

Patent Nationally, Innovate Locally

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Abstract

Innovation – doing things that are new and in some way better than what existed before – produces new information that benefits others across geographic regions. But innovation is also an intensely local activity that produces economic benefits for the region in which innovators work and reside. This unique attribute of innovation deeply influences how government supports innovation in the United States. At a descriptive level, the federal government vigorously protects intellectual property rights in new inventions and original expression, but directly funds research only in a few circumstances—primarily national defense. In contrast, sub-national governments like states and cities do not grant intellectual property rights, but perform a similar function using innovation finance: direct subsidies for innovation paid from general tax revenues.

This asymmetry can be explained and justified by the principle that *public goods should be supplied by the smallest unit of governance that internalizes the benefits*. States cannot internalize the benefits of innovation using patents and copyrights, but they can draw on public money to capture the geographically localized benefits that result from the agglomeration economies that grow up around knowledge exchange (called “innovation clusters”). This justifies federal patents and copyrights and federal funding for research of high national relevance, but *not* federal funding for the majority of private sector innovation.

This conclusion casts doubt on proposals to use federal funds to directly finance innovation in lieu of IP. But it also casts doubt on the argument that government *must* rely exclusively on IP because it cannot effectively use public money to promote innovation. Instead, the American innovation system is bifurcated: the federal government protects exclusive rights in information that “spills over” state lines; state and local governments finance the practical development of innovations within their particular geographic communities.