A Pluralistic Vision of Incentivizing Innovation

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Daniel J. Hemel & Lisa Larrimore Ouellette, *Beyond the Patents-Prizes Debate*, 92 **Texas L. Rev.** 303 (2013).

In the 19th century, legal scholarship focused on legal doctrine. In the 20th century, legal scholars began to examine the policy effects of legal doctrine, paying particular attention to how changes in doctrine could yield better policies. Now, such policy-oriented approaches are cemented into nearly every U.S. law review article. Although this shift has in my view generally been beneficial, it still suffers from a doctrinal myopia: legal scholars usually write about only the swaths of law they know well, often overlooking other strands of law that are quite pertinent to the *policy* issues being addressed.

For example, although patent law scholars frequently opine about the nuances of patent doctrine and how changes in those nuances may affect innovation incentives, they have often ignored how other available policy tools—such as grants and government prizes—affect innovation. Although there is certainly law that deals with grants and prizes, it is rarely the subject of litigation and is fairly specialized (hence, occupying the minds of a small number of lawyers). None of it is taught in law schools. As such, law professors tend to know (and write) little about it.

On the other hand, economists who write about innovation tend to consider all of the available policy tools. Thus, there is a substantial literature in economics on grants and prizes. Yet, from a legal scholar's perspective, most of this literature is too broad-brush, as it tends to abstract away from important legal nuances. Generally, economists either don't examine in sufficient detail how changes in the law can impact policy, or else (at least in the absence of a law professor co-author), offer overly simplistic legal analysis.

Recently legal scholars, drawing from discussions in the economics literature, have applied more rigorous analysis to various policy tools not typically examined in the legal literature. In the field of patent law, several articles have explored the interaction between patents, prizes, and grants.

Oddly, none have explored in any detail the tax deductions and tax credits undertaken for R & D. Hemel and Ouellette make an impressive contribution by considering from a rigorous legal perspective this important—and otherwise overlooked—driver of innovation. This lacuna in the literature is even more shocking because, as the authors point out, the U.S. government spends tens of billions of dollars each year merely in R & D tax credits, plus surely tens of billions more in general deductions for R & D expenditures.

What is most valuable about Hemel and Ouellette's paper is their "compare-and-contrast" analysis of the four main policy tools—patents, prizes, grants, and tax credits—used to promote innovation. Importantly, and in contrast with some recent works on prizes by others in the field, they properly recognize that there is generally "no free lunch" in the innovation game. As such, all of the policy alternatives tend to be costly.

My favorite example of theirs on this score regards an innovative drug for baldness. With some basic assumptions, they show that the number of potential consumers priced out from purchasing the drug *is*

exactly the same under a patent and prize regime, as long as the specific users are taxed in order to pay for the prize. One can extend this example. Even if the prize amount is generated from taxpayers as a whole, this leads to a mandatory insurance system of sorts for innovation. The marginal additional tax paid by each person represents the premium charged for the right to purchase a "needed" innovation of interest at marginal cost. Of course, such a regime—as well as one premised on grants, tax credits, or patents—all lead to similar "deadweight losses," at least from the ideal perspective in which innovation appears out of thin air.

Importantly, Hemel and Ouellette also contrast these policy tools, engaging in a sophisticated analysis of ex ante vs. ex post trade-offs, cross-subsidization, racing, coordination, risk, and administrative costs. Of course, this sort of discussion could occupy several lengthy books, and one cannot fault the authors for not considering every nook and cranny of these important topics. Instead, they have displayed in consummate fashion how such analysis should and could occur on a more detailed level.

On a broader level, Hemel and Ouellette's analysis shows that legal scholarship—and to some degree, legal pedagogy—ought not to solely concern itself with a narrow set of legal doctrines as the means to policy ends. Rather, it should strive to consider a range of legal *and* non-legal options that are related by achieving a common goal—for instance, innovation.

In other words, merely considering one's own realm of expertise—at least in a broad, policy-driven article—will tend to be myopic, resulting in an incomplete analysis. Of course, such a view implies that co-authoring (e.g., one expert in patent law, another in antitrust, another in tax, another in economics, etc.) will often be essential. Writing in larger and larger groups will certainly be a tough transition, individually and institutionally. Nonetheless, the sciences learned this valuable lesson many years ago. As Hemel and Ouellette have shown us, now it's our turn.

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