

Staging of Venture Financing, Investor Opportunism and Patent Law

Jochen Bigus 

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Abstract

Abstract: Stage financing provides a real option that is valuable when facing external uncertainty. However, it may also induce investor hold-up, if the property rights on an invention are not sufficiently protected. As a consequence, the entrepreneur may not work hard. Investor opportunism is less likely to occur, if investors' residual cash-flow-rights are contingent on verifiable 'milestones' in the previous stage. Equity-linked financing also provides high-powered incentives to the investor not to 'steal the idea' because his payoff becomes sensitive to the project value. The paper provides a new explanation for both types of contractual provisions.

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