THE FINANCIAL PAGE
EXPORTING I.P.

Free trade is supposed to be a win-win situation. You sell me your televisions, I sell you my software, and we both prosper. In practice, free-trade agreements are messier than that. Since all industries crave foreign markets to expand into but fear foreign competitors encroaching on their home turf, they lobby their governments to tilt the rules in their favor. Usually, this involves manipulating tariffs and quotas. But, of late, a troubling twist in the game has become more common, as countries use free-trade agreements to rewrite the laws of their trading partners. And the country that is doing this most aggressively is the United States.

Our recent free-trade agreement with South Korea is a good example. Most of the deal is concerned with lowering tariffs, opening markets to competition, and the like, but an important chunk has nothing to do with free trade at all. Instead, it requires South Korea to rewrite its rules on intellectual property, or I.P.—the rules that deal with patents, copyright, and so on. South Korea will now have to adopt the U.S. and E.U. definition of copyright—extending it to seventy years after the death of the author. South Korea will also have to change its rules on patents, and may have to change its national-health-care policy of reimbursing patients only for certain drugs. All these changes will give current patent and copyright holders stronger protection for longer. Recent free-trade agreements with Peru and Colombia insisted on much the same terms. And CAFTA—a free-trade agreement with countries in Central America and the Caribbean—included not just longer copyright and trademark protection but also a dramatic revision in those countries' patent policies.

Why does the U.S. insist on these rules? Quite simply, American drug, software, and media companies are furious about the pirating of their products, and are eager to extend the monopolies that their patents and copyrights confer. These companies are the main advocates for such rules, and the big winners. The losers are often the citizens in developing countries, who find themselves subject to a Draconian I.P. regime that reduces access to new technologies.

Intellectual-property rules are clearly necessary to spur innovation: if every invention could be stolen, or every new drug immediately copied, few people would invest in innovation. But too much protection can strangle competition and can limit what economists call "incremental innovation"— innovations that build, in some way, on others. It also encourages companies to use patents as tools to keep competitors from entering new markets. Finally, it limits consumers' access to valuable new products: without patents, we wouldn't have many new drugs, but patents also drive prices of new drugs too high for many people in developing countries. The trick is to find the right balance, insuring that entrepreneurs and inventors get sufficient rewards while also maximizing the well-being of consumers.

History suggests that after a certain point tougher I.P. rules yield diminishing returns. Josh Lerner, a professor at Harvard Business School, looked at a hundred and fifty years of patenting, and found that strengthening patent laws had little effect on the number of innovations within a country. And, in the U.S., stronger patent protections for things like software have had little or no effect on the amount of innovation in the field. The benefits of stronger I.P. protection are even less convincing when it comes to copyright: there's little evidence that writers and artists are made more productive or creative by the prospect of earning profits for seventy years after they die, and the historical record suggests only a tenuous connection between stronger I.P. laws and creative output.

The U.S., in its negotiations, insists on a one-size-fits-all approach: stronger rules are better. But accepting a diverse range of I.P. rules makes more sense, especially in light of the different economic challenges that developing and developed countries face. Lerner's study found that the benefits of stronger patent laws were reduced in less developed countries. And developing countries, being poorer, obviously have more to gain from shorter patent terms for foreign innovations, since that facilitates the spread of new technology and the diffusion of ideas. Tellingly, this is the approach the U.S. takes when it comes to labor standards, arguing that we shouldn't impose developed-country standards on developing countries. But in the case of intellectual property the government's position is exactly the opposite. The only difference, it seems, is whose interests are at stake.

The great irony is that the U.S. economy in its early years was built in large part on a lax attitude toward intellectual-property rights and enforcement. As the historian Doron Ben-Atar shows in his book "Trade Secrets," the Founders believed that a strict attitude toward patents and copyright would limit domestic innovation and make it harder for the U.S. to expand its industrial base. American law did not protect the rights of foreign inventors or writers, and Secretary of the Treasury Alexander Hamilton, in his famous "Report on Manufactures," of 1791, actively advocated the theft of technology and the luring of skilled workers from foreign countries. Among the beneficiaries of this was the American textile industry, which flourished thanks to pirated technology. Free-trade agreements that export our own restrictive I.P. laws may make the world safe for Pfizer, Microsoft, and Disney, but they don't deserve the name free trade.

—*James Surowiecki*

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