of One Party
  - Funding Source Does Not Dictate Ownership
- Provide for Necessary Licensing to All Parties of IP Developed in Collaboration
- Specify Manner in Which Commercialization Will be Handled and Also Rights to Further Improvements By One Party to Joint IP
- Wall Off Non-Collaborative IP
- Identify How Jointly Developed IP Will be Administered—Which Party Will Be Responsible, Contribution of Costs, Approval Rights, etc.

QUESTIONS