

On the Importance of Property Rights in Intangibles like IP to Access, Competition, and Economic Development

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Studying Market-Oriented, Property-Rights Approaches to Innovation

Directed by:
[Stephen H. Haber](#) (co-investigator) [F. Scott Kleff](#) (primary investigator) [Troy A. Paredes](#) (co-investigator)

Core Components:

- [Intellectual Property and Innovation](#)
The ways laws, rules, and norms can help private and public sectors work to facilitate the complex processes of innovation and its commercialization
- [Corporate Governance and Securities Regulation](#)
The ways individuals can order their private affairs within collective organizations, or firms, and the ways in which governments can regulate securities markets
- [Property Rights, Finance, and Developing Economies](#)
The role of property rights in intangible assets in the developing world
- [Antitrust](#)
Market structure and performance and the ways antitrust regimes can best promote competition
- [Bankruptcy](#)
The ways the possibility of bankruptcy can influence the way business deals are structured, even at the earliest stages of a venture

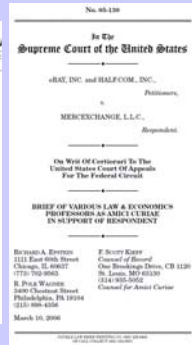
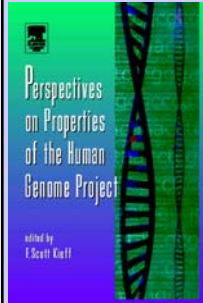
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Modes of Action



Appellate Mediation Program



PATENT PUBLIC ADVISORY COMMITTEE

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How Can Property Rights Help Private Ordering?

- Far more than homes and land
- Modern economic growth is about intangible assets
 - Property rights in contracts
 - Property rights in capital
 - Property rights in intellectual assets
- By “property rights” we mean:
 - predictable and enforceable version of what law calls property and contract
 - more property-based and less regulatory-based
- Not about protecting the wealthy, it’s about fighting poverty

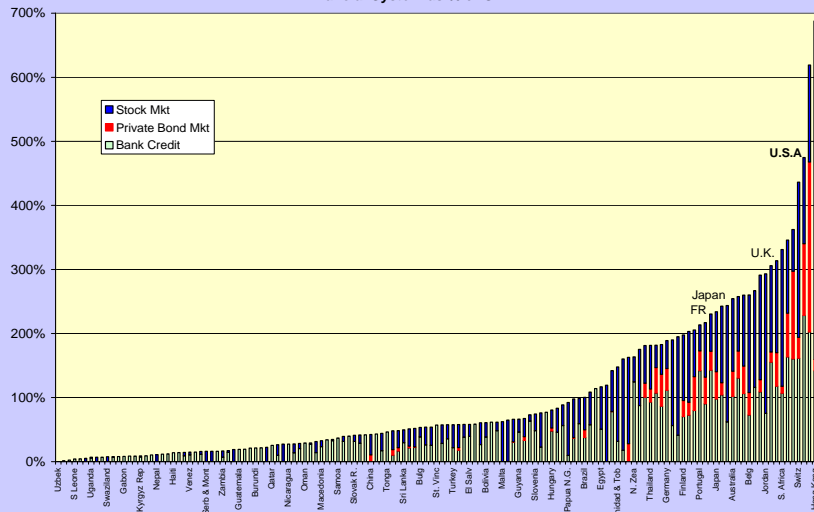


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Comparing Financial Systems

Financial System as % of GDP



(Source World Bank Financial Structure Database)

(Perhaps private ordering is key)

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Example from Finance

(using various intangible assets)

- Consider how banking works
 - Depositors vs. banks
 - Banks vs. debtors
 - Minority shareholders vs. insiders
 - Banks vs. governments
- Compare Mexico
 - No property rights
 - Almost no banking system
 - Around 18,000 home mortgages in entire country last year
 - That's fewer than in Santa Clara County by Stanford



Source: Stephen Haber, Why Banks Don't Lend: The Mexican Financial System (forthcoming), at 26



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Hedge Fund Regulation Example

- SEC rule that hedge fund managers must “register” under the “Investment Advisors Act” (immediately overturned by DC Cir.)
 - Supposed to protect investors
 - Only opt out was if fund had at least a 2-year lock-up window during which investors could not withdraw
 - But threat of withdrawal is what gave investors in small funds needed comfort and control
 - So only large funds with established reputations could attract investors

Patent “Reform” Example: Lofty Goals

- Current patent bill in Congress & Recent Cases like *KSR*
 - One key set of changes focus on what patent lawyers call the “prior art”
 - Today a court adjudicates as a question of fact, based on evidence like lab notebooks or printed theses
 - Proposals would defer to government examiner’s discretion in administrative proceedings about what the state of some art was on some date
- Compare recent *eBay* case giving more discretion for injunctions
- Discretion means flexibility and who wants to be rigid?

Patent “Reform”: Unintended Consequences?

- Problems of discretion – Flexibility’s Achilles Heel
 - Influenced by political pressure and lobbying
 - Big guys win, which turns a law designed to help competition into one that hurts competition
- Example: IBM & Kennedy/Johnson/Katzenbach
 - Discretion to reject any software patent, and eventually all
 - Absence of property rights lead to single large player



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Targeted Solutions to Specific Problems

- Real problem for patents is threat of litigation over bad patents that are presumed to be valid
- So dial down the presumption of validity
- Brings symmetry to fee shifting for baseless cases
 - Today, patentee wants to tell infringer about patent to get attorney fees
 - While the alleged infringer plugs his ears and hides
 - Tomorrow, the alleged infringer would want to tell patentee about prior art
- Helps parties avoid or settle cases sooner



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Why Have IP? Ever Forward!

Mark Twain's Connecticut Yank went to Warwick Castle, England. There he was magically transported back to the time of King Arthur. He did well. He was made First Minister. He was called Sir Boss. What was the first thing he did in power?

The very first official thing I did, in my administration – and it was on the very first day of it, too – was to start a patent office; for I knew that a country without a patent office and good patent laws was just a crab, and couldn't travel anyway but sideways or backwards.

Lord Robin Jacob, Royal Courts of Justice, London, England, *One Size Fits All?* in F. Scott Kieff, PERSPECTIVES ON PROPERTIES OF THE HUMAN GENOME PROJECT 449 (2003).



Why Have IP? Really?!

Is intellectual property good?

To call it “intellectual” is misleading. It takes one's eye off the ball. “Intellectual” confers a respectability on a monopoly which may well not be deserved. A squirrel is a rat with good P.R.

* * * * *

[H]owever justified the cry, “what we need here is protection” may be for an anti AIDS campaign, it is not self evident for a process of the creation of new or escalated kinds of monopoly

Lord Robin Jacob, Royal Courts of Justice, London, England, *Industrial Property-Industry's Enemy*, The Intellectual Property Quarterly, Launch Issue, (Sweet & Maxwell), 1997, pp 3-15.



Property Rights in IP Are Key to Innovation and Competition

(See Kieff, *Coordination, Property & Intellectual Property: An Unconventional Approach to Anticompetitive Effects & Downstream Access*, 56 Emory L.J. 327 (2006))

- Increase innovation
 - Not just incentives to invent
 - Get inventions put to use
 - By facilitating coordination among complementary users of the invention (investors, managers, marketers, laborers, owners of other inventions, etc)
 - The D part of R&D
- Help new companies compete
 - Anti-monopoly weapons
 - Vital slingshot for David against Goliath
- History: Hon. Giles Rich, 1952 Patent Act – don't focus on inventing!



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Property & Coordination – Mechanisms

(See Kieff, *Coordination, Property & Intellectual Property: An Unconventional Approach to Anticompetitive Effects & Downstream Access*, 56 Emory L.J. 327 (2006))

(See Kieff, *On Coordinating Transactions in Information: A Response to Smith's Delineating Entitlements in Information*, 117 Yale L.J. Pocket Part 101 (2007))

- Beacon effect, not control – start conversations
- Bargaining effect – get deals struck
- Liability rules
 - Boil everything down to \$\$, but what about unique assets?
 - Help get bad coordination done (Keiretsu effect)

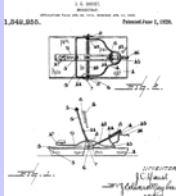


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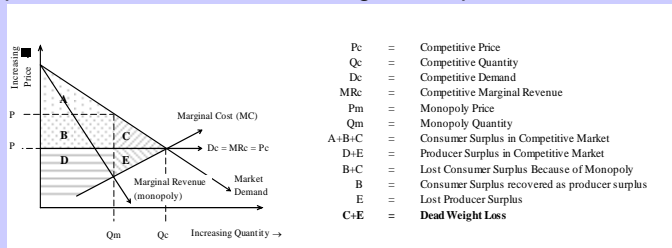


Two Often Missed Keys to IP & AT

- Monopoly refers to markets, not to particular goods or services



- The efficiency problem of monopolies is tied to decreased output, so price discrimination can be of great help



Keiretsu Strategy for IP & AT

- Consider how big players play with and against each other
 - They'd love to talk directly
 - But face two key problems: trust, and antitrust
- What if every legal test turns on discretion?
 - This ensures large numbers of low value IP assets
 - Which helps them coordinate to keep out competition
 - Mitigates trust problem: improves communication
 - Decisions to push and yield transmit preferences
 - Discovery ensures fidelity
 - Mitigates antitrust problem: (blessed by Federal Judges)
 - Insulates from scrutiny generally
 - Mitigates chance of treble damages and jail time even if scrutinized
 - Avoids slingshots from Davids

But Large Players Are at Risk, Too

- Flexibility and discretion are slaves to fashion
- Fighting “The Man” often is the fashion
- And it’s easy to call any big player “The Man”
- Intel calls for flexibility in the US for patents while complaining about flexibility in the EU for antitrust
- The EU favors flexibility for antitrust, but just issued a formal complaint against Thailand for being so flexible on compulsory licenses for drug patents
- As we avoid property in US, we give ammunition to calls for compulsory licensing abroad

Example of Dangerous Flexibility in CFI Microsoft Decision

- Complaint expressed fears about leverage into Media market
 - But most media producers provide content in the formats of multiple players
 - And most producers of players produce players that read multiple formats
 - No surprise the one media player installed on ~99% of Web-connected computers is Adobe’s Flash, used by popular sites like YouTube, owned by Google (and our Hoover page!)
- Remedy demanded version of Windows without player
 - But only copies you can find of those are souvenirs used by law professors as demonstrative aids in class
- The new openness company just announced is better for consumers, which is why the company was already doing it and now increased the practice
- Government pressure may have been one cause, but at what cost?
 - Lack of credibility, in complaint and remedy
 - And why is it otherwise good to shift hundreds of millions of dollars from broad base of public shareholders towards government coffers?

Biotechnology Example

- Before 1980, U.S., Europe, & Japan all had NO patents in basic biotechnology, like DNA
- After 1980, only the U.S. has patents in biotech
 - Large increase in number of new drugs & devices actually commercialized
 - Large pool of ~ 1,400 small & medium biotech companies

(Source 2003 Hearing at House Energy & Commerce Committee, Health Subcommittee, Statement of Stanford Associate Dean Phyllis Gardner)



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Software Example

- No meaningful patents 1972-1996: single large player
- Major threat to MS is not antitrust
- But it is Google, which raised capital and grew using strong patents on search during 1996-2007 window of availability



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Benefits of Norm Communities Like Open Source Compared to Property

(North et al.)

- Any centralization can coordinate
- Can rely on informal norms rather than formal rules
 - Enforcement and other administrative costs can be lower
 - Enforcement can be more predictable and more effective



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Costs of Norm Communities Like Open Source Compared to Property

- Attributes of leadership element – such as fame
 - Not widely accessible, not predictable
 - Less tradable, bundle-able, and divisible
- Problems of crony capitalism
 - Asset specificity and opportunism for insiders
 - Decreased diversity
 - No outsiders
- Empirical research shows open source projects actually are very closed, by very small control groups (consider Linus Torvalds and Linux)
- No meaningful patents 1972-1996: single large player



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Examples of Large Firms and Open Source

- Open source is supposed to make everything free (e.g. IBM gives lots of patents to the public these days)
 - Property rights lead to coordinated development
 - Avoiding property leads to uncoordinated development
 - Uncoordinated software increases demand for consulting services
 - More so than hardware and software, IBM now sells consulting services
- Open science is supposed to increase sharing
 - Merck gave Washington University several million dollars for Human Genome Project on condition of no patents
 - Example of a biotech firm against patents on its own assets?
 - No! Big Pharma against patents on its own inputs!



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Overstating Patent Anticommons

- What if a vast number of IP rights cover a single good or service?
 - Will such a line of business be unduly taxed or retarded?
 - Will transaction costs alone prevent any investment in it in the first place?
- Heller on “anticommons” in the post-socialist environment
 - Why are so many vendors using kiosks in front of empty storefronts
 - Why don’t they come in from the cold?
 - If too many people can say “no” to a use, that use may not occur
- But the explanation is wrong: it’s not the number of permissions that matters
 - It’s the nature of the people from whom permission is needed
 - Bureaucrats can’t openly sell a “yes”
 - Patentees can, want to, and do
 - And the nature of the permission that can be given
 - Permissions of bureaucrats can’t be enforced against them, or others
 - Courts enforce patent licenses and bind everyone
- Think about the typical laptop computer: a bundle of thousands of IP licenses that can be bought with one click on the Internet for \$1,000



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World Health & Development: Lofty Goals?

- Fear of patents helping people in Africa die from AIDS and malaria
- Initiatives at WHO & WIPO last year and this year
 - Increase compulsory licensing (like Thailand)
 - Reject technical assistance as hegemonic

World Health & Development: Reality Check

- What's wrong with the new initiatives?
 - Over 95% of drugs on WHO's essential medicines list are off patent
 - When patented drugs are given to those countries for free they are heavily taxed or outright taken by corrupt local governments – sometimes even resold on black markets to U.S., Japan, Europe, etc
 - Millions of real people are dying from war, famine, unsanitary conditions, lack of basic health care, etc
 - Uganda's DG of public health, Dr. Zaramba, wants DDT for malaria
- Who is behind them? (Argentina, Brazil, India)
 - Holders of biodiversity inputs (upstream of those patents)
 - Having developed manufacturing organizations (that would need to pay royalties)
- Who disagrees? (Botswana, Malawi – they're in Africa!)

World Health & Development: Keys to Success

- Strengthening the rule of law empowers local populations at the grassroots level to overcome distribution obstacles
- Protecting patents and enforcing contracts serve as essential enabling devices for development of the businesses needed to get distribution done
- Why reject gifts of technical assistance? Just because it comes from someone you think is hegemonic doesn't mean it's a bad idea
- Many wonderful government, private, foundation, and NGO efforts are already being made to improve access to basic health care and have high impact, immediately



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World Health & Development: Untapped Resources

- One natural resource uniformly distributed among peoples of the world is intellectual capital
 - Sure, patents won't immediately cause those in a LDC to develop the next blockbuster pharmaceutical of the type we know takes teams of PhDs and hundreds of millions of dollars
 - But it takes academic snobbery to think innovation can't be valuable unless it happens at a G8 university
 - Lots of valuable IP is particularly likely to be found in LDC's
 - Necessity can be the mother of invention and regions where improvements in basic irrigation and agriculture techniques are to help the most are those where innovations are likely to occur
 - Valuable IP need not be technological – remember how much of the commercially successful music and fashion in the west incorporates substantial African influences



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These stories are not just fantasy: They are real, and current



Also remember the ongoing trademark disputes between Anheuser-Busch Budweiser (U.S.) and Budejovicky Budvar (Czech)



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At Bottom, the Details Matter: Property Rights at Their Best

- Attributes
 - Predictable enforcement
 - Good flexibility
 - Can be traded and licensed
 - Can be bundled & divided
 - Users deal with private individuals
- Effects
 - Easy for market actors to use
 - Stimulate competition, innovation, economic growth, and jobs



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At Bottom, the Details Matter: Property Rights at Their Worst

- Attributes

- Bad flexibility
 - Created or changed at discretion of government
- Rigidity
 - Fixed owner
 - Fixed contours
- Users deal with government

- Effects

- Easy for political actors to use (regulators and powerful political constituents)
- Concentrate wealth and power

Why even call these things property rights?
Aren't they really regulatory entitlements?

