

The Patent Prejudice: Intellectual Property As Monopoly

by Solveig Singleton*

"[T]alk of the 'patent monopoly' weds patents to prejudice, which is not conducive to clear thinking."

- Judge Giles S. Rich¹

Many key technology policy debates in the last hundred years or so have turned on the concept of monopoly. Patents and copyright, each a grant of exclusive rights in created works, have also come under the scrutiny of anti-monopolists. The assessment of IP as monopoly is now particularly predominant in international policy circles, including comments of World Bank economist Joseph Stiglitz.²

This paper considers the justice of the charges that intellectual property rules establish "monopolies." While intellectual property—like physical property—fits into a loose definition of monopoly, this is a rhetorical flourish rather than a policy insight. Physical property rights also fit. Neither patents nor copyrights can be fairly thought of as creating economic monopoly in a way that injures consumers. Recent developments in antitrust law bear this out, with the courts retreating from doctrines that presume that intellectual property creates undue market power, and theorists noting that the overall goals of antitrust and intellectual property are consistent.³

IP As Monopoly: An Overview

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¹ Giles S. Rich, "The Relation Between Patent Practices and the Anti-Monopoly Laws," 14 Fed. Cir. B. J. 8 (2004-2005).

² See, e.g., Joseph E. Stiglitz, "Give Prizes Not Patents," The New Scientist, Sept 16 2006, p. 21; Stephen Kotkin, "Aiming to Level Global Playing Field," The New York Times, September 3, 2006, p. 7.

³ See, e.g., Presentation of Thomas O. Barnett, Assistant Attorney General, to the George Mason University School of Law Symposium Managing Antitrust Issues in a Global Marketplace, "Interoperability Between Antitrust and Intellectual Property," September 13, 2006. An alternative argument is that insofar as IP and antitrust cannot be reconciled, especially in the individual case, that IP is actually more effective than antitrust in promoting competition, provided one avoids an extremely short run view of competition and a narrow definition of markets.

The treatment of intellectual property, particularly patents, as monopoly, has venerable historical roots. But since this initial experience, both intellectual property law and the economy have undergone significant changes. This section surveys the record.

At one time, patents were handed out to favorites of Queen Elizabeth and James I, a practice limited by the Statute of Monopolies of 1623, which extended the rights only to the true and first inventor of a method of manufacture for fourteen years. Copyright was in the beginning a monopoly right to publish and an instrument of content control, in England originating with in 1556 with a grant to the Stationers Company. Being associated with monarchy and mercantilism, monopolies naturally were a focus of classical liberal political theorists during the eighteenth and nineteenth century. This includes leaders of the American Revolution, such as Jefferson and Madison as well as economists such as Adam Smith and Bastiat.

But the assertion that the early debate about patents or copyrights concluded that intellectual property is on a par with monarchical grants to favorites, or even with purely utilitarian primitive attempts at industrialization, is a gross oversimplification. As Adam Mossoff's historical research has shown, social contract theory began to make both patent and copyright into something befitting an advanced civil society and justified by the labor theory of value.⁴ Thus Adam Smith concluded, "the property one has in a book he has written or a machine he has invented, which continues by patent in this country for fourteen years, is actually a *real right*."⁵ And by the nineteenth century, judges commonly treated patents as a species of property right, speaking of, for example, "trespass" on the patent, "piracy," "tenants in common" of a patent, and patents as "title."⁶

A comparison to physical property law is helpful here. Physical property law has its own appalling history of association with powerful interests, slavery being one glaring example. Yet it would be a mistake to think of physical property rights in essence as a form of rapine, as did Proudhon ("property is theft!"); these rights are the foundation of markets, trade, and conflict resolution, and attempts to abolish property altogether have gone sadly awry for want of better arrangements.

The condemnation of intellectual property as monopoly continues in vogue today, as if we were still living in the seventeenth century. Eldred's brief before the Supreme Court uses the term "monopoly"⁷ at every possible opportunity (the technical legal term for this is "overplaying your hand"). And so various reports describe the profits of IP owners as "rents," the term for inefficiently high revenues; their prices are supposedly too high; finally, IP is said to encourage wasteful clustering of investment, or

⁴ Adam Mossoff, "Who Cares What Thomas Jefferson Thought About Patents? Reevaluating the Patent 'Privilege' in Historical Context," 92 Cornell Law Review (forthcoming 2007).

⁵ Adam Smith, Lectures on Jurisprudence, 82-83 (R.L. Meek et al eds., Oxford Univ. Press 1978)(1762).

⁶ Mossoff, at 41-49 (pages numbers refer to submission draft on file with author). Note that there were exceptions, judges and legal scholars who took Jefferson's more skeptical view of patents.

⁷ Brief for Petitioners at 3 n. 5; 10; 16; 16 n.5; 17, 18, 21, 22, 23, 24, 27 n. 12; 37 n.4, Eldred v. Ashcroft, 123 S. Ct. 769 (2003) (No. 01-618).

overinvestment. If IP did create monopoly in the economic sense, these conclusions would follow.

But both the law of intellectual property and the economy have changed drastically over the centuries. From the standpoint of an advanced economy, the formation of ground rules to facilitate trade in intellectual goods seems understandable. More and more value is created in the form of intangibles in association with intellectual capital, as compared to physical capital. Sweeping references to patents or copyrights as forms of monopoly add nothing to one's understanding of today's law and markets, and indeed confuse the issue.

Everything and Nothing as a Monopoly: Definitions, Definitions

Today's intellectual property is often spoken of as legal or economic monopoly. But monopoly is a rather slippery concept. Defined too broadly, almost anything is a monopoly, but then it ceases to be either interesting or frightening. The narrower definition is more interesting, but then monopoly becomes rather rare. And both these observations turn out to hold for intellectual property rights as "monopolies" as well.

The Legal Monopoly

One definition of a monopoly is the grant of an exclusive right by the state,⁸ a legal monopoly usually intended to give control of a particular market. Patents and copyrights easily fit that definition, thus the Supreme Court routinely refers to intellectual property as a "limited monopoly." But physical property also fits this definition. A restaurant with an auspicious location on a busy corner has a monopoly on that unique locale, and claims an exclusive right to enjoy the profits that flow from it. Copyright is similar--it gives the rights-holder the right to say, one poem, and the corresponding profits if that poem proves wildly popular.

Now, the rights granted by intellectual property are broader than physical property rights; the property right in an apple gives you the exclusive right to one apple, not to all apples, or to all copies of a poem. But here it should be noted that it would be a rare patent that gave one a claim to anything analogous to "all apples."⁹ (While some

⁸This definition does not clearly include private monopolies; these would usually be the economic monopolies described below.

⁹ Similarly, Richard Epstein argues, "Monopoly and property rights are not opposite sides of the same coin, they are the same side of the same coin. To some extent, if you look at the formal definitions, they are remarkably similar, in their stress on the sole control over a given thing. But it's a vast difference to control a piece of land, on the one hand, and to control a complete market on the other hand. So, to go to the real estate situation, I may have the right to exclude everybody absolutely from 4824 South Woodlawn Avenue where I live, but I don't have that right over 4830 or 4820, my two neighbors. Most critically, when you have monopolies that are close substitutes for one another, in practice, you have a competitive market with strong property rights. In the intellectual area, exactly the same issue has to take place. [In *Independent Ink*] the Supreme Court did exactly the right thing when it eight-to-nothing stressed the difference between the patent that dominates the entire area and one which, by way of analogy, just gives its holder 4824 South Woodlawn, and nothing more." Richard A. Epstein, "The Structural Unity of Physical and Intellectual Property," *Progress on Point* 13.4, October 2006, at 9.

such patents have indeed been granted—the Australian patent on the wheel being a case in point—they would not survive any attempt at enforcement). Patents are limited in time and scope. And it makes little sense to think of every copyrighted poem as existing in its own market. Most importantly, in all of these cases—physical property, copyright, and patent—while exact substitutes for the claimed property are not available, enough "good enough" substitutes are available over the long run that these "monopolies" are not very interesting from a policy standpoint. That is, the "market" that they allow control over is from the standpoint of price, consumers, and common sense not susceptible to a narrow definition. If everything is a monopoly, nothing is.

Legal monopolies become interesting if the market that they facilitate control over is a broad one rather than a narrow one. The Post Office is such a monopoly (though the advent of email, a ready substitute for first class mail, has made it less so). When the market controlled is fairly broad, the legal monopolies tend to turn into economic ones, where competition is restrained in a meaningful sense.

The Economic Monopoly

The economic definition of monopoly and related¹⁰ antitrust doctrines are concerned with restrictions on output and prices. Under this theory, interesting monopolies are those for which so few substitutes are available that the monopolist can charge supra-market prices. As described by Professor Edmund Kitch, the seller is "protected from competition and able to sell into a market with a downward sloping demand curve."¹¹ That is, even if the good could be provided at a marginal cost less than the price buyers are willing to pay, there is demand that would not be met.

Note that there are problems with this definition. The theory relies on a definition of efficiency from which it follows that prices "ought" to be set at or near marginal cost. But if this happened in the real world, the economy would grind to a halt. There would be no profits to excite entrepreneurs to enter the market. This suggests there is something wrong with using this definition of efficiency for normative purposes, and a number of economists have subjected it to a vigorous critique.¹² Antitrust concepts of monopoly are even more troubling, for they combine dubious measures of efficiency with a set of populist policy goals and the peculiar incentives of the legal system.

Setting these issues aside, how well does intellectual property fit the usual definition of an economic monopoly?

Not ordinarily, Professor Kitch points out. Certainly not every "legal monopoly" described above does (and a common sleight of hand in arguments about intellectual property is to switch from the former "anything goes" legal definition of monopoly to the

¹⁰ The dispute about how closely economic and antitrust ideas of monopoly follow one another is beyond the scope of this paper.

¹¹ Edmund W. Kitch, "Elementary and Persistent Errors in the Economic Analysis of Intellectual Property," 53 Vand. L. Rev. 1727, 1730 (2000).

¹² See, e.g., Gordon Tullock, "The Two Kinds of Legal Efficiency," 8 HOFSTRA L. REV. 659, 668 (1980).

latter). Patents are limited to the new and non-obvious. In well-developed fields, such as aerodynamics, patents tend to be narrow and rather rare. In new fields, patents may be broader and more common, but "[s]ince the technology is new, there is usually very little demand for it. In order to achieve commercialization, much more work remains to be done."¹³

Thus while patents can help give an entrant a head start that leads to a monopoly in the economic sense, this is quite rare. This remains true even though some patents granted by the patent office would not, upon closer scrutiny, satisfy a more exacting standard of non-obviousness. When there is what economists would usually call monopoly, there are usually dominant contributing factors other than the mere existence of a patent.¹⁴ One example might be the Bell company's nineteenth-century patents on elements of the telephone network, which gave Bell a head start over the independent's in building out their network. But here the other dominant factors include being first to market, licensing terms, network effects, and the possession of key physical assets. Finally, "good enough" substitutes for a patented product are almost always available, if not in the immediate run, then in the short or long run.

This is even more true of copyrighted items, such as a song or a book. While each good is indeed unique, the media market offers plenty of goods that a consumer would buy instead if his first choice is not available. Thus professor Kitch concludes, "it seems likely that all trademarks, almost all copyrights, and most patents are not monopolies."¹⁵ If patented products are priced above marginal costs, this is because the producers must recover all the costs of production, including research and development. And patents and copyrights help them to do that by excluding free riders. Following Schumpeter, strong exclusive rights may sometimes be necessary to encourage innovation¹⁶ and thus there is more competition with such rights than without. Richard Epstein notes, "the patent system, in fact, undermines the economic power of the first patentee by giving incentives to rival inventors to develop ... other combinations."¹⁷

Antitrust cases are beginning to recognize that intellectual property rights ought no more to be automatically equated with monopoly than any other valuable asset. In

¹³ Ibid., at 1731.

¹⁴ Robert Pitofsky remarks that markets based on intellectual property have a greater tendency to exhibit network effects. Prepared Remarks of Robert Pitofsky, "Antitrust and IP: Unresolved Issues at the Heart of the New Economy," March 2, 2001, available at <http://www.ftc.gov/speeches/pitofsky/ipf301.htm> (accessed October 19, 2005). See also Ariel Katz, "Intellectual Property, Antitrust, and the Presumption of Market Power, Making Sense of Alleged Nonsense," DRAFT, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=702462. But the observation simply fails for the vast majority of sectors based on IP--pharmaceuticals, publishing, biotech, and so on. When markets based on IP exhibit such effects (e.g. telecommunications in the nineteenth century) the network effects are attributable, not to the IP, but to the presence of a network. It makes as much sense to attribute the presence of such effects to contracts as to IP.

¹⁵ Kitch, at 1734.

¹⁶ Joseph A. Schumpeter, *Capitalism, Socialism and Democracy* 84 (3rd. Ed. 1950).

¹⁷ Epstein, at 9.

Loew's v. United States,¹⁸ the Court had that market power could be presumed when the sale of one product was tied to another which was patented or copyrighted. In 2006, the Court finally reversed this presumption in *Illinois Tool Works, Inc. v. Independent Ink, Inc.*,¹⁹ so that market power must be proved even when the product is patented or copyrighted.

The case of pharmaceuticals that cure fatal diseases such as AIDS are worth a special note. In poor countries where such diseases are widespread, it is tempting for policymakers to find a short-cut out of this very real crisis by denigrating patents. If patents are exploitive monopolies, there would be no great cost to simply taking the asset using a mechanism like compulsory licensing and redistributing it to those in need. But to maintain the incentives to produce medicines in the long run, the simple economic fact is, that the market price for the medicine must be well above marginal cost. Compulsory licensing or other forms of outright expropriation would turn out to have high costs indeed, for the next generation of medicines. Unfortunately, this does not make the AIDS crisis go away. The best alternative is to support patent-friendly solutions to the problem, such as reducing tariffs on imported medicines in poor countries. But sympathy for those who suffer from illness does not constitute an argument against the patent system.

Conclusion: Competition, Creation and Consumers

Akin to if not exactly alike physical property rights, intellectual property rights do more for competition than against it. Patent and copyright offer basic ground rules to enable producers to transform intellectual capital into bundles of rights that can be bought, sold, or licensed. In the vast majority of cases, they simply do not fit any interesting definition of monopoly. In the short run such a product might be—indeed, must be—priced above cost. This is simply an incentive for other producers to offer substitute goods. Consumers will tend to have more choices in a universe with intellectual property rights than without. There is room for argument about exactly what form such rights should take, but rhetoric about monopolies is nothing but a distraction.

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¹⁸ 371 U.S. 38 (1962).

¹⁹ 506 U.S. ____ (March 1, 2006).