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Who owns the invention?

Why IP title can make or break a start-up investment or exit

For many start-ups, intellectual property is the asset on which future value is built. But creating, paying for or using IP does not necessarily mean that the company owns it. When that distinction emerges during an investment round or exit, the commercial consequences can be significant.

AT A GLANCE: KEY TAKEAWAYS

- A start-up does not necessarily own IP simply because it paid for, commissioned or uses it.
- Pre-incorporation development, contractors, former employers, universities and informal collaborators are common sources of defective title.
- Investors and buyers focus on whether the company owns or securely controls the assets supporting its valuation.
- Missing assignments and uncertain ownership can lead to lower valuations, conditions precedent, escrow, indemnities, transaction delays and additional cost.
- Good IP governance at formation is usually far cheaper than repairing ownership defects during a funding round or sale.

The asset a start-up may not own

Start-ups are usually built around future potential rather than substantial physical assets. For technology, life-sciences, engineering, creative, consumer-brand and data-driven ventures, much of that potential resides in intellectual property: software, algorithms, inventions, technical know-how, product designs, databases, content, brands, confidential processes and digital assets.

Yet ownership of those assets is surprisingly often addressed only after product development, fundraising or commercial launch. Founders are focused on building products, winning customers and raising capital. Development is iterative. Friends help. Former colleagues provide input. Freelancers build prototypes. An agency creates the brand. A student develops code. A founder begins work before the company even exists.

Everyone may understand that the work is being done “for the business”. Legally, however, that may not be enough.

CORE PRINCIPLE

Creation, possession, payment, use and legal ownership are different concepts.

A founder may have created the technology. A contractor may have written the source code. A university may have supported the underlying research. An agency may have designed the brand. The start-up may have paid for and commercially exploited all of it. None of those facts, by themselves, necessarily establishes that the company owns the relevant intellectual property.

That distinction matters because investors do not invest merely in a good idea or the continued goodwill of its creators. They invest in a legal entity and expect that entity to own, or at least securely control, the assets required to execute its business plan.

What Does "Chain of Title" Mean?

A sound IP chain of title allows a company to demonstrate how the relevant intellectual property moved from its original creator or owner into the company. It is not enough to state that "the company owns the IP". The company should be able to explain the legal basis for that conclusion.

MATERIAL IP	Identify the technology, software, brands, designs, data, documentation, content, know-how and other material assets.
CREATOR / SOURCE	Record who created, supplied or originally owned each material asset.
BASIS OF RIGHTS	Identify the contract, assignment, statute, licence or other legal basis on which the company owns or may use the asset.
RESTRICTIONS	Record third-party rights, licences, open-source terms, territorial restrictions, security interests and other limitations.
EVIDENCE	Keep executed agreements, registrations, contributor records and other evidence that can be produced in diligence.

The analysis must be undertaken asset by asset. Copyright, patents, trade marks, designs, confidential information, domain names and digital accounts do not all follow identical ownership rules. Nor will the legal outcome necessarily be the same for an employee, consultant, director, founder, university researcher or independent contractor. Jurisdiction also matters.

The assumption that "we paid for it, therefore we own it" is consequently a dangerous basis on which to build an IP-intensive company.

Where Does the Chain Most Often Break?

1. IP created before incorporation

The start-up frequently begins before the company does. A founder may develop the prototype, code, invention, database, product design or brand months before incorporating a company. Incorporation does not automatically transfer those pre-existing rights. The individual may later become a shareholder, director or employee, but unless the relevant IP is properly transferred or licensed, the legal owner may remain the founder.

That can remain invisible while relationships are good. It becomes considerably more important if the founder leaves, dies, becomes insolvent, falls into dispute with the other shareholders or refuses to cooperate with an investor or acquirer.

2. Contractors, developers and consultants

Independent contractors are another major source of title uncertainty. An external developer may have created the company's entire minimum viable product. A designer may have produced its visual identity. An engineering consultant may have contributed patentable technology. An agreement to perform work does not invariably amount to an agreement transferring all intellectual property arising from that work.

CONTRACT DRAFTING SHOULD DISTINGUISH

- Background IP – technology, methodologies, software, know-how or materials the contractor already owned before the engagement.
- Foreground IP – intellectual property created specifically through the engagement.
- The rights the company needs to modify, commercialise, sublicense and ultimately transfer the deliverables.
- Confidentiality, inventions, improvements, further-assurance obligations and third-party materials.

Without this clarity, a company may discover that it owns the commercial relationship but not the technology on which that relationship depends.

3. Departing founders and informal collaborators

Early-stage ventures are often collaborative and informal. That works until it does not. A former founder or contributor who created material technology without signing an assignment may retain ownership or claim an interest in the IP. A missing signature that seemed unimportant in year one may become decisive five years later when an acquisition agreement is ready for signature.

Retrospective remediation is rarely as simple as saying “we will just get the person to sign an assignment”. The contributor may no longer be contactable, may refuse, may dispute the company’s account of events, or may recognise that the transaction cannot proceed without their cooperation.

4. Prior employers and university research

Founders also bring histories with them. Relevant technology may have originated while the founder was employed elsewhere, undertaking postgraduate research, working within a university, participating in publicly financed research, working under a consultancy, subject to confidentiality obligations or collaborating with another organisation.

In South Africa, university spin-outs require particular care where intellectual property emanates from publicly financed research and development. The Intellectual Property Rights from Publicly Financed Research and Development Act 51 of 2008 establishes a specific statutory framework around ownership, management and commercialisation of qualifying publicly financed IP.

The commercial question is not simply whether a university or former employer would ultimately succeed in litigation. A credible competing claim may itself be enough to unsettle an investor or buyer.

5. Digital assets in the wrong name

Not every title problem looks like a patent or copyright dispute. The domain may be registered personally by the founder. The code repository may sit in an employee’s account. The cloud environment may be contracted through a consultant. The trade mark may have been filed in the name of an individual. The app-store account may belong to the developer.

PRACTICAL CONTROL MATTERS

Ask not only “Who owns the IP?” but also “Who controls the infrastructure through which it is commercialised?”

6. Open-source and third-party software

Open-source software presents a slightly different issue. Open source does not mean that a company has no rights to use the software, nor does every open-source component create a problem. The difficulty arises when a company cannot identify what third-party software has been incorporated into its product or what licence terms apply.

Depending on the licence, obligations may relate to notices, attribution, availability of source code, modifications, distribution or licensing of derivative works. A maturing software business should increasingly be able to identify its material components and corresponding licences, potentially through a software bill of materials and a structured open-source compliance process.

Chain of title is not freedom to operate

Ownership answers one question: whether the company owns, or has adequate rights to use, the intellectual property in its own business. Freedom to operate asks a different question: whether commercialising the product may infringe rights held by somebody else.

WHY THE DISTINCTION MATTERS

- A company may have a perfect assignment from every founder and contractor and still face third-party patent, copyright or trade mark risk.
- Conversely, a product may not infringe third-party rights but the company may still lack title to its own underlying IP.
- Sophisticated diligence considers both: ownership/control and third-party infringement exposure.

When legal detail becomes commercial risk

A title defect does not remain confined to the legal department. If a company cannot demonstrate ownership or adequate control of its core technology, it may affect its ability to grant valid licences, enforce rights against competitors, enter exclusive arrangements, prevent former contributors from exploiting the same technology, provide investor warranties, sublicense technology, use IP as security or transfer the business to an acquirer.

The problem therefore creates a gap between the company the founders believe they have built and the company the legal documentation shows they own. That gap may remain invisible during ordinary operations. Due diligence exposes it.

The investment conundrum

Investment due diligence tests the assumptions supporting valuation. Where intellectual property drives the start-up's value, one of those assumptions is that the company owns or validly controls the technology it intends to scale.

WHAT INVESTORS ARE LIKELY TO ASK FOR

- Registered IP schedules and filing records.
- Founder, employee, consultant and development agreements.
- Invention and contributor history.
- Licences, university or former-employer consents and third-party restrictions.
- Open-source and third-party software records.
- Evidence of ownership or control of domains, repositories and key digital accounts.
- Details of disputes, claims, threatened claims or unresolved ownership questions.

Where a gap is discovered, the investor may require it to be fixed before funds are advanced. That could mean a confirmatory assignment, waiver, consent, release or licence. If remediation cannot happen quickly, the commercial response may include a valuation adjustment, additional warranties, a specific indemnity, escrow, holdback or a delayed closing.

The investor's concern is not necessarily that litigation is inevitable. The more immediate issue is whether uncertainty about the asset base makes the business more difficult to value, finance or scale.

The exit conundrum: When diligence debt becomes due

The consequences can become even more pronounced during an acquisition. A purchaser expects to acquire a business capable of continuing after the sellers leave. If the target's value resides primarily in intellectual property, the purchaser needs confidence that it is actually acquiring that IP.

This is where years of informal practices can crystallise into what might be called IP diligence debt. Like technical debt, diligence debt is created when a company adopts an expedient short-term solution but leaves the underlying issue unresolved.

- unsigned assignments
- incomplete development records
- unclear contractor terms
- unrecorded transfers
- personal ownership of business assets
- undocumented licences
- unresolved university or employer claims
- unmanaged third-party software

During an exit, that debt becomes payable at precisely the point when the company's leverage is weakest and the stakes are highest. A missing assignment that could have been obtained at little cost when a developer joined the project may, years later, delay a multimillion-rand transaction.

Commercial consequences matrix *(quick view)*

Failure type	Likely investor response	Typical remedy	Cost drivers
Missing assignments	Holdback; lower valuation	Retroactive assignment; indemnity	Legal fees; founder negotiation
Contractor ownership	Escrow; indemnity	Assignment or buy-out	Contractor fee; delay
Open-source contamination	Re-engineering; licence negotiation	Replace code; re-license	Dev cost; time to market
University claims	Licence negotiation; revenue sharing	Option/assignment	Licensing fees; ongoing royalties

Common IP ownership failures can translate quickly into valuation adjustments, transaction protections and remediation costs.

The important point is that an IP defect does not always destroy a transaction. Risk can sometimes be priced, insured, ring-fenced or remedied. But it rarely disappears merely because everyone agrees that the underlying business is promising.

What should a start-up do?

The objective is proportionate IP governance, not unnecessary bureaucracy.

At formation

Identify what IP already exists and who owns it. Transfer or appropriately license material pre-incorporation IP to the company. Make sure important domains, repositories, trade marks and digital accounts are held or controlled by the correct entity.

During development

Put every material contributor under an appropriate written agreement before the work begins. Address IP ownership, confidentiality, background IP, foreground IP, inventions and improvements, third-party materials, further-assurance obligations and moral rights where relevant.

Manage third-party technology

Know what is entering the product. Maintain an appropriate register of third-party and open-source components and understand the corresponding licence terms.

Investigate founder history

Ask difficult questions early. Was the technology developed while someone was employed elsewhere? Did university resources contribute? Was publicly financed research involved? Could a collaborator be entitled to rights? Resolving these questions before they become contentious is usually easier and cheaper.

Before financing or exit

Conduct an internal IP audit and create a simple chain-of-title schedule. The objective is not perfection. It is to ensure that material risk is known, explainable and manageable before a third party discovers it.

ASSET	What is the material IP or digital asset?
SOURCE	Who created or supplied it?
RIGHTS	Who owns it now, and on what legal basis?
RESTRICTIONS	What licences, third-party rights or limitations apply?
EVIDENCE	Where are the signed agreements, filings and supporting records?
REMEDIATION	What needs to be fixed, recorded or clarified before diligence?

Why this matters

For founders, IP governance may initially feel like expenditure on documents rather than product. That perspective changes dramatically when the business seeks investment. The cost of documenting ownership when a contractor is appointed is usually modest. The cost of negotiating with the same contractor when they discover that an acquisition depends on their signature may be very different.

For investors and acquirers, the issue is equally straightforward. They are not merely acquiring access to clever people or promising technology. They are acquiring rights. If those rights cannot be demonstrated, the risk must either be cured, allocated or reflected in price.

IP BRIEFS® TAKEAWAY

Innovation creates value. Clear ownership captures it.

A start-up may have outstanding technology, strong customers and considerable market momentum. But if the company cannot establish that it owns or securely controls the intellectual property underlying the business, those achievements may not translate into a readily financeable or transferable asset.

Good IP hygiene is therefore more than legal compliance. It is value preservation. The earlier a business identifies its material IP, documents contributor relationships, secures assignments, manages third-party rights and establishes an intelligible chain of title, the stronger its position will be when investors or buyers eventually ask the most basic diligence question of all: who actually owns the innovation?

About the Author

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