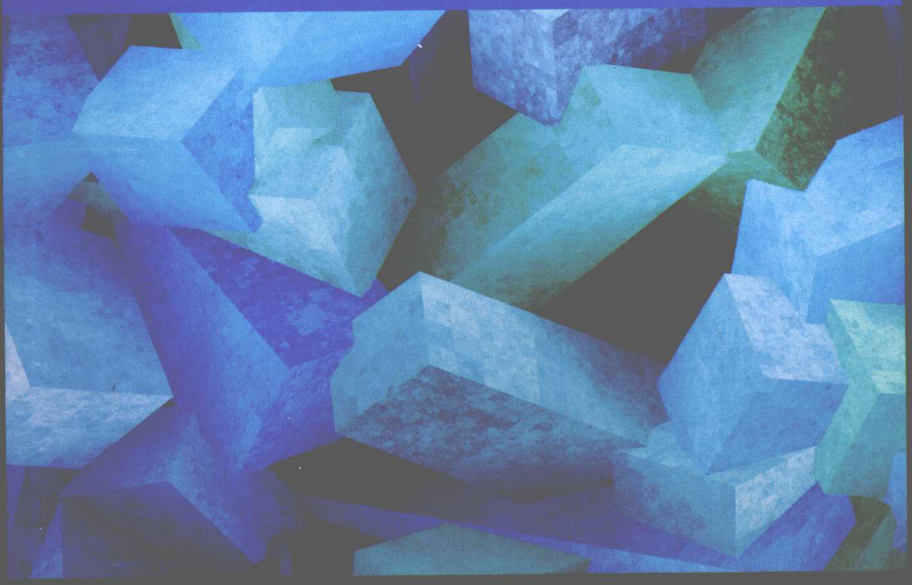
Innovation, Competition and Consumer Welfare in Intellectual Property Law



Gustavo Ghidini

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Preface

Giuliano Amato

Gustavo Ghidini has an excellent grasp of both the principles and the many specific provisions underlying intellectual property law in Italy and Europe. Nevertheless, he is neither a dogmatist nor an exegete immersed within the horizon of the texts he reads. He has a powerful vision of the politics of law, regularly setting it out in his premises and grounding it in his interpretation of current principles, which he justifies. He then projects it in his examination of concepts and individual regulations, which sometimes corroborate it but in other cases refer back to it, and on yet other occasions contradict it – at which point Ghidini observes that the original idea was wrong. This is why Ghidini's books are never dull. Just the opposite: they are always warm, argumentative and intent on proving a hypothesis. As a result, his works are far more enjoyable than conventional law books and the merit is his alone, because he goes beyond the most rigorous standards of scientific soundness and plainly legal analysis.

Experts on industrial property and antitrust law are very familiar with his vision of the politics of law. Nonetheless, Ghidini, who also appreciates – and practises – economic analysis, has never accepted the conclusions reached by the school that, more than any other, established this field: the Chicago School. Thus, he has never replaced efficiency with competition as the ultimate aim on which to base regulations and decisions concerning the market. Consequently, he has never ceased to promote the openness and well-being of the consumer, achieved by not reducing output and by the variety of possible choices, nor has he ever been ashamed of the legal opinion – once American but now purely European – according to which, in some cases, the weakest competitors must be protected in order to protect competition.

In the context of such a vision, the monopoly rights of intellectual property law – patents, copyrights and trademarks – are embraced if and as long as they are consistent with 'the guiding principle of free competition', whereas the laws governing them must preferably be interpreted from a pro-competitive standpoint. As Ghidini rightly points out, however, this does not go against their nature by any means. Indeed, their juxtaposition with competition couldn't be simpler, given the monopoly element that characterises them, but their ultimate purpose is to make the market more competitive.

Ghidini is quite harsh towards industrial countries as well as TRIPs (which have denied emerging countries what industrial countries once granted to themselves). At the same time, however, he goes to great pains to distance himself from the generalised and often ideological 'no global' protest against these same targets, accusing this protest of completely ignoring the reasons for protecting investments earmarked for research. Furthermore, and precisely because he, in turn, does not think along ideological lines, he is also very careful to avoid generalising the claim that monopoly rights have counterproductive effects, since, in reality, these have emerged only in specific sectors. And he cites network industries, starting with communications, biotechnologies, and automotive and household-appliance components, and culminating with the 'rapidly expanding frontier' of areas (chiefly communications for the time being) in which consumers can interact with manufacturers and redevelop, integrate and transform the product or service they are receiving. But when this happens – he wonders – what then is the meaning of traditional absolute protections?

No one, not even those who usually disagree with Ghidini, can deny the meaning and implications of such a question. This kind of necessary acknowledgement is the best reward for his vision and for the steadfastness – never aprioristic nor unwarranted – with which he applies it. It is thanks to this vision that he grasps change and, more rapidly and readily than others, notes its effects on law and previous legal opinions, to which one cannot remain indiscriminately faithful when their impact given a changed reality generates effects that are the opposite of the ones that warranted them in the first place.

A great legal scholar, Carlo Esposito, wrote that not only regulations but even principles themselves do not express absolute truths, but rather incorporate contingently persuasive practical reasons. Consequently, rules must remain in place as long as the principles that they express continue to be valid, but they must be changed when it turns out that they are no longer shared and perhaps other rules are de facto taking their place. Perhaps Esposito, who loved to go to extremes in his reasoning, overshot the mark by denying the absolute value of any principle and submitting to actuality. Of course, if regulation of the wheel had been based on the wheel being square and then someone finally invented a round wheel, such regulation could hardly remain the same. Esposito was unquestionably right about this, and it is this very subject that Ghidini discusses in his book. Those who fail to heed him are doing so entirely at their own risk.

Preface to *Intellectual Property and Competition Law*[1]

J.H. Reichman

Professor Gustavo Ghidini has undertaken a searching study of the way the European intellectual property system is evolving away from pro-competitive premises that underlie the classic patent and copyright paradigms in response to strong protectionist pressures (and relentless special-interest lobbying) that have accompanied the integration of markets at both the regional and global levels. Alarmed by what he finds, Ghidini reminds us at the outset that intellectual property rights are not ends in themselves. Properly conceived, they are instruments for preserving and enhancing that system of free enterprise and free competition that finally replaced the 'guild' and 'corporate' models of the not too distant past. Viewed from this perspective, Ghidini warns that more intellectual property rights, and especially too much of the wrong kind of intellectual property rights, may cumulatively yield unacceptably high social costs by compromising the competitive ethos whose tenets were embodied in Italy's post-war economic constitution.

With these tenets in mind, he proceeds to evaluate the far-reaching reforms of recent years, which have aligned the European Union member countries' intellectual property laws with the harmonising directives of the European Commission and with the international minimum standards of the World Trade Organization's Agreement on Trade-Related Aspects of Intellectual Property Rights ('TRIPs Agreement'). His project is to determine the extent to which the product of these reforms remains consistent with the fundamental goal of promoting free competition. Have the reformers preserved an appropriate balance of public and private interests that suitably accommodates that goal? Or have they rewritten the rules of the game so as to allow powerful firms to exploit rent-seeking legal monopolies that create barriers to entry and that may actually discourage the kind of innovation on which today's processes of dynamic competition most depend?

[1] G. GHIDINI, *Intellectual Property and Competition Law: The Innovation Nexus*, Edward Elgar, 2006.

To answer these questions, Ghidini focuses attention on the economic justification of intellectual property rights as a means to address the potential market failure associated with the production of public goods. Here he emphasises that the purpose of using intellectual property rights to cure market failure is to avoid suboptimal investment in innovation by entrepreneurs who might otherwise remain vulnerable to unbridled free-riding on the fruits of their investment. If, however, the set of legal incentives used to stimulate the first-comer's investments unduly deters second-comers from making further investments in follow-on applications, the regime in force will merely have traded one kind of market failure for another. Thus configured, a national system of innovation might produce no net long-term gains in competitive output, and it could actually slow the pace, and distort the quality, of research and development over time. In short, a modern intellectual property system devoted to stimulating constant innovation must seek a dynamic equilibrium that avoids both the perils of free-riding duplication and the proliferation of ill-conceived legal monopolies that enable rent-seeking oligopolists to control and stifle follow-on innovation.[2]

These premises lead Ghidini to treat the separate intellectual property disciplines – especially patents, copyrights, and trademarks – as part of a single national system of innovation and to examine the extent to which the reforms under way in each compartment of that system coherently promote cultural progress and the growth of investment in productive research and development. He will particularly single out ways in which recent legislative developments may have tipped the balance too far in a protectionist direction; and in each case, he proposes interpretations or, where necessary, modifications and amendments that could help to redress the balance in favor of those underlying competitive goals that ought to drive the system as a whole. In effect, he undertakes a quest for present-day functional equivalents of the 'pro-competitive antibodies' that were built into the classical, bipolar system of intellectual property rights that Italy inherited from the industrial revolution.

At the same time, Professor Ghidini looks beyond these disciplines to ancillary rules sounding in unfair competition law and to the principles of antitrust law, which have the power to curb and limit the strength of specific intellectual property rights in order to promote the maintenance of orderly and efficient market conditions. He thus views both unfair competition law and antitrust law as major potential correctives of the vices and abuses that increasingly distort the workings of legal incentives to invest. Here, indeed, he

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[2] See, e.g., KEITH E. MASKUS and JEROME H. REICHMAN, *The Globalization of Private Knowledge Goods and the Privatization of Global Public Goods*, in *International Public Goods and Transfer of Technology under a Globalized Intellectual Property Regime*, Cambridge, 2005.

is comforted by new developments in both legislation and case law that seek to promote the interests of researchers, users, consumers, and competitors in ways that balance the protectionist thrust of the intellectual property regimes themselves and that seek to restore the conditions needed for healthy competition. To the same end, he advises courts, legislators and administrators to view these correctives as an integral part of the Italian system of innovation, and he attempts to provide them with the legal tools they will need to accomplish this task, without the parochialism that has sometimes constrained judicial applications of unfair competition law in the past.

Professor Ghidini's latest work thus provides scholars, judges and practitioners with a comprehensive and penetrating study of intellectual property law that attempts to integrate its specific incentives to create into a larger system of free competition. His ability to weave these diverse strands into a compelling and coherent vision of the whole is an educational delight in itself, even if one comes away from the exercise in a more pessimistic mood than that which inspired the author to guide us through the ever-expanding thicket of intellectual property regimes in the first place. To my mind, the European Commission has taken the Union down a dangerously protectionist road that threatens to balkanise the upstream flow of knowledge, data, and information in ways that will hamstring rather than promote the work of basic science, which is the real source of wealth in the knowledge economy.[3] While the pro-competitive conditions of an integrating European marketplace are everywhere to be felt in the old economy based on tangible assets, the overly protectionist intellectual property rules that routinely emanate from Brussels cast a shadow over the long-term prospects for dynamic growth in a large part of the developed world. If any single group of policymakers needs to read and meditate on Ghidini's pro-competitive message, it is surely those intellectual property authorities at the European Commission for whom 'protection' has become a mantra and 'competition' something of a dirty word in recent years.

In reality, studies show that the most dynamic conditions of innovation and creativity have lately emerged from areas of relatively weak intellectual property protection, in which ideas and talents flow freely from one firm to another with enormous spillover effects that stimulate the cumulative and sequential contributions of the relevant technical communities as a whole. I refer, of course, to the Silicon Valleys and Research Triangles of California,

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[3] See, e.g., JEROME H. REICHMAN, *La guerra delle banche dati – Riflessioni sulla situazione americana*, 6 *AIDA* 226–36 (1997); J.H. REICHMAN and PAMELA SAMUELSON, *Intellectual Property Rights in Data?*, 50 *Vanderbilt L. Rev.* 51 (1997); J.H. REICHMAN, *Database Protection in a Global Economy*, Revue Internationale de Droit Economique, 455–504 (2002).

Massachussets, and North Carolina, and to the innumerable research parks that have sprung up elsewhere in which innovation and competition remain the driving force. The innovative capacity of these communities is threatened, not enhanced, by the proliferating mixture of special-interest intellectual property rights[4] that increasingly impede the flow of scientific and technical information upstream and that slow the pace of follow-on applications of know-how to industry later on.

As for Italy, no other country in Europe has so much benefited from a Silicon-Valley-like mentality in the post-war period. The design industries of the Veneto region in particular serve as a model that developing countries could profitably emulate. These industries arose in a pro-competitive environment that was unencumbered by overly protectionist design laws like those that governed the French design industries during the same period. Will a new cumulative regime of copyright protection make Italy's design industries more productive than in the past? My guess is that it will hold them back in subtle ways, by generating lost opportunity costs that are hard to document but certain to result whenever strong exclusive property rights are used to regulate small-scale applications of know-how to industry.

To my mind, a proliferation of unbalanced intellectual property rights has increasingly become a cancerous growth on the free-market economies of the developed world, which leaves those same economies ever more vulnerable to developing countries that are able to adopt a more pro-competitive approach to implementing international minimum standards of intellectual property protection.[5] At the same time, promising new forms of industrial production are being experimented with, such as the Linux open-source operating system, which may help to counteract some of the anti-competitive effects of recent legislative initiatives.[6] It is surely remarkable that IBM, which once spent millions of dollars championing the 'technology copyrights' and software patents whose social costs Ghidini's book (and my own writings) have called

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[4] See, e.g., J.H. REICHMAN, *A Contractually Reconstructed Research Commons for Scientific Data in a Highly Protectionist Intellectual Property Environment*, 66 *Law & Contemporary Problems* 315–462 (2003).

[5] See, e.g., J.H. REICHMAN, *From Free Riders to Fair Followers: Global Competition under the TRIPS Agreement*, 29 *N.Y.U. J. Int'l L. & Policy* 11 (1997); see also MASKUS and REICHMAN, above, note 2; J.H. REICHMAN, *The TRIPS Agreement Comes of Age; Conflict or Cooperation with the Developing Countries?*, 32 *Case Western Reserve J. Int'l L.* 441–70 (2000).

[6] See, e.g., YOCHAI BENKLER, *A Political Economy of the Public Domain: Markets in Information Goods versus the Marketplace of Ideas*, in Rochelle Dreyfuss et al. (eds), *Expanding the Boundaries of Intellectual Property – Innovation Policy for the Knowledge Society* 267–92 (2001).

into question,[7] is now spending millions of dollars promoting open-source platforms and the Linux system instead!

Whether Professor Ghidini's proposed reforms of existing patent and copyright regimes would succeed or not is hard for me to gauge. I personally believe that the greatest need is for a new type of intellectual property regime, based on liability rules rather than exclusive property rights, which would stimulate investment in cumulative and sequential innovation without impeding follow-on applications and without impoverishing the public domain. This new type of regime, which I now call a 'compensatory liability regime', is most fully elaborated in a recent article,[8] which I will not anticipate here. Suffice it to say that, in my view, the existence of a liability rule to protect small-scale applications of know-how to industry would relieve the pressures on the patent and copyright subsystems and allow courts and administrators to let those regimes regain some of their former coherence which, as Ghidini so ably documents, they have lost in recent years.

What I can say with confidence is that Ghidini's attempt to re-examine present-day intellectual property law in the light of the pro-competitive premises underlying a free-market economy provides a timely and enlightening contribution from which every reader interested in this field stands to benefit. I augur that this book will be widely read and appreciated and that, over time, it may help to prepare a new generation of scholars and practitioners who will retain a healthy scepticism about the protectionist virtues of ill-conceived intellectual property rights and a healthy regard for the competitive ethos.

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[7] See, e.g., PAMELA SAMUELSON, RANDALL DAVIS, MITCHELL D. KAPOR and J.H. REICHMAN, *A Manifesto Concerning the Legal Protection of Computer Programs*, 94 *Columbia L. Rev.* 2308–431 (1994).

[8] J.H. REICHMAN, *Of Green Tulips and Legal Kudzu: Repackaging Rights in Subpatentable Innovation*, 53 *Vanderbilt L. Rev.* 1743–98 (2000), abridged version reprinted in ROCHELLE DREYFUSS ET AL. (eds), *Expanding the Boundaries of Intellectual Property – Innovation Policy for the Knowledge Society* 267–92 (2001). See also J.H. REICHMAN, *Legal Hybrids Between the Patent and Copyright Paradigms*, 94 *Columbia L. Rev.* 2432–578 (1994); J.H. REICHMAN, *Charting the Collapse of the Patent-Copyright Dichotomy: Premises for a Restructured International Intellectual Property System*, 13 *Cardozo Arts & Ent. L.J.* 475 (1995).

A nouvelle vague? Author's brief foreword

The need to incorporate the numerous and significant developments in legislation, case law and scholarly opinion at national and international level was an important factor in writing a much expanded edition of this work. However, it was not the primary motivation.

Above all, there was a desire to explore new perspectives on intellectual property and proposals for reform that have come to the fore in the past few years. Interpretative and legislative approaches, even at international level, which Jerome H. Reichman has defined as 'over-protectionist', no longer seem to be as dominant as they traditionally have been. Those earlier approaches, with cultural roots that can be traced back to Joseph Schumpeter, expressed an era and models of industrial development characterised by large capital-intensive investments that seemingly justified the call for strong patents and more generally for intellectual property rights with broad excluding powers. By contrast, today, boosted by the expansion of the knowledge economy, there is a growing worldwide desire to strike a new balance in the paradigms of intellectual property rights in a direction away from the strong and blanket exclusionary models that have traditionally held sway.

This rebalancing is not only advocated for trade with the developing world and especially with the least developed countries but now across the board. It is a way of advancing – through both interpretation and reform of positive law – the interests of individuals and groups other than the protagonists (intellectual property rights (IPR) holders and challengers/competitors) directly involved in the creation of intangible assets. These individuals and groups were previously relegated to the position of having to passively bear the effects of the application of the law. Now these interests are increasingly being recognised as of constitutional rank. They are the new 'stakeholders' whose protection deserves *at least* equal status to that afforded to the holders of intellectual property rights. I am referring to consumers and users of tangible goods, information and culture, as well as researchers and scholars involved in processes of cultural innovation. Furthermore, I am also referring to the interests of the citizens' community as such in the development of innovation and the dissemination of information in a structurally competitive market that does not foster but actually reduces the opportunity for rent-seeking situations.

The heart of this *nouvelle vague*, which is spreading from the academic

world towards important social, economic and even institutional actors, such as the World Intellectual Property Organization (WIPO), is not primarily 'legal', although it aims at reshaping the normative framework. Indeed, the dynamics of economic competition and the innovation of the current industrial revolution (especially in the information technology, biotechnology and nanotechnology sectors) combine – in synergy with the speed of communication processes – to demand and foster new patterns of production and distribution. The progressive erosion of profit margins caused by the intensification of the competitive dialectic, by broader and more stringent business regulation, the ever increasing interdependence between technologies, systems and even research and production patterns, the role that 'soft' assumes in the knowledge economy compared to 'hard', are all factors that prefigure the expansion of horizons characterised by network effects and connections, forms of cooperation among competitors ('co-opetition') and even *open innovation* processes. And it seems reasonable to agree with the diffuse forecast that even the present global economic crisis will push towards more cooperation and interdependence, hence accelerating and strengthening those new dynamics.

These, then, promise to be the new research, production and distribution horizons of the fruits of human ingenuity and creativity, in connection with which processes of development and the circulation of the 'new' are no longer fostered but actually hindered by the traditional *all-exclusionary* effect of intellectual property rights in various industries marked by modern innovation. And the more so the further the technological frontier moves forward. To take just one example: software standards that are required for the direct dissemination and exchange of data via the Internet are – were born: functionally – more open than those designed for the personal computer.

This, therefore, is the greatest novelty, which in order to be grasped by the jurist in a timely way requires *inter alia* that the usual sources of documentation be supplemented by the 'live' expressions of economic and technical information, in line with an approach that from Levin Goldschmidt onwards has been kept alive by many a master of commercial law.

Of course, what I am describing is too recent a development (still clouded by uncertainty and contradictions, as well as the focus of harsh criticism) to predict that it will gain hegemony. History teaches that the emergence of new legal models corresponding to new phases of technological and economic development does not supplant previous models if the conditions that gave rise to those earlier models continue to exist in other areas of economic activity. However, the ongoing expansion of those new horizons is no longer an expression of wishful thinking by isolated academics, and it reinforces the tendency to read the rules through the lens of a more pronounced opening up to values/principles of free competition and the widespread dissemination of culture and information and the promotion of research and creativity. These

principles were those that founded and still underpin – resisting many attempts to chip away at them – the intellectual property system fashioned by the revolutions at the end of the 18th century. This system views exclusive rights as an exception compared to the fundamental freedom to know and do: in short, like *islands in a sea of freedom.*

The foregoing thoughts, together with more in-depth analysis of some issues and welcome comments and criticism) within the framework of a method that gives more weight to systemic consistence than to the (never decisive) 'will of the legislator'. Altogether arguments enunciated in *Intellectual Property and Competition Law* (and elsewhere), offer suggestions for legislative reform as well as new interpretative proposals, for example regarding the impact of the TRIPs Agreement on North/South trading relations, compulsory and voluntary licences for patents, protection of secrets, shape marks, de facto trademarks, cumulation between patent and copyright protection, technological protection measures for data and works that are disseminated electronically, the scope of freedom to access and share copyrighted works, the relationship between the protection of exclusivity and competition rules (antitrust and unfair competition), and so on.

The suggestions which are offered to the reader aim, in the final analysis, to contrast that widespread interpretive inversion and associated social perception of intellectual property portraying exclusive rights as ends in themselves rather than as a means to promote 'the progress of science and useful arts', thereby expanding the size of the above-mentioned islands to the point where the surrounding sea becomes an interstitial channel.

I believe that it is possible as well as right to combat that approach also on the plane of positive law. What is required is that the jurist uses as her/his compass loyalty to the principles that embody the spirit of modern democratic legal systems: which is the spirit of freedom.

G.G.

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