

# A Framework for the Promotion and Protection of Intellectual Property Rights in China

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# A Preview

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- ◆ Introduction
- ◆ Seeking a Win-Win Solution
- ◆ Are the Intellectual Property Rights Owners Damaged Economically?
- ◆ The Importance of Investment in Intangible Capital for Intellectual Property Rights
- ◆ The Issue of Copyright Durability
- ◆ Concluding Remarks

# Introduction

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- ◆ The protection and promotion of intellectual property rights should not be viewed as a purely legal enforcement problem.
- ◆ It is also an ethical problem, with roots in long held traditions, customs and conventions, for example, the copying of paintings by older and established artists by aspiring artists (almost always with attribution).
- ◆ But it is above all an economic problem.
- ◆ Is there some way to craft a Pareto-Improving (i.e., win-win), but not necessarily Pareto-Optimal (i.e., globally efficient) solution?
- ◆ In order to enable a win-win solution, one must create opportunities for gains on the part of Chinese participants/players so that they will have the incentive to enforce the conditions necessary for the effective implementation of the solution.

# Price Discrimination and Market Segmentation

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- ◆ One way to design such a win-win solution is to take advantage of the fact that if the owner of the presumably exclusive intellectual property rights is allowed to price discriminate between markets, its profits are actually maximized.
- ◆ For example, in the 1950s and 1960s, there are authorized Asian editions of U.S. textbooks published and sold in India and Japan, at a fraction of the price of the same textbooks in the U.S. The books may be smaller in size, the print size may be smaller, and the paper may not be as good. But they are functionally equivalent. Of course there are also the well known pirated editions produced and sold in Taiwan.
- ◆ One can also apply the concept of authorized editions to the production of drugs.
- ◆ The use of site licensing for software is yet another way to achieve de facto price discrimination.
- ◆ The problem then comes down to how to enforce the market segmentation, as one does not wish to see the same products being sold less expensively in China find their ways back to developed country markets in which the sale price is much higher.

# Keeping the Markets Segmented: New Technologies Come to the Rescue

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- ◆ In order to prevent unauthorized exports of authorized local editions, there are many possibilities. For example, Prof. Joseph E. Stiglitz can publish an edition of his textbook in China, but using Chinese data and drawing examples from the Chinese economy. (Authorizing an older edition is another possibility.) Such a textbook will have little resale market in the U.S. and elsewhere, and therefore will not cut into the sales of his book elsewhere. (Drugs can also be particularized to the Chinese population. E.G., birth control pills.) Software can be modified so that they only run with Chinese commands so that for a potential user who does not read or write Chinese, the software is basically worthless, no matter how inexpensive it is.

# Keeping the Markets Segmented: New Technologies Come to the Rescue

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- ◆ However, there are also new technologies that can be harnessed to prevent exports in commercial quantities. For example, one can have an RFID identifier attached to an authorized Chinese edition so that it can be spotted easily when an attempt is made to take it out of the country. For another example, one can make the site-license provided software specific machine dependent, through encryption or other means, so that it cannot be transferred to another machine without authorization from the original software provider (potentially even taking advantage of GPRS capabilities to identify the location of the user). This would prevent unauthorized secondary distribution which undermines the foundations of site licenses.

# Incentives for Enforcement

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- ◆ The publisher of the authorized edition will have an incentive to prevent other unauthorized local editions from emerging and to press for rigorous enforcement of by now its intellectual property rights.
- ◆ The site licensee also has an incentive to enforce the no-transfer rules on its members because its license may be cancelled if it is found that its members engage in unauthorized transfer. This will force the site licensee to either pay much higher prices for the software or to use pirated versions and risk prosecution and law suits for damages.

## How is This Win-Win?

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- ◆ This is win-win because the owner of the intellectual property rights can realize additional returns otherwise not available; the local users have legal access (with maintenance) to software and updates; and both the Chinese Government and the foreign governments are reasonably happy. It also allows Chinese users to be “honest”.
- ◆ Of course the producers of the pirated editions are hurt—so strictly speaking it is not completely win-win. But then a lowering of the tariff rates or a lifting of the import control hurts the smugglers.

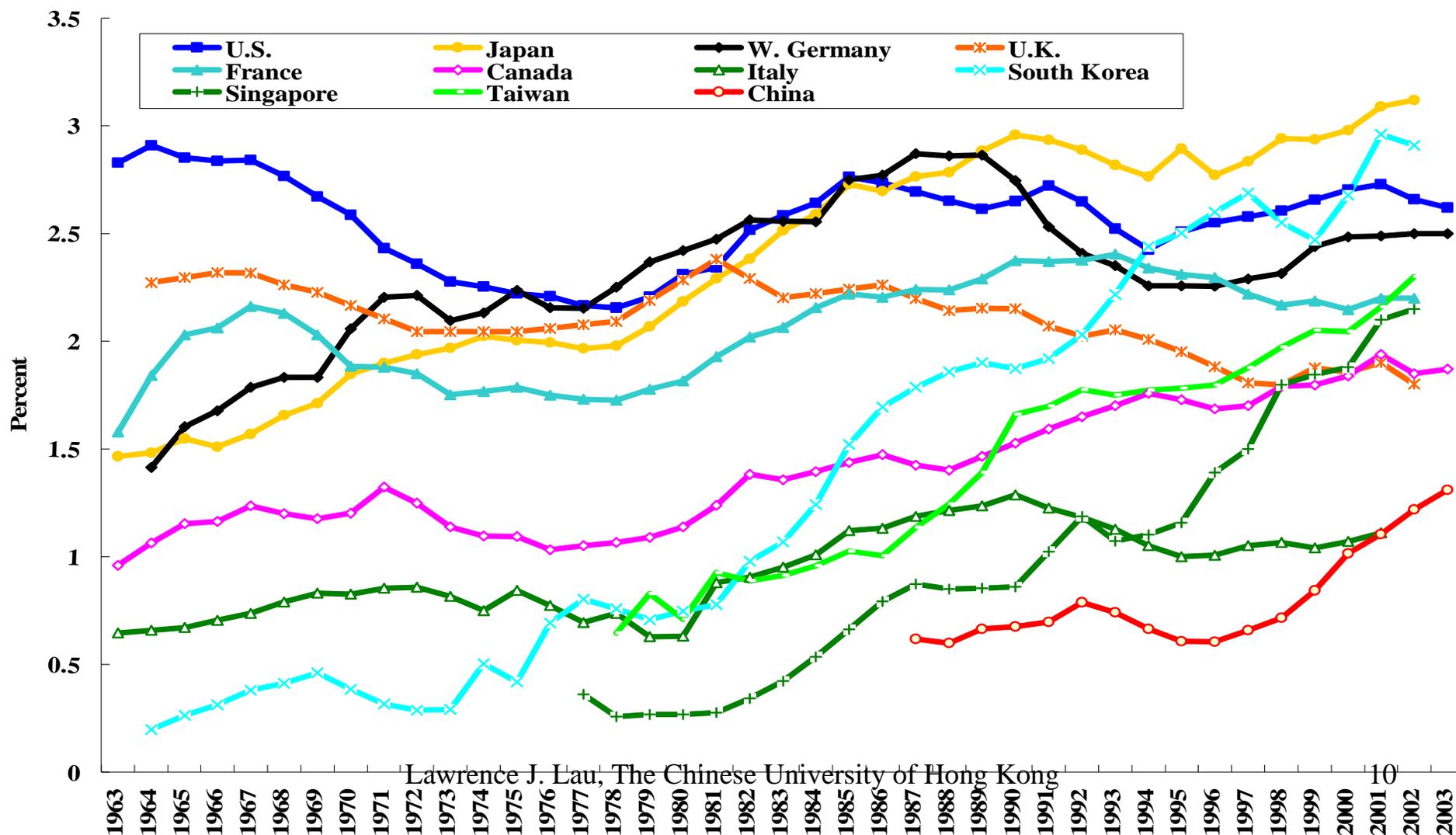
# Are There Damages?

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- ◆ Intellectual property rights infringement and violation do not necessarily damage the owner of the intellectual property rights.
- ◆ For example, Louis Vuitton handbags and Rolex watches. A fake one is a poor substitute for the real thing. The owner “knows”. So in a way, it is free advertising.
- ◆ This is not true for DVD’s or for software, because there is no particular satisfaction in using the “real” software as opposed to owning a “real” Vuitton handbag or a Rolex watch.
- ◆ In a way, one can also apply this argument in part to books.

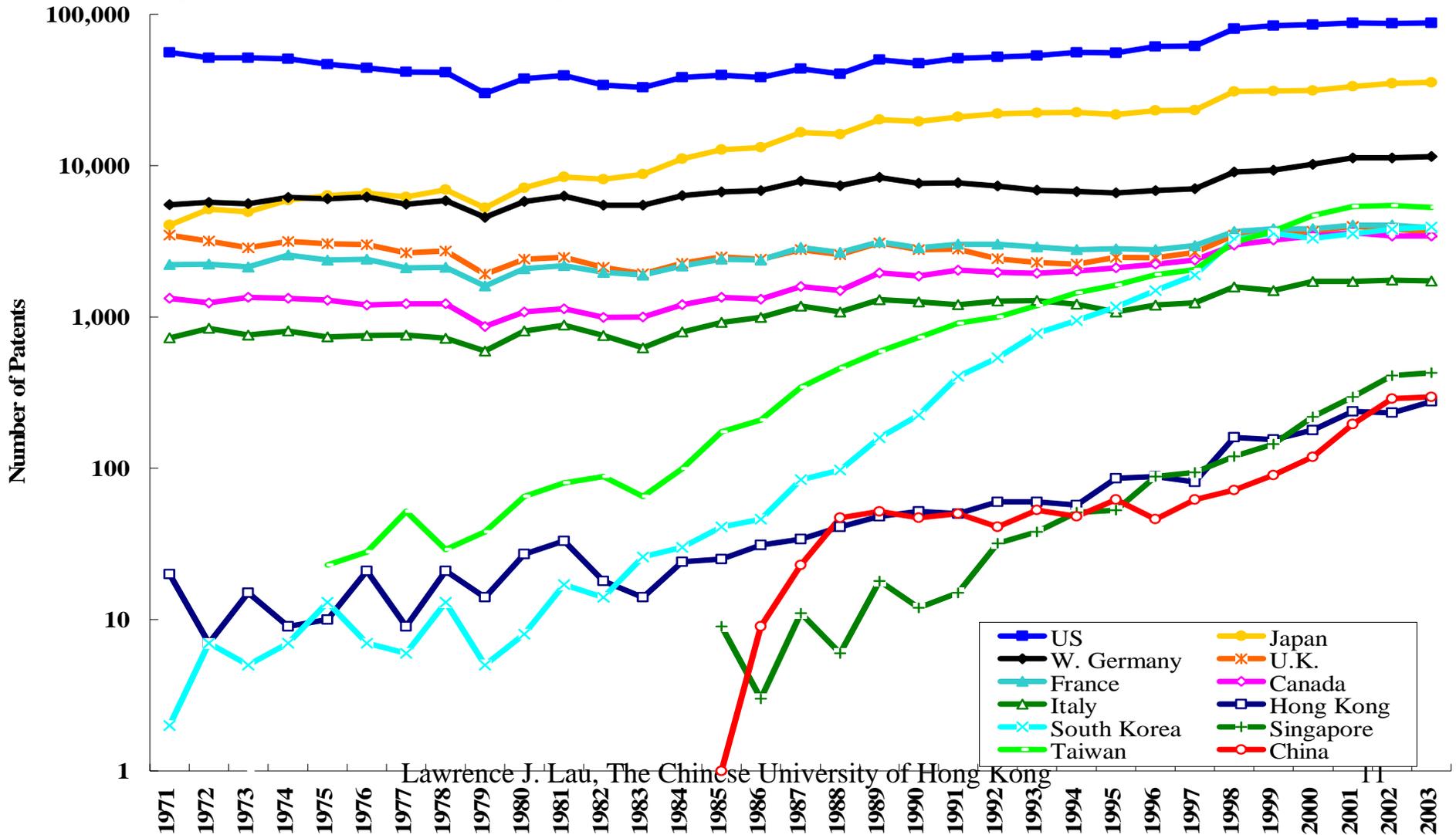
# R&D Expenditures as a Ratio of GDP: G-7 Countries, 3 East Asian NIES & China

Figure 8.1: R&D Expenditures as a Percentage of GDP: G-7 Countries, 3 East Asian NIEs and China



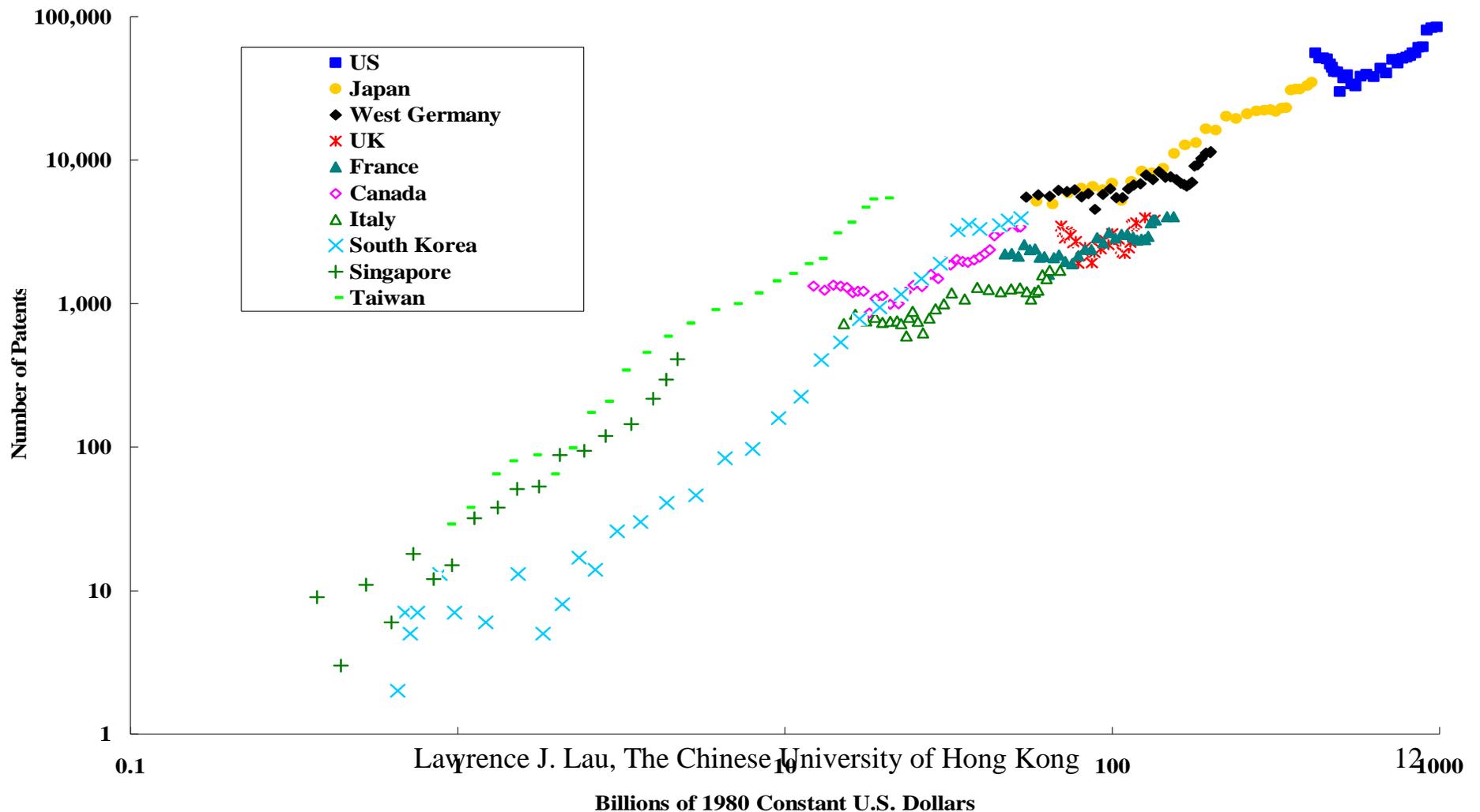
# Patents Granted in the United States: G-7 Countries, 4 East Asian NIEs & China

Figure 8.3: Patents Granted Annually in the United States: G7 Countries, 4 East Asian NIEs and China



# Patents Granted in the United States and R&D Capital Stocks, Selected Economies

Figure 8.4: The Number of U.S. Patents Granted Annually vs. R&D Capital Stocks



# The Issue of Copyright Durability

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- ◆ Current copyright laws in developed economies which extend the rights to 70 years beyond the life of the creator seem too long.
- ◆ It is a serious impediment to digital distribution of published material. For example, Google has basically digitized all of the books at Harvard University, and one can search the entire corpus on a keyword but downloads are not permitted.
- ◆ China should enact copyright laws that either provide for shorter durations for copyrights created in China in China itself or to mandate compulsory licensing in China.

# Concluding Remarks

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- ◆ Intellectual property rights require not just enforcement but also promotion.
- ◆ The best way to promote and protect intellectual property rights is to devise win-win solutions so as to create constituencies both domestically and overseas to sustain these solutions.