

A Closer Look at China's Supposed Misappropriation of U.S. Intellectual Property

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The ongoing trade conflict between the United States and China dominates today's news on international trade. Analysts cite China's misappropriation of foreign intellectual property as an important source of bilateral tension that has prompted the United States to impose tariffs on certain Chinese goods.¹

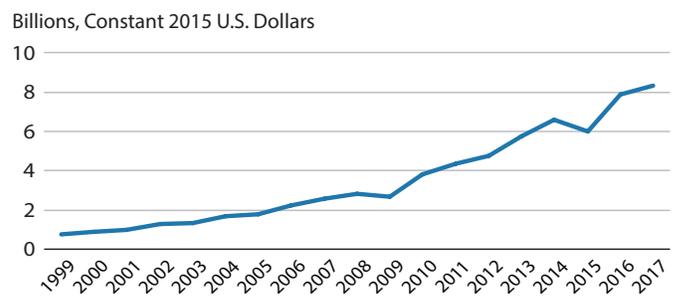
Given the growing trade tensions between the United States and China, and the economic implications of tariff increases, it is important to analyze whether China has taken steps to improve its enforcement of intellectual property rights. One way to do so is to look at data on China's royalty payments to the United States.

China has significantly increased its payments for the use of U.S. intellectual property.

People and firms pay royalties to use intellectual property, which can be covered under licensing agreements, trademarks, patents, and copyrights. Royalties are recorded as a trade in services in the international balance of payments. For instance, payments for the use of U.S. technology by a Chinese firm are recorded as an import of services by China and an export of services by the United States. The Organisation for Economic Co-operation and Development (OECD) provides bilateral data on trade in services at the industry level over time and includes data on charges for the use of foreign intellectual property.²

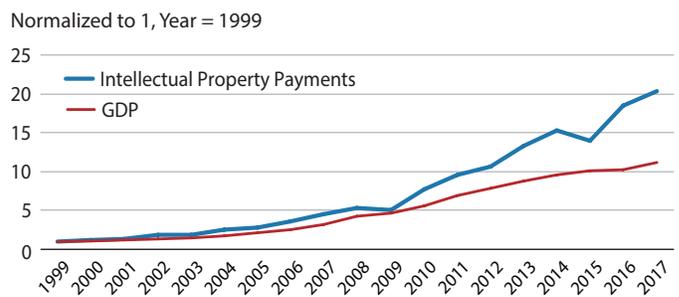
The data show that Chinese royalty payments to the world grew from \$1.4 billion in 1999 to \$27.2 billion in 2017. In 2016, China ranked fourth in royalty payments to the world, at just under \$30 billion, right behind the United States at just over \$40 billion. Both countries are listed behind Ireland (just under \$80 billion) and the Netherlands (just under \$50 billion) in the same year. Ireland and the Netherlands are special cases because low corporate taxes in these countries incentivize profit shifting by multinational corporations located in other countries. For instance, several

Figure 1
A. China's Payments for the Use of U.S. Intellectual Property



SOURCE: OECD.

B. China's Payments for the Use of U.S. Intellectual Property and China's GDP



SOURCE: World Bank and OECD.

American companies have opened affiliates in these countries to transfer their technology (i.e., patents) there. The affiliate pays the parent company royalties for the profits obtained using those technologies. These profits are not repatriated to the United States and therefore are taxed at the lower corporate tax rates of Ireland and the Netherlands, where the affiliates are domiciled.³

In Figure 1A, we look specifically at China's payments for the use of U.S. intellectual property. The payments grew significantly, from \$755 million in 1999 to \$8.3 billion in 2017—more than 11-fold. Even more interesting, as shown

in Figure 1B, is that China's royalty payments to the United States (blue line) grew faster than China's GDP (red line).

These data may suggest improvement of China's enforcement of intellectual property rights. One cannot infer from the data, however, whether China is paying what it would be expected to pay for the use of U.S. intellectual property. The issue of China's potential misappropriation of U.S. intellectual property calls for further research. ■

Notes

¹ Office of the United States Trade Representative. "USTR Finalizes Tariffs on \$200 Billion of Chinese Imports in Response to China's Unfair Trade Practices." Press release, September 2018; <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2018/september/ustr-finalizes-tariffs-200>.

² OECD. Trade in Services (indicator). 2019; <https://doi.org/10.1787/3796b5f0-en>, accessed January 7, 2019.

³ Lardy, N.R. "China: Forced Technology Transfer and Theft?" Peterson Institute for International Economics, April 20, 2018.