IP and Other Regulations¹

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Intellectual property (IP) is a form of regulation. As I have argued elsewhere,³ IP laws are deliberate government interventions in the market to try to shape how people participate in that market, encouraging new creation by rewarding it with above-market returns and discouraging imitation by imposing damages or even barring it altogether.

Once we understand IP laws as government social policies that seek to alter market outcomes, we can start to think of those laws as part of a broader tapestry of government rules that affect innovation in a complex variety of ways. Daniel Hemel and Lisa Ouellette have already situated IP regimes among a variety of other government policy levers designed to affirmatively encourage innovation and market entry, including prizes, grants, and tax incentives.⁴

But the potential role of regulation in encouraging market entry is not limited to offering various forms of government-sponsored largess to innovators. More traditional forms of regulation restrict market entry. Doing so offers supracompetitive returns to market incumbents who benefit from the entry barriers regulations impose. Taxi drivers benefit – or did until quite recently – from the absence of a truly competitive market, propped up by government limits on market entry. So too do the learned professions, which limit entry into their fields, sometimes in quite blatantly anticompetitive ways.⁵ Pharmaceutical companies benefit from the limits the FDA puts on generic entry, over and above – and sometimes regardless of – the existence of patents.⁶

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³ See, e.g., Mark A. Lemley, *Taking the Regulatory Nature of IP Seriously*, 92 **Tex. L. Rev. See Also** 107 (2014); Mark A. Lemley, *The Regulatory Turn in IP*, 36 **Harv. J. L. & Pub. Pol'y** 109 (2013).

⁴ Daniel J. Hemel & Lisa Larrimore Ouellette, *Beyond the Patents-Prizes Debate*, 92 **Tex. L. Rev.** 303 (2013).

⁵ See, e.g., *National Society of Professional Engineers v. United States*, 435 U.S. 679 (1978), *North Carolina Board of Dental Examiners v. Federal Trade Comm'n*, ___ S.Ct. ___ (2015).

⁶ John R. Thomas, *Regulatory Exclusivities* (working paper 2015); Rebecca S. Eisenberg, *The Role of the FDA in Innovation Policy*, 13 **Mich. Tel. & Tech. L. Rev.** 345 (2007); Rebecca S. Eisenberg, *Patents, Product Exclusivity, and Information Dissemination: How Law Directs Biopharmaceutical Research and Development*, 72 **Fordham L. Rev.** 477 (2003); cf. Benjamin N. Roin, *Unpatentable Drugs and the Standard of Patentability*, 87 **Tex. L. Rev.** 503 (2009) (arguing that patent law should be expanded to cover drugs that were not novel in order to give regulatory exclusivity).

Each of these forms of market-entry regulation, like patents, can be defended as a socially desirable departure from the competitive norm. I find some of those claims more plausible than others. Artificial restrictions on the number of taxis, for instance, seem to me to do far more harm than good. Restrictions on free entry into drugs or the medical profession seem more important for health and safety reasons, though often government regulations in these fields impose more significant limits on competition than those rationales require. But there is nothing *inherently* good about restricting competition. At a minimum, the claimed need to depart from the market outcome to achieve some social goal must be viewed with some skepticism and weighed against the loss of competition that results from regulation. Insulating companies from competition allows them to raise prices, hurting consumers. It may also insulate them from the very forces that drive efficiency and change.⁷

So too with IP. Whether an IP rule is worth the cost depends, as it does with any other regulation, on whether the benefits we get from that rule (presumably increased or higher-quality innovation or creativity) are worth the costs. Answering that question is hard, not just because the evidence we have about the efficacy of IP rights in encouraging innovation is mixed at best.⁸ It is also hard because sometimes – often, in fact – it is competition, *not* regulation, that drives innovation.⁹ So sometimes creating or strengthening an IP regime can be counterproductive, not only raising prices but stifling the very innovation it was supposed to encourage. The fact that the most innovative companies in the world today are overwhelmingly defendants, not plaintiffs, in patent cases is a worrisome sign that the patent system is not serving its purpose in many industries.

Finally, striking the balance is hard because IP is not the only regulatory regime that might be used to insulate innovators from competition and hence potentially encourage them to innovate. Both Nicholson Price and Guy Pessach explore this complication in their papers for this symposium. Price points out that FDA restrictions on generic entry in the pharmaceutical and biologics markets can be more powerful than patents in blocking entry, and that restricting patent rights may drive companies to greater reliance on trade secrecy. He worries that the combination of secrecy and the FDA rules regarding generic drug entry may make it even harder for generic drug companies to enter the market than patents do, and may restrict the benefits of public disclosure of ideas.¹⁰ I am less worried about a shift to trade secrecy than he is, in part because I think secrecy is a lot less airtight in the modern world than one might

⁷ Kenneth J. **Arrow**, *Economic Welfare and the Allocation of Resources for Invention*, in *The Rate and Direction of Inventive Activity: Economic and Social Factors* 609 (Richard Nelson ed., 1962).

⁸ Mark A. Lemley, *Faith-Based Intellectual Property*, __ **UCLA L. Rev.** __ (forthcoming 2015); Lisa Larrimore Ouellette, *Patent Experimentalism*, 101 VA. L. REV. 8 (2015).

⁹ Arrow, *supra* note __; Mark A. Lemley, *Industry-Specific Antitrust Policy for Innovation*, 2011 **Colum. Bus. L. Rev.** 637.

¹⁰ W. Nicholson Price II, *Regulating Secrecy* (working paper 2015).

suspect,¹¹ and in part because I think the benefits of public disclosure from patents are overstated.¹² But the core point that FDA entry regulation represents an alternative and potentially more anticompetitive restriction than patent rights is an important one. And it may become more important still; Congress is talking about a dramatic expansion in data exclusivity for traditional pharmaceuticals from five years to match the twelve-year period for biologics. Whether that is a good or a bad thing depends, of course, on whether we think we need even stronger insulation from competition to drive drug discovery. But it means that patents are not the only form of regulation we need to assess in deciding innovation policy for pharmaceuticals.

Guy Pessach worries that the reduced efficacy of IP, particularly copyright, in the Internet era will lead to a variety of harmful social consequences. As it becomes harder to charge for content online, he fears we will see a concentration among content providers, concentration among intermediaries, as well as a shift towards socially-problematic non-price means of recouping investments, like ubiquitous surveillance and the loss of privacy. He sees government regulation as a solution to some of these concerns, and views IP rights as potentially serving a social end beyond encouraging creativity: encouraging us to pay for that creativity in direct and visible rather than indirect ways.¹³ Here, too, IP is serving as a form of regulation, one that in Pessach's view trades off against other forms of regulation.

The potential loss of privacy that accompanies the free flow of information on the Internet is a concern that has occupied a number of people. But I'm not sure that stronger IP rights or other forms of government regulation are the answer. Pessach assumes that because consumers have been willing to trade private information for free access to content, making it easier to charge for that content will induce creators and intermediaries to give back the privacy we have lost. I'm dubious. The lesson of other markets has been that if companies can find a way to charge twice, they will. (Remember when paying for cable television was justified on the basis that you wouldn't have to see ads?). And precisely because the sharing of customer information is an indirect, non-transparent way of charging companies are unlikely to give it up unless forced to. And while the government could take a more direct regulatory approach, limiting what information people can collect and share, doing that has its costs as well. I trust the government with control over my information far less than I trust Apple or Google.

¹¹ Indeed, trade secret law may actually encourage disclosure and licensing. See, e.g., Mark A. Lemley, *The Surprising Virtues of Treating Trade Secrets as IP Rights*, 61 **Stan. L. Rev.** 311 (2008).

¹² Mark A. Lemley, *The Myth of the Sole Inventor*, 110 **Mich. L. Rev.** 609 (2012). Compare Lisa Larrimore Ouellette, *Do Patents Disclose Useful Information?*, 25 **Harv. J. L. & Tech.** 531 (2012).

¹³ Guy Pessach, *Beyond IP – The Cost of Free: Paradoxes of Informational Capitalism* (working paper 2015).

I am also dubious that reducing IP will drive greater market concentration. Certainly the lesson of the Internet so far has been the opposite. It has driven an unprecedented outpouring of new content from a far wider variety of creators than ever before in history.¹⁴ Nonetheless, that astounding variety of new content is being transmitted through fewer and fewer intermediaries, and the government has exercised little control over those intermediaries. Pessach is right that IP doesn't exist in a regulatory vacuum, and that the market moves as IP recedes may be ones that trigger other forms of commercial behavior (such as market concentration) we like even less.

All of which leads to a final point. Regulation (whether IP or not) tends to restrict market entry in various ways. Doing so interferes with competition. It might be worthwhile to block that competition if the market-entry regulation serves a useful social purpose, and encouraging innovation can be such a useful social purpose. But traditional forms of regulation, including IP, should be viewed with skepticism, because they reflect the government's judgment that it knows better than the market. That is a judgment that has often proven false.

There is another form of regulation, however, that tends to open markets rather than restrict them. If Pessach turns out to be right that the weakening of IP on the Internet leads to increased market concentration, we might turn to regulation, not to give market control to incumbents, but to take that control away from them. Antitrust is a classic example of regulation in the service of deregulation: a government intervention designed to preserve the functioning of the market in the face of anticompetitive conduct or a systemic market failure. The new net neutrality regulations may be another example, keeping the Internet open to new entry in the face of structural forces that would concentrate it among a few players.

Here too we need to be careful; market-opening regulations like antitrust have in the past been coopted by incumbents to restrict rather than promote competition, and the same could still turn out to be true of net neutrality. But as we think of the broader regulatory toolbox for encouraging innovation, it is worth keeping in mind not only regulations that encourage innovation by restricting competition (within IP or without), but also regulations that might encourage innovation by encouraging competition.

¹⁴ See, e.g., Mark A. Lemley, *IP in a World Without Scarcity*, __ **NYU L. Rev.** __ (forthcoming 2015) (collecting evidence).