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SYMPOSIUM: INTELLECTUAL PROPERTY RIGHTS

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INTELLECTUAL PROPERTY RIGHTS AND THE GATT

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Intellectual property rights allow individuals and companies that invest the time and money in innovation, research and development to reap the rewards of their labor. Indeed, the presence of intellectual property rights is essential for the maintenance of innovative industries. While domestically this issue has great importance, internationally the issue of effective and fair intellectual property rights has gained great momentum over the last decade. Intellectual property is the foundation of international competitiveness. If adequately protected, intellectual property promotes the expansion of international trade, investment and transfers of technology. In addition, a regime that adequately protects intellectual property can help improve and expand the industrial base and standard of living of developing countries as it has done in industrialized countries.

The patent system in use today in the United States has evolved from the one perceived by the framers of the Constitution, which was to be and is today a system of incentives and rewards (Besen and Raskind, p. 8). Yet while the U.S. strives to maintain a rigorous system, other developed nations and (specifically) developing nations either do not have and adequate system or simply do not have the resources to monitor such a regime. The result is ineffective protection of intellectual property against infringements of intellectual property rights, which has led to substantial distortion of trade.

The role of intellectual property rights within foreign trade is discussed by various economists and policy makers. Gerald Mossinghoff writes, "The United States depends on high technology products in its trade relations. These products are the result of intensive research and development and are protected by the patent system" (Mossinghoff, p. 238). Mossinghoff goes on to list eight reasons why patents and trademarks play a vital role in U.S. trade and industry. First, patents provide incentive for innovation. Second, they provide technology and market information through public disclosure. Third, patent statistics reveal trends in trade

competition. Fourth, the U.S. patent system protects domestic markets against foreign copying. Fifth, foreign patent protection helps U.S. firms enter foreign markets. Sixth, intellectual property provides an important source of international license fee income (a 1982, the U.S. made over $7 billion in royalties and licensing fees). Seventh, trademarks provide product recognition in the international marketplace. Lastly, effective patent protection in developing countries is critically important to their economic growth (Mossinghoff, p. 237). I will discuss this last point later. The first seven, however, illustrate the importance of a strong international intellectual property right regime for developed countries.

Unfortunately, this strong regime does not exist. In *Basic Framework of GATT Provisions on Intellectual Property*, the statement of views of the Intellectual Property Committee (USA) and the parallel agencies in Japan and the EC, one passage reads, "Despite efforts taken...the extensive losses to worldwide industry due to inadequate and ineffective national protection of intellectual property continues" (IPC, p.7). Activities that distort international trade, including copying another company's product through similar packaging, trademarks or willful reproduction and unauthorized manufacture, sale and use of another's property are still prevalent. An ITC questionnaire of 193 U.S. firms in 1986 estimated the worldwide loss due to inadequate intellectual property protection at $23.8 billion, or 27% of sales affected by intellectual property. The ITC estimates the worldwide losses to all U.S. industry between $43 billion and $61 billion (IPC, p.12). According to the European Parliament, counterfeit foods sold in the EC resulted in the loss of 100,000 jobs, while the U.S. copyright industries put annual loss of sales at over $1.3 billion as the result of failure of certain countries to provide adequate protection to U.S. copyrighted works (IPC, p.13). An excellent example is the semiconductor industry. Semiconductor integrated circuits cost $100 million dollars to develop and produce, but can be copied for under $1 million. Indeed, by the mid 1970's, so much illegal copying and distribution of chips was occurring that in 1978, the industry appealed to Congress, the result being the Semiconductor Act of 1984 (Besen and Raskind, p. 19). Overall, the lack of international protection for intellectual property has hurt industry within developed countries

and threatens the economic welfare of the U.S. and other countries that export high-tech goods. The IPC writes, "Industries are finding it increasingly difficult to achieve an economic return commensurate with the risks when foreign infringers, who do not face similar development costs, effectively displace legitimately produced goods and works from international markets" (IPC, p. 14).

Countries with inadequate and ineffective intellectual property protection are also injured by extensive infringement. First, financial losses by foreign property rights owner from such activities make it difficult for them to generate new capital that could be invested in the economic development of those countries. Second, displacement of legitimately produced goods reduces the willingness of industry to commit long-term planning to develop new goods and services for those countries. Finally, without intellectual property protection, the technically advanced work force either leaves the country or changes the focus of its activities from innovation to copying and imitation (IPC, p. 14). Carlos Braga agrees with this sentient, stating "Economic growth in turn depends on providing incentives to those nations, incentives that realistically can only be achieved by rewarding creativity and innovation" (Braga, p. 264).

International agreements on intellectual property rights, such as the Berne Convention for the Protection of Literary and Artistic Works, the Universal Copyright Convention and the Paris Convention for patent and trademarks have addressed the problem of inadequate international intellectual property protection, but have not stopped the losses. This is due to the fact that many conventions call for equal national treatment for foreign and domestic goods, but do nothing to raise the intellectual property rights standards in some countries. Further, these agreements do not provide bilateral or multilateral dispute settlement provisions to ensure compliance (IPC, p.15). In light of the present situation, the Uruguay Round of GATT negotiations includes a working group on intellectual property.

According to the IPC, "The principle focus of the GATT negations should be the reduction and eventual elimination of trade distortions due to the absence of a multilateral settlement mechanism for intellectual property disputes" (IPC, p.11). The GATT should focus on a)

effective and non-discriminatory enforcement mechanisms, including those at the border, to create a deterrent to mechanisms, including those at the border, to create a deterrent to trade in illegal goods, b) dispute settlement procedures to ensure that the domestic laws of the signatories effectively and adequately embody the GATT fundamental principles of intellectual property rights and c), preferential treatment to confer benefits on signatories and to encourage adherence to the new GATT regime (IPC, p. 9).

The approach favored by the IPC and the parallel agencies in Japan and the EC is the creation of a code, called the GATT IPP. The code would require all signatories to create adequate and effective trade and intellectual property laws for use by private rights holders, and to use multilateral consultation and dispute settlement procedures when other signatories fail to meet their obligation to provide adequate and effective protection (IPC, p.8). Determining whether or not a country has adequate intellectual property laws will depend on the GATT fundamental principles of intellectual property protection, defined as "those adequate minimum standards of intellectual property protection contained in the relevant laws of those countries which engage in most of the trade in goods embodying intellectual property..." (IPC, p. 24). These fundamental principles will be used to determine whether a country's intellectual property protection laws need changing, and will also serve as a reference in dispute settlement procedures. Since countries solely need to achieve a specific minimum, harmonization of national intellectual property protection laws is unnecessary.

The elements of the GATT IPP can be broken down into three parts. First, the owner of the intellectual property must monitor international markets to detect infringement. If the owner finds any kind of impropriety, then stage two comes into effect, where the owner uses the intellectual property laws and procedures, including border controls, established by governments pursuant to the GATT IPP. Finally, if a signatory country fails to carry out its obligations and the owner is denied justice by the judicial system within the offending country, then the owner can request its government to use the consultation and dispute settlement mechanisms included in the GATT IPP (IPC, p. 19). The GATT dispute settlement procedure could include the use of

panels of experts and could allow for retaliatory action sanctioned by GATT. The IPC states, "This procedure would subject member countries to multilateral scrutiny, enhance international cooperation and reduce the use of...bilateral and unilateral actions which might become barriers to legitimate trade" (IPC, p. 23). Indeed, the GATT IPP would enhance the various enforcement a reality.

There are various incentives for countries to join the GATT IPP. For developed countries, it offers multilateral discipline and international cooperation. For developing countries, special treatment, including delayed entry, transition period, preferential treatment as a signatory and pledges by developed nations to increase technical assistance, along with incentives outside the GATT structure, can make joining very attractive. One article states, "Transition rules for individual nations should be encouraged, and incentives created to spur developing nations to graduate to GATT norms and standards" (Dastenmier and Beirer, p. 306).

Various problems arise when dealing with this issue that have clouded the GATT negotiations. The extent of intellectual property protection is a contentious issue, especially between developed and developing countries, but also between different developed nations. In addition, many developing nations believe that the GATT is not the appropriate forum for discussion of intellectual property rights, and support the existing international agreements (Braga, p. 249). However, the incredible losses to both developed and developing nations due to inadequate and ineffective international intellectual property rights laws makes it essential that something be done. At the present time, the GATT is the only institution with the scope and enforcement ability to create a viable intellectual property rights code.

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TRADEMARKS AND GENERIC NAMES

BY TODD SCHULMAN

I hope to explain economic issues relating to trademarks and generic names. First, I will discuss some economic benefits and costs of trademarks in general. Next, I will explain how genericness is determined. Finally, I will note the economic aspects of choosing a trademarked name.

INTRODUCTION

A trademark is a word, symbol or other signifier which denotes a difference between one good or service and its competition (Landes 268). Suppose that you wanted to buy decaffeinated coffee at the grocery store. If you have had Sanka-brand decaffeinated coffee before and were happy with this product, you could choose it again based on your positive past experience with the trademark of the product. In this manner, your search cost has been lessened. Moreover, as Landes and Posner have noted (269), a trademark allows for "an economy of words." It would be difficult to order "the decaffeinated coffee made by General Foods;" instead, in a restaurant, you may simply ask for the Sanka-brand coffee. Uniqueness makes a trademark effective.

BENEFITS

Our market is not an ideal market with perfect information. As consumers for decaffeinated coffee, we may not have knowledge about the costs and qualities of decaffeinated coffees at other outlets for comparison with a trademarked decaffeinated coffee. As the costs involved in the search for this knowledge become greater, substitutes are less likely to be tried. A lack of perceivable substitutes is advantageous to the seller of the product with the well-known trademark.

A trademark provides a quick way of associating a product with a past experience and

reduces the need for search. Additionally, a trademark will also help to ensure continuous quality of the trademarked good: the company possessing the trademark has a standard of quality up to which it must live. If the company's quality level deviated from this standard, consumers would not be able to consistently equate past experiences with the product. Moreover, the investment that the company has spent on the promotional campaign of the trademark would not be realized. A trademark which is applied to a consistently well-made product can benefit the consumer by lowering the search cost.

Trademarks can also create greater profits for the companies which they represent. Trademarks are based on reputations which are heavily dependent upon past experiences and advertising. Creating a positive image for a trademark has achieved a favorable reputation, a company can earn greater profits because consumers will be willing to pay more in return for lower search costs and an assurance of quality. This is not an unnecessary expenditure for the rational consumer because the search cost foregone would have exceeded the additional amount paid by the consumer.

COSTS

Although effective trademarks may offer assurances of quality and may lower search costs, they may also create monopoly rents and dead weight losses. The trademark may prevent consumers from finding comparable products sold at lower prices and may therefore result in unnecessary expenditures. Furthermore, one firm's campaign to promote itself may cancel out that of another firm. Expenditure for these campaigns force consumers to pay extra for unproductive competition (Landes p. 274). Additionally, there is an incentive for companies to try to "free-ride" by assimilating their image into the image of the company with the successful trademark.. Such action, however, is illegal because it raises the costs of search by creating confusion.

GENERICNESS

If a trademark is perceived to represent the whole category of products and no longer just a specified product, then it is declared a generic name and loses its trademark value. The generic name can then be used by all companies. In other words, "trademarked words become generic when their primary significance in the minds of potential buyers is the identification of a product category rather than a product's brand name" (Folsom p. 1328). Moreover, if there is no other name to describe the product of a company entering into a market dominated by a trademarked name, then the dominant trademarked name would be canceled.

When a name is generic, it is cheaper for competing firms to let the public know about their product and barriers to entry are minimal. For example, if "airplane" was trademarked, a competitor would have to describe its product differently. The competitor might call its product an XYZ "heavier than air flying body" as opposed to an XYZ-brand airplane. The genericness of "airplane" makes it cheaper for all firms to name their products and reduces barriers to entry.

Additionally, Formica Corp., a maker of decorative laminates was told by the Patent and Trademark Office that its trademark would be canceled. The rationale of the Office was that "formica" has become so popular that it constituted a barrier to entry to other companies in the laminate industry. The Office claimed that the name had entered the language as the generic name of decorative laminate and was therefore available for use by any manufacturer. Making "formica" a generic word made it cheaper for competing firms to effectively inform the public about their products and reduced the barrier to entry. Elevator, thermos, zipper and cellophane are other examples of trademarked names that have become generic words.

ECONOMICS OF CHOOSING TRADEMARKED NAMES

It seems logical to ask, "why would a company choose a fanciful or descriptive name which is likely to become generic?" Like most issues in economics, there is a tradeoff. First, a firm may choose a name likely to become generic because it feels that through this name it can

convey more information about its product to the consumer. A potentially generic name will also be effective because it will exclude all mention of competing brands. It will therefore raise the search costs for consumers who may try to seek competitors' products. In this manner, the use of a trademarked name which is likely to become generic can create barriers to entry for competitors and can raise the profits of the firm fortunate enough to have come up with this name. Moreover, when a trademarked name is used by the public in reference to the whole category of products and not just that specific company's product, it serves as "free advertising" (Folsom p. 1337). For example, confusion arises when a consumer asks for a box of "Kleenex". It is unclear whether he wants a close substitute of facial tissues or specifically wants "Kleenex" brand.

Moreover, a company may choose a name which is likely to become generic because there is little that a competitor can do about challenging a trademarked word which is perceived as generic. It usually must wait until a ruling is made by the Patent and Trademark Office. When the challenging company extends its resources on a campaign to demonstrate that a word is in fact generic, all other competitors (who are "free-riding") are also benefiting from the possible positive ramifications of this action. Even if the effort fails, the other competitors can now under-sell the challenging company (Folsom 1338). In sum, a company would choose a name that will likely be considered generic in order to raise profits by being more descriptive, by raising search costs and by advertising itself freely. A company may also choose this name to take advantage of the free-rider problem in challenging a perceived generic trademark.

On the other hand, some companies avoid names that may become generic. For example, General Foods stresses the word "brand" in its advertisements (recall from earlier when I referred to Sanka-brand decaffeinated coffee). Although this admits that there are alternatives to buying Sanka-brand decaffeinated coffee, it also prevents the word Sanka from becoming generic and reinforces "decaffeinated coffee" as the generic words. General Foods has chosen to market its product in a conservative manner.

CONCLUSION

When a trademark is perceived as referring to only one company's product, it can be an efficient benefit to society by reducing search costs and can also increase the profits for this company. However, when a trademark approaches genericity, it can create a monopolistic situation and therefore inefficiencies. Declaring genericness helps to eliminate the monopolistic situation. Finally, when a company chooses a trademarked name, it considers these benefits and costs.