

The Bridges of “IP County”: Bringing Creative Works to Market

**GMU – Center for the Protection of IP,
7th Annual Conf. Oct. 4, 2019**

**Prof. Robert Merges
UC Berkeley**

- **“From the lab or studio, to extensive development, to branding and distribution, intellectual property empowers the inventors, artists, manufacturers, retailers, and marketing professionals who contribute to flourishing economies.”**

Main Themes

- **Bridges along the “IP Value Chain”**
 - From idea to finished product
- **How does IP law affect the locus of creative work?**
 - Contracting and organizational forms

Compensation for Creators

- **Not a simple incentive story**
- **Depends in part on where creative people fit in the organizational pattern/contracting chain**
 - **Employee creators**
 - **Small teams**
 - **Independent contractor creators**



First generation theories

- **“Recoupment” or “Appropriability” was the key**
- **Implicit sequence: (1) Up-front investment; (2) Revenue earned**

Profiting from technological innovation: Implications for integration, collaboration, licensing and public policy

Research Policy 15 (1986) 285-305

David J. TEECE *

School of Business Administration, University of California, Berkeley, CA 94720, U.S.A.

3. 1. Regimes of appropriability

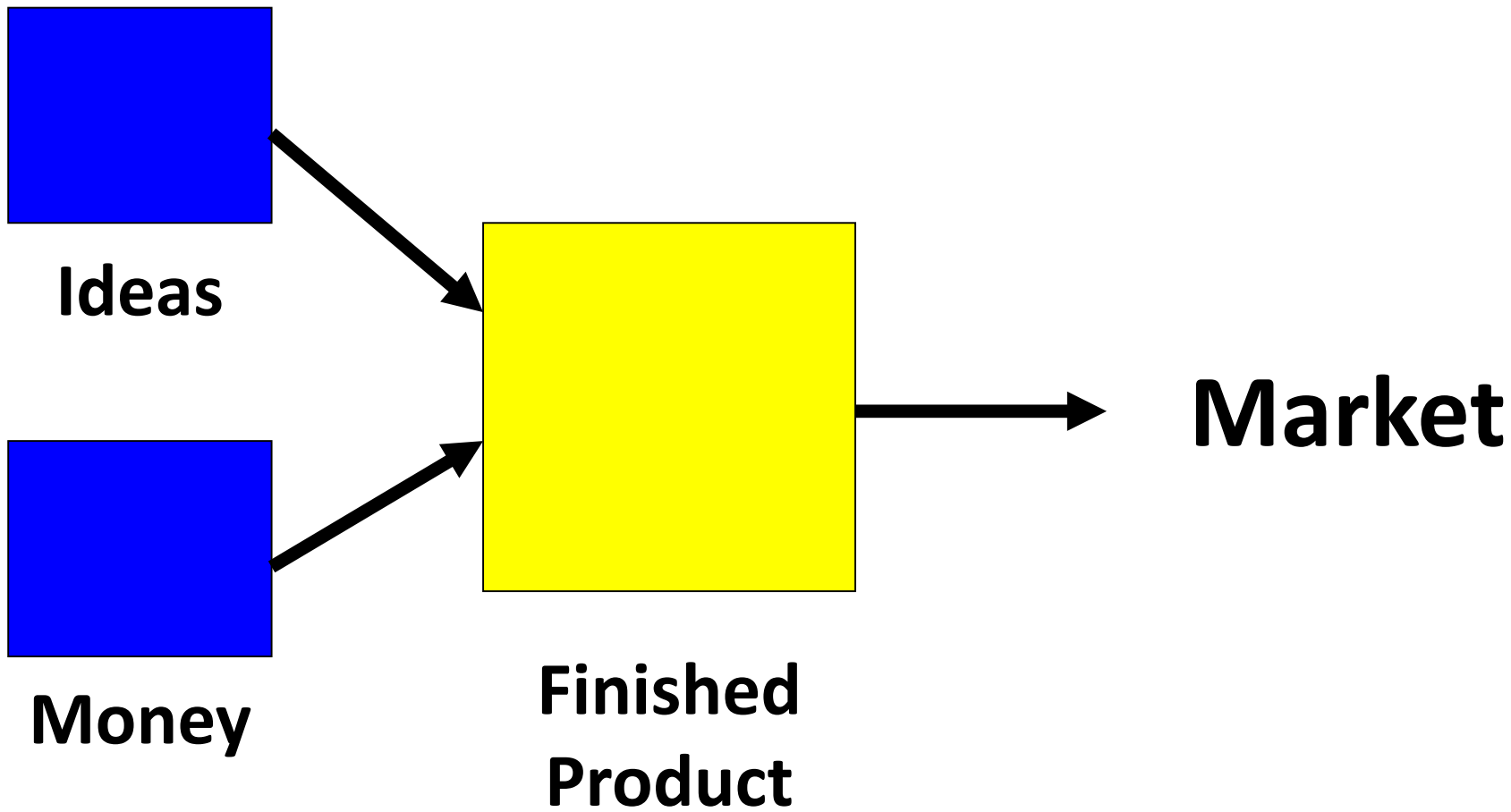
A regime of appropriability refers to the environmental factors, excluding firm and market structure, that govern an innovator's ability to capture the profits generated by an innovation.

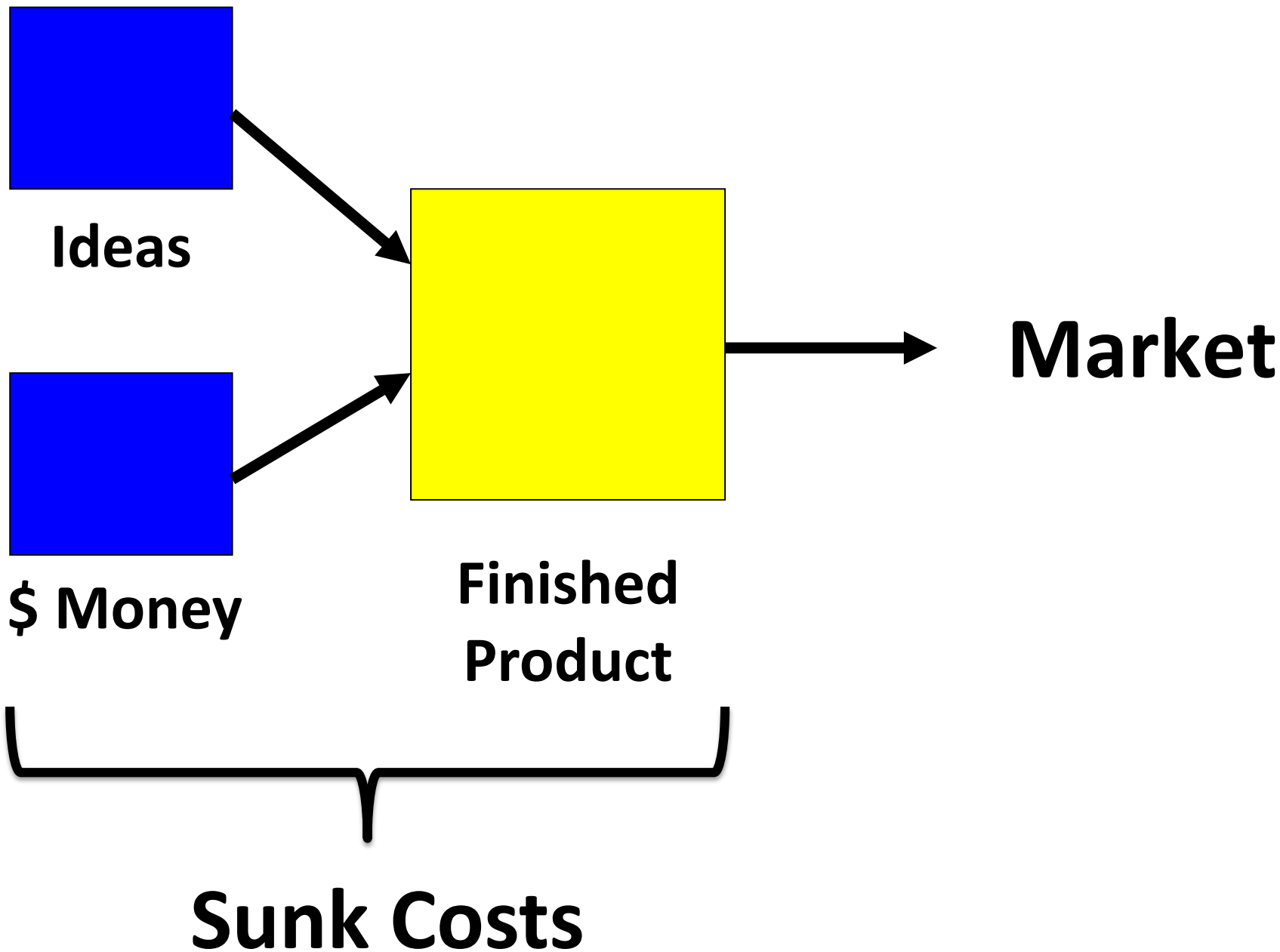
APPROPRIATING THE RETURNS FROM INDUSTRIAL R & D

by

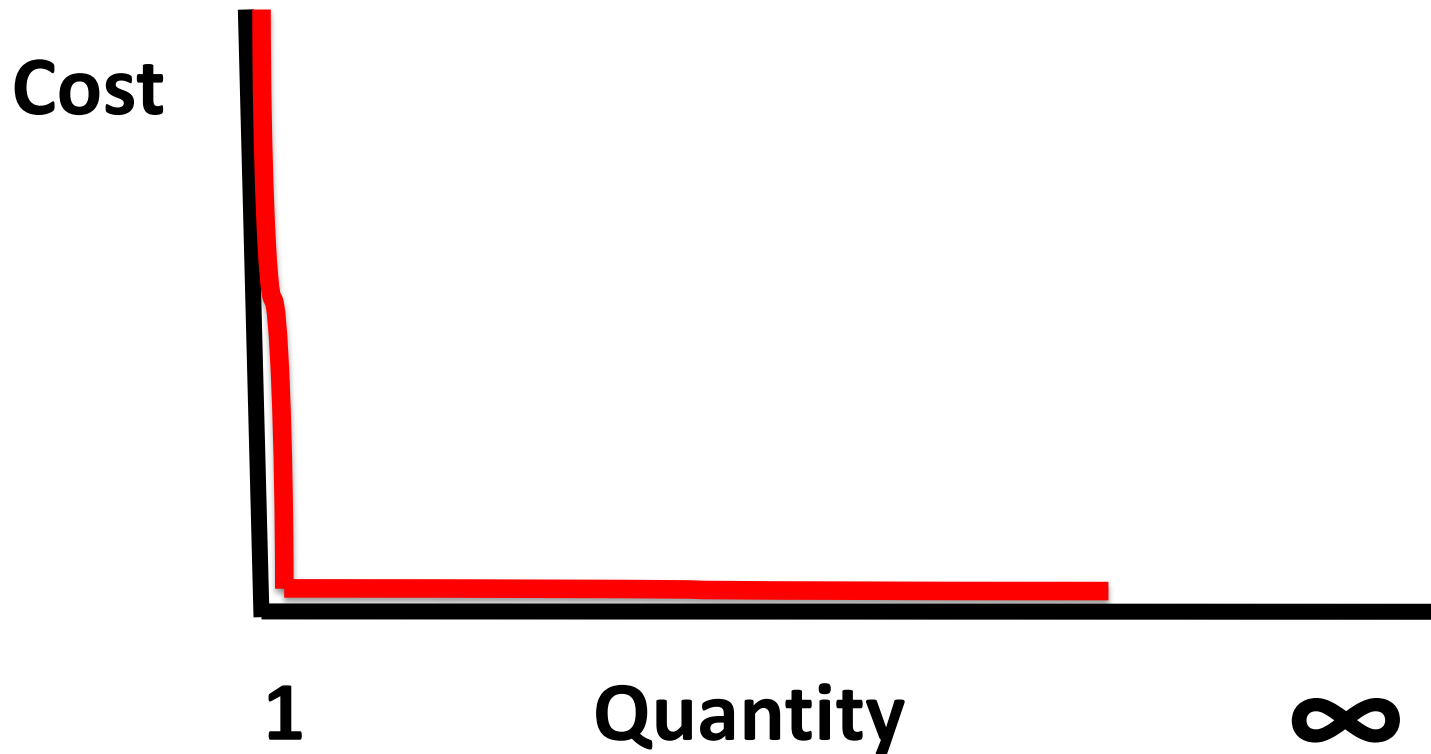
Richard C. Levin
Alvin K. Klevorick
Richard R. Nelson
Sidney G. Winter

February 1988

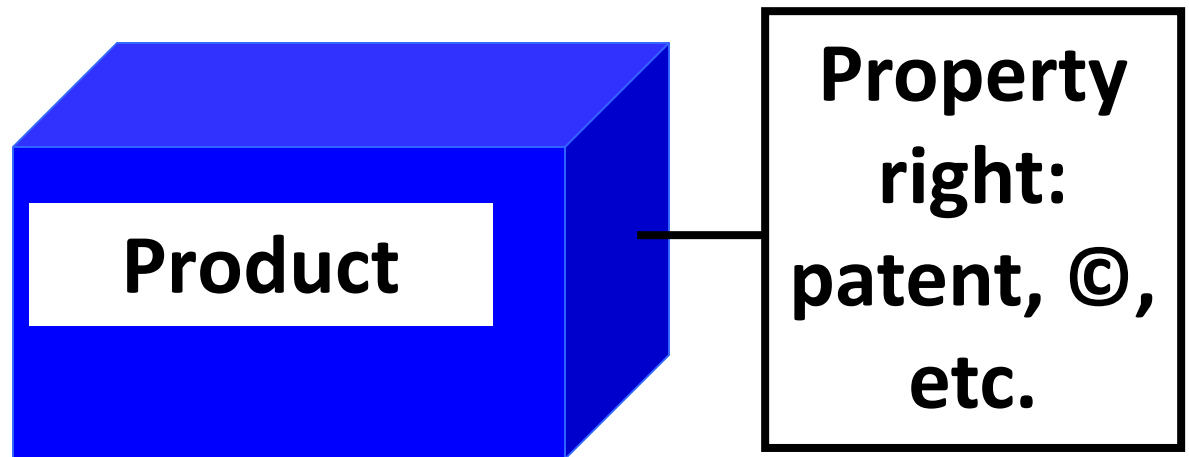




The “L-Shaped” Marginal Cost Curve

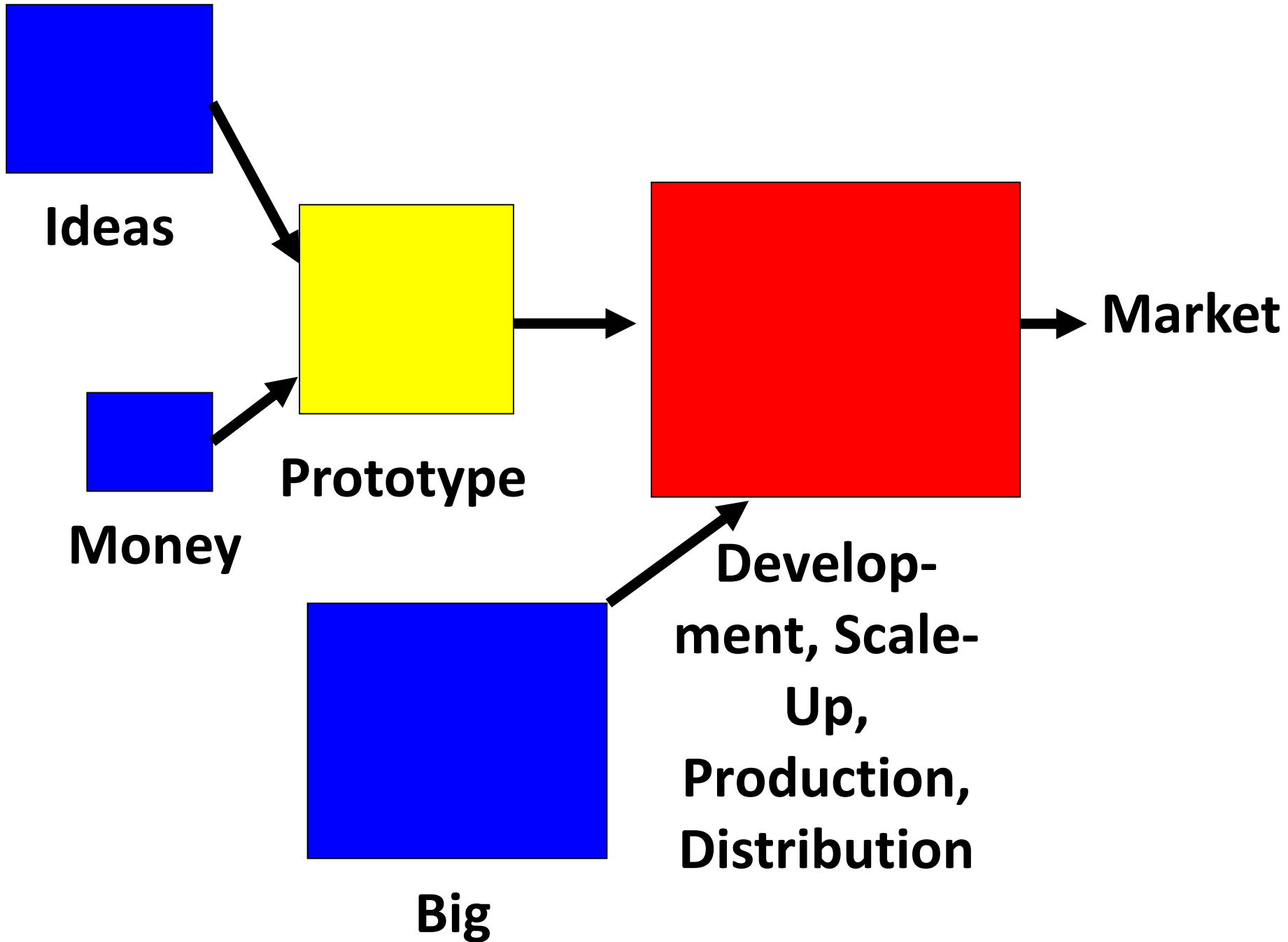


Model 1: Seller has a property right in the product that is traded



Model 2 Adds Complexity

- **Components, not products**
- **Value chain/dis-integrated production**
- **Distribution is often of crucial importance**



\$\$\$ →

**Development,
Scale Up,
Production,
Distribution**

**Property rights:
patents, TMs,
©, etc.**

Model 1 vs. Model 2: Key Differences

- Model 2: Investments in development, scale-up, distribution, branding, etc. are added to basic incentive story of Model 1
- Leads to a focus on patent portfolios, rather than the older (and simplistic) 1 patent, 1 product, market monopoly model

IP and Capital Formation

- **A new focus in the literature on the economics of IP rights**
- **Joan Farré-Mensa, Deepak Hegde and Alexander Ljungqvist, “What is a patent worth? Evidence from the U.S. patent ‘lottery’”, Journal of Finance, forthcoming 2019**

Farre-Mensa et al.

- Using unique data on all first-time applications filed at the U.S. Patent Office since 2001, we find that startups that win the patent “lottery” by drawing lenient examiners have, on average, 55% higher employment growth and 80% higher sales growth five years later. Patent winners also pursue more, and higher quality, follow-on innovation. Winning a first patent boosts a startup’s subsequent growth and innovation by facilitating access to funding from VCs, banks, and public investors.

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PATENTS AS SIGNALS FOR STARTUP FINANCING*

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Germany and France

Haeussler, Carolin and Harhoff, Dietmar and Mueller, Elisabeth, To Be Financed or Not... - The Role of Patents for Venture Capital-Financing (2012). ZEW - Centre for European Economic Research Discussion Paper No. 09-003. Available at SSRN: <https://ssrn.com/abstract=1393725> or <http://dx.doi.org/10.2139/ssrn.1393725>



- ***High Technology Entrepreneurs and the Patent System: Results of the 2008 Berkeley Patent Survey***
- **Stuart J.H. Graham, Robert P. Merges, et al., 24 Berkeley Tech. L.J. 1256 (2010).**

Empirical findings

- **1332 startups (1998-2008), primarily in software and biotech industries**
- **Average firm holds 4.7 patents and applications, with the average venture-backed firm holding 18.7 patents and applications**

Patents important for startup financing

- **67% of broadest group of survey respondents said patents were important to at least one financial investor in the startup**
- **73% of venture capital-backed startups said this**

Implications for Law/Policy

- **Pay attention to role of IP rights in transactions (contracting) and the unique place of creative professionals in industry “ecosystems”**
- **Role of finance and distribution are highlighted**

Why help “creative professionals”?

- Much of the literature in IP law emphasizes the rights of users, consumers, “the public domain,” etc.
- But a few of us believe in *the traditional account of IP law as especially concerned with the “care and feeding” of creatives*

ROBERT P. MERGES

JUSTIFYING INTELLECTUAL PROPERTY



知財法の正当化根拠は何か、
果たして人類に裨益しているのか？
本書はそのような根本問題を問う
世界的名著である。



商務印書館
The Commercial Press

JUSTIFYING INTELLECTUAL PROPERTY

ROBERT P. MERGES

HARVARD UNIVERSITY PRESS
Cambridge, Massachusetts
London, England

2011

Justifying IP

- **Chapter 7: Creative Professionals, Corporate Ownership, and Transaction Costs**
- **Teams and group production**
- **Large companies in the creative ecosystem of various industries**

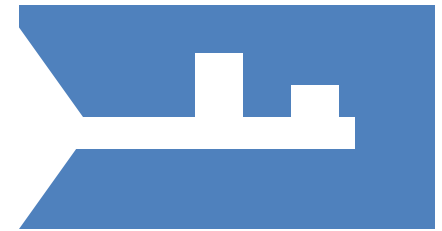
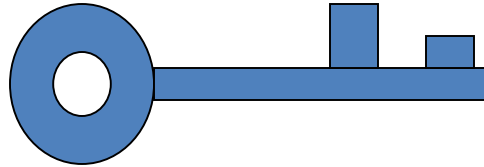
Component production: specialized teams

- Do they need to be integrated into a larger group – high transaction costs if they are independent company?
- Or are the transaction costs manageable enough for them to be an independent company? [Slight policy preference for this?]

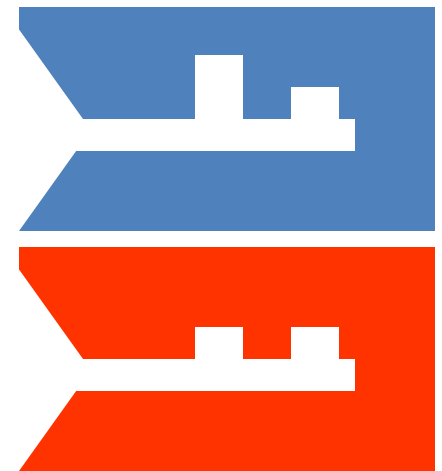
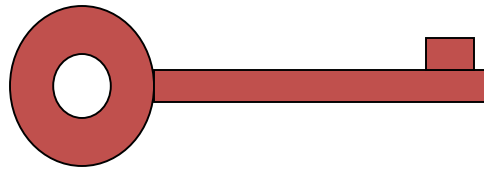
Seller

Buyer(s)

**Uniquely
adapted
input**

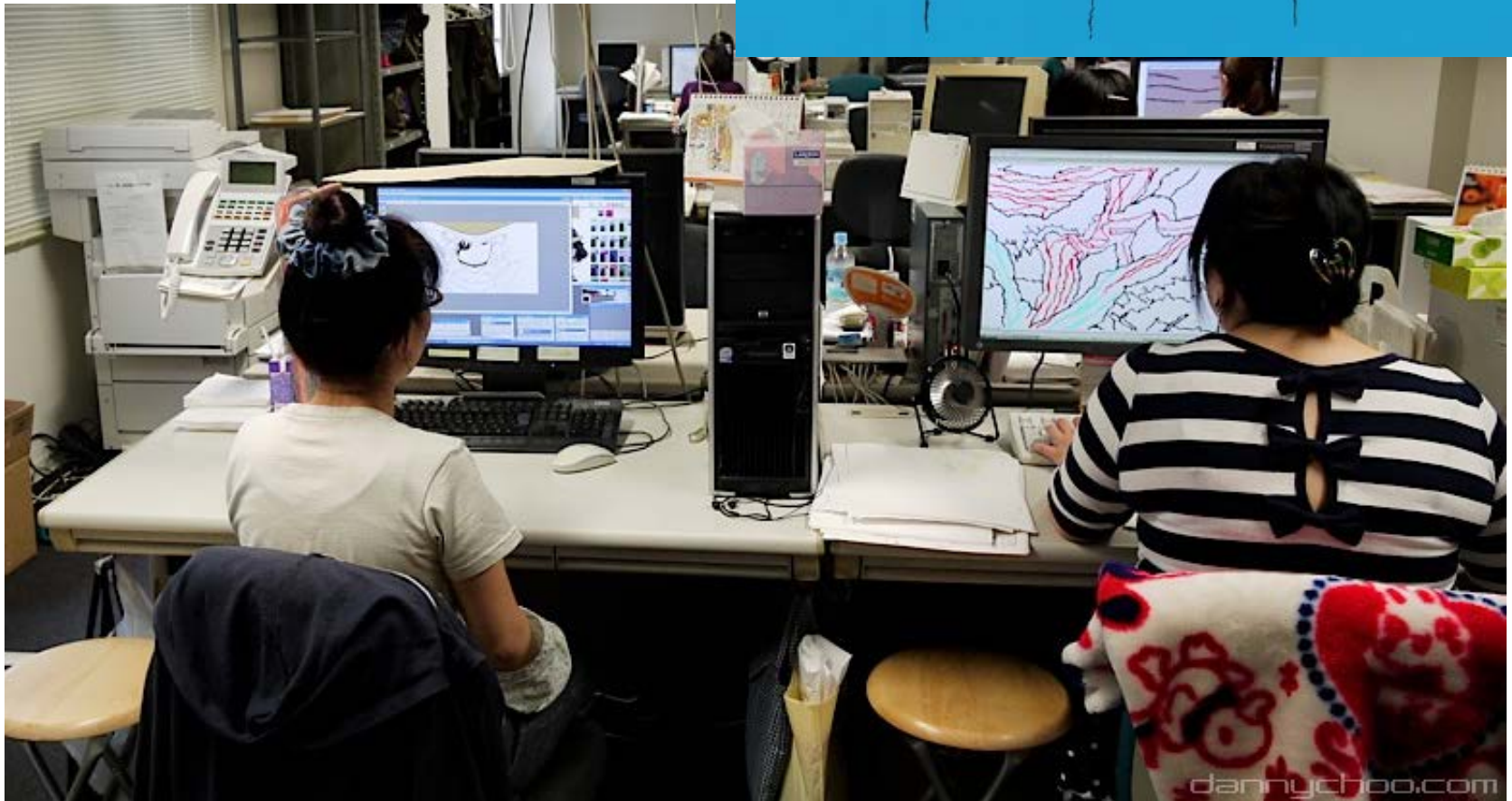


**Modular
design:
more
generic
input**



Comparing Two Creative Tasks in the Film Ecosystem

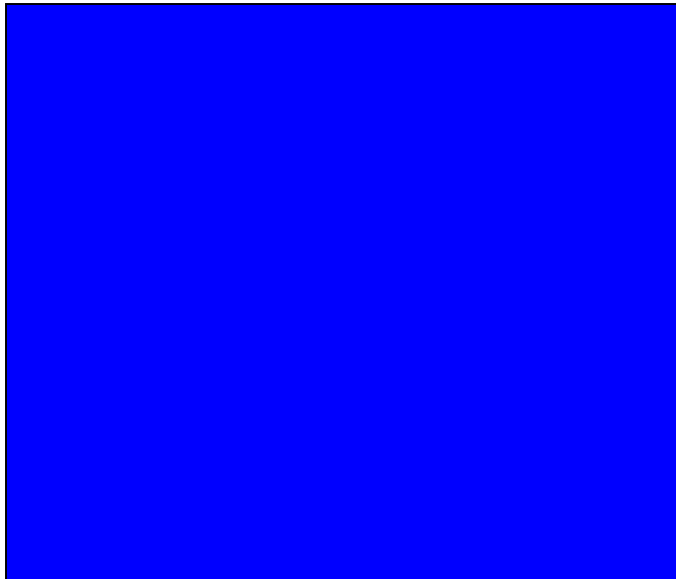
- **Large scale animation (Disney, Studio Ghibli etc.)**
- **Title sequence studios**



Nickelodean Animation Team



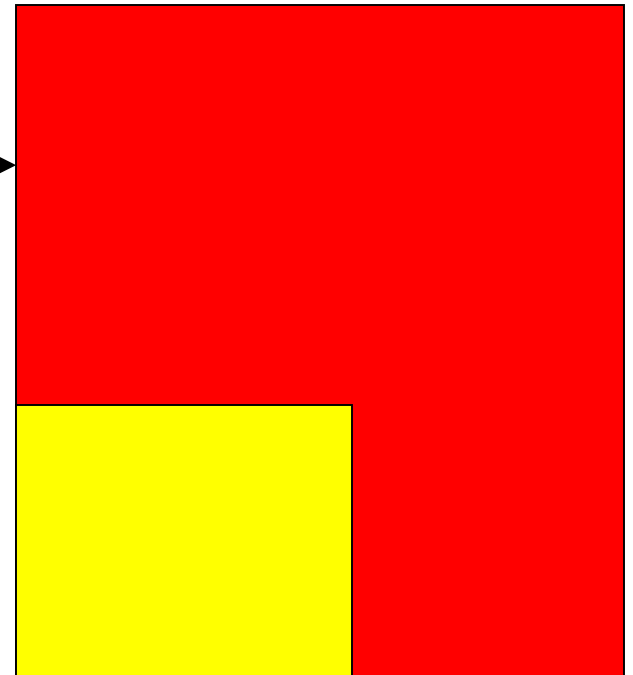
Firm A



Contract



Firm B



Division

Title Design Studios

Art OF THE TITLE

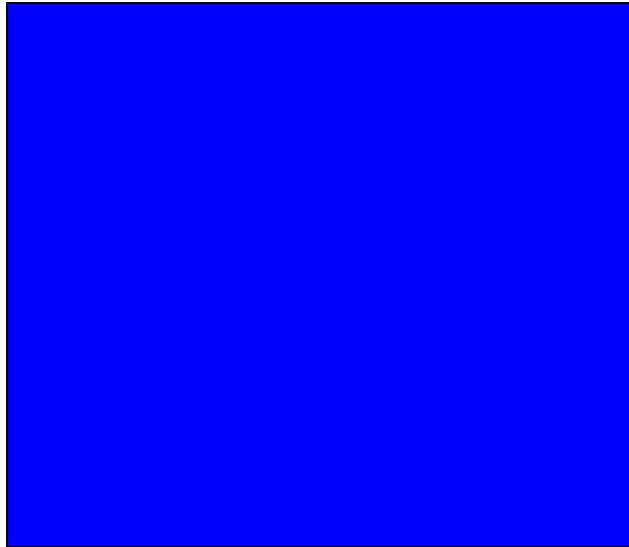




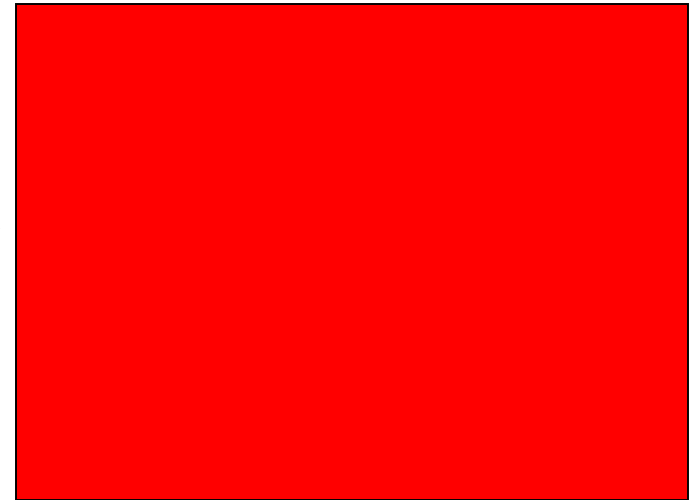
- **Imaginary Forces is a creative company specializing in visual storytelling and brand strategy. We make design-driven content for a wide range of partners and projects.**



Firm A



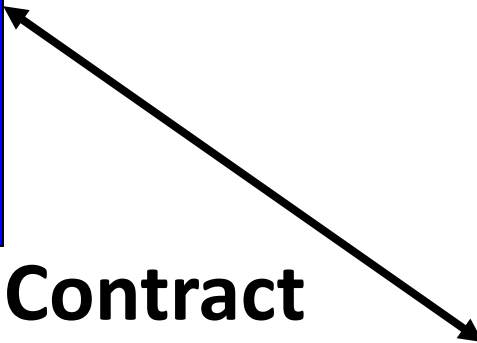
Firm B



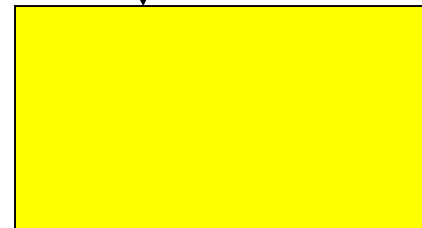
Contract



Contract



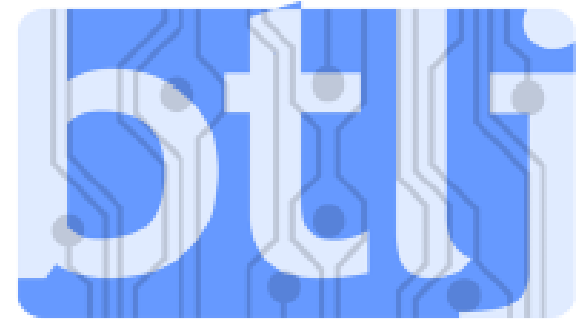
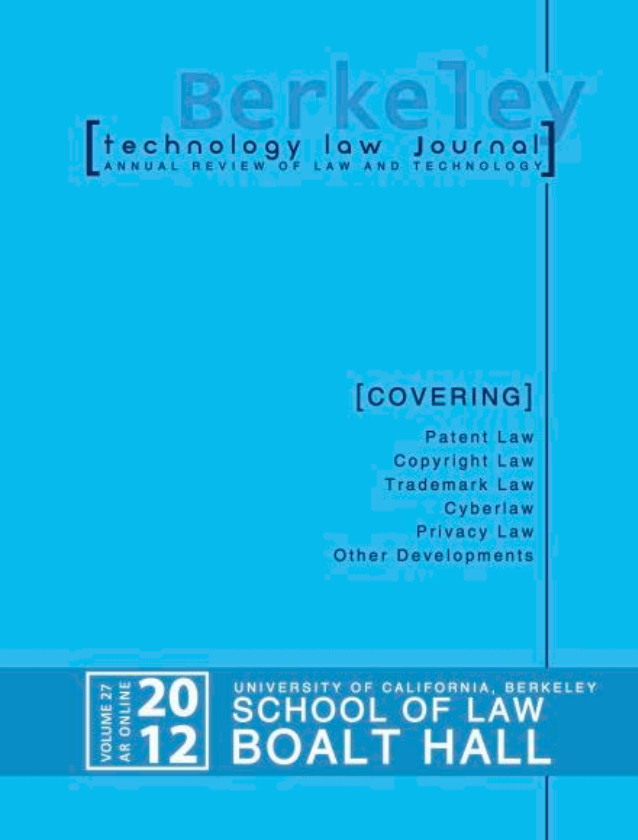
Contract



[New] Firm C

Two special problems

- **Failed product companies, patent litigation, and patent trolls**
- **Technology platforms and creative professionals: market power in online platform industries**



2019–2020

Patent Markets and Innovation in the Era of Big Platform Companies

Robert P. Merges

Platform Companies and Innovation

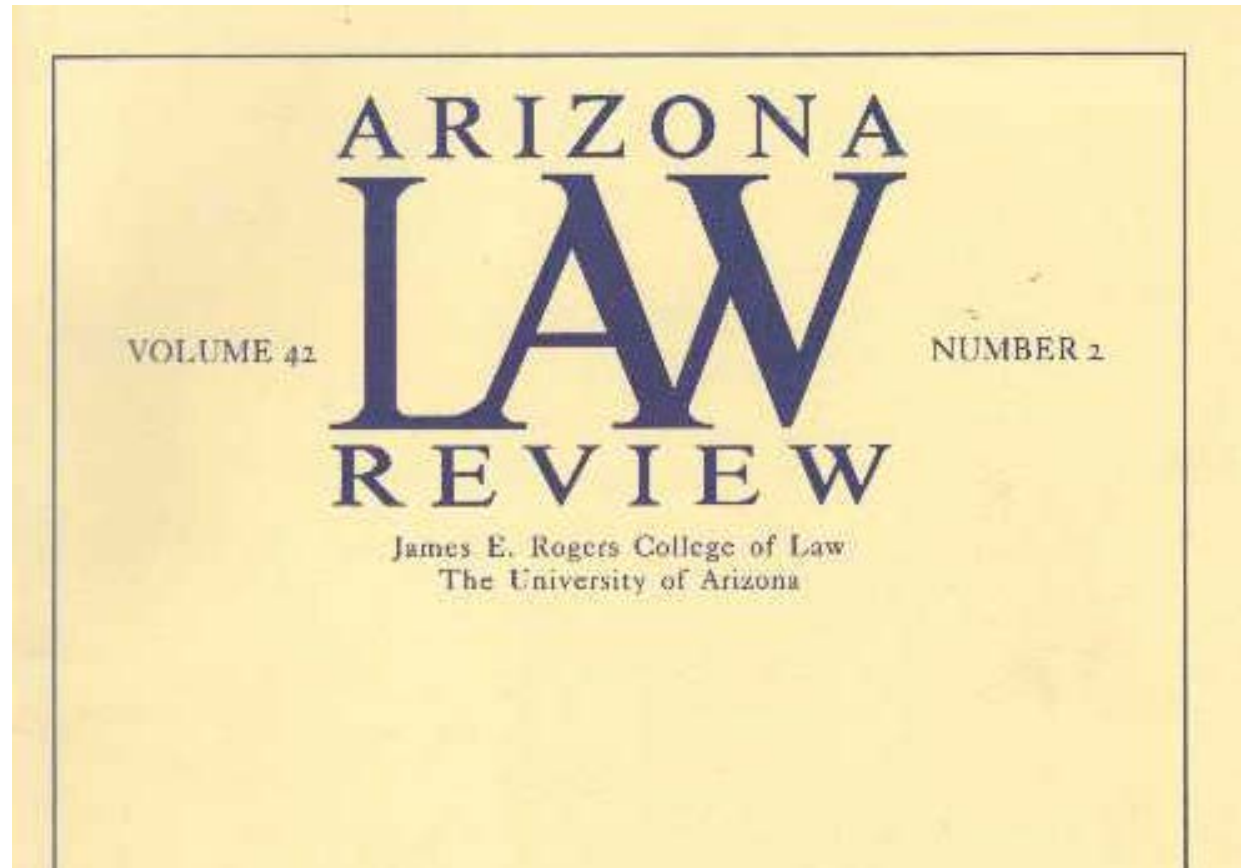
- **Big platform companies often invest in in-house R&D departments**
 - Google
 - Amazon: A9 Labs
- **They also acquire many smaller, innovative companies – “exit by acquisition” and “acqui-hiring”**

- **Peter Lee, Innovation and the Firm: A New Synthesis, 70 Stan. L. Rev. 1431 (2018).**
- **Rediscovering the benefits of integration in the platform era**
- **Lower transaction costs (esp. regarding “tacit knowledge”)**

Adjusting policies to (slightly?) favor independent teams

- **Benefits of multiple, rivalrous sources of new ideas/R&D**
- **Autonomy of small teams as an independent value?**

- **Merges, Autonomy and Independence: The Normative Face of Transaction Costs, 53 Ariz. L. Rev 145 (2011)**



Patents → Technologies → Products → Product Markets

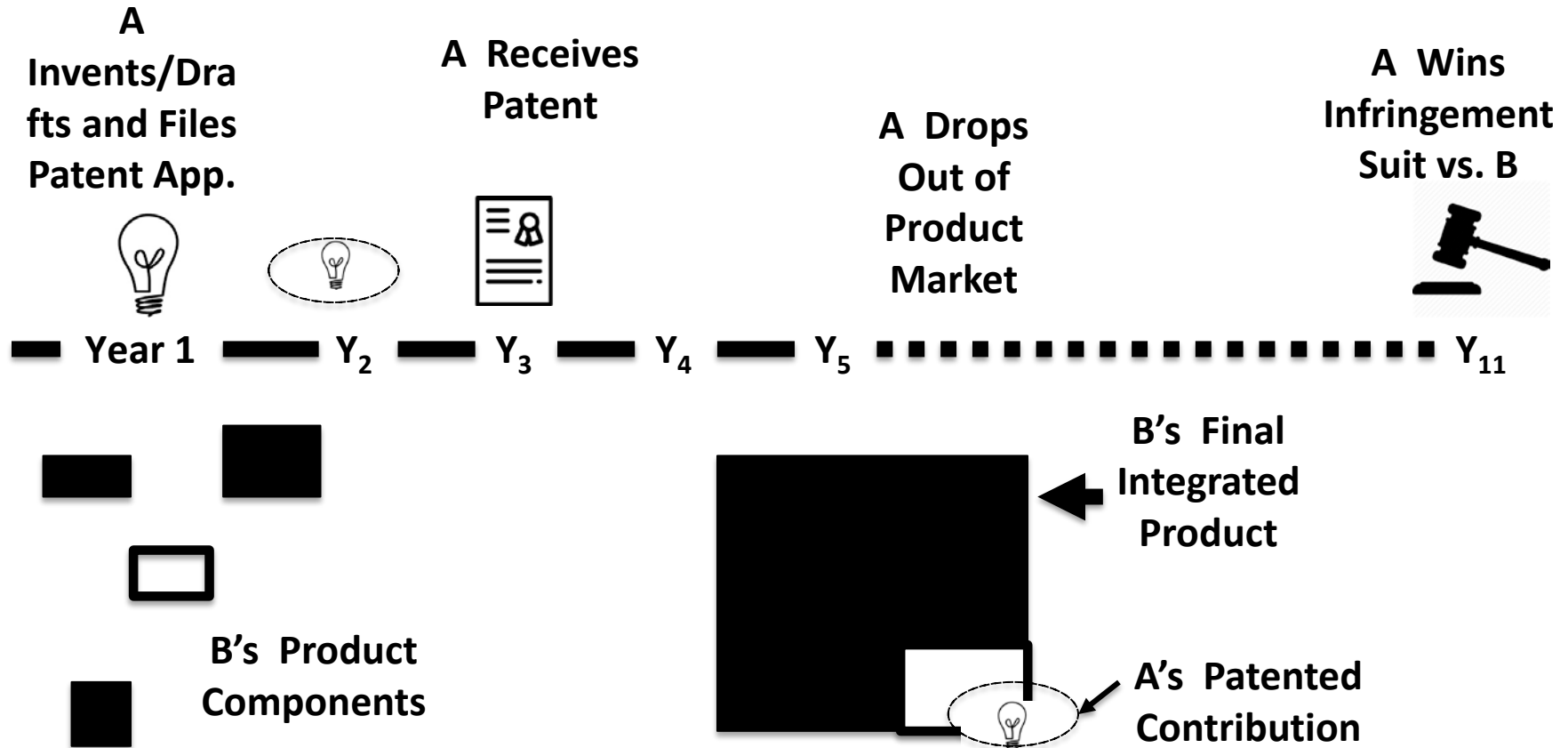


Figure 1: Mapping Patents into Product Markets

Patent markets

- **Idea factories, failed startups, “orphan technologies” and corporate spinoffs**
- **Can they help maintain more rivalrous sources of innovation in the platform era?**

A's Invention/Patent Timeline



B's Product Development Timeline

What about markets for creative expression (copyrighted works)?

- Signs of Hope

- US: **Music Modernization Act**
- New statutory collective rights organization for music composition owners for streaming, downloads, etc.
- Europe: Copyright Directive of 2019

MMA, US

- The Collective shall be governed by a Board of Directors consisting of 14 voting members and 3 non-voting members. 10 voting members represent music publishers; **the other four voting members will be professional songwriters who have retained their exclusive rights.**
- 17 U.S.C. § 115(d)(3)(A)

- MMA: “The act is favorable to musicians and *should increase payments to many Songwriters and Producers.*”
- <https://www.careersinmusic.com/music-modernization-act/>

And then there is pharma . . .

PhRMA Member Company R&D Expenditures 2001-2017 (BILLIONS)



And then there is pharma . . .

From 1997 through 2016, **medical marketing expanded substantially, and spending increased from \$17.7 to \$29.9 billion**, with direct-to-consumer advertising for prescription drugs and health services accounting for the most rapid growth, and pharmaceutical marketing to health professionals accounting for most promotional spending.

- **In re Generic Pharmaceutical Pricing Antitrust Litigation, No. 16-MD-2724, 2019 WL 3842901 (E.D. Pa. Aug. 15, 2019)**
- **Antitrust suit alleging pricing conspiracy survives motion to dismiss**

Senator Warren: Affordable Drug Manufacturing Act

- **Establishes an Office of Drug Manufacturing within HHS charged with lowering prices, increasing competition, and addressing shortages in the market for prescription drugs**
- **Mostly aimed at generic drugs; but Warren website includes this: “We should crack down on rampant abuse of the patent and regulatory system”**

