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Pros and Cons of IP Ownership: LLC vs. Private

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For most organizations, the most valuable thing that they possess is their intellectual property (IP) portfolio. Patents, trademarks, and copyrights aren't just papers and concepts; they embody potential revenue streams, competitive advantages, and brand reputations. However, for LLCs, deciding the ownership structure of these IP assets is a critical decision, with implications on profitability, legal exposure, and overall business sustainability. To better understand what approach might be best for an organization, it is important to know the pros and cons of each type of ownership.

IP Ownership as an LLC

Pros

At the heart of the advantages of owning IP under an LLC is the foundational premise of asset protection. An LLC serves as a distinct legal entity, separating the business's liabilities from those of its owners or members. Should there be litigation targeting the IP, the potential financial repercussions are typically confined to the business, safeguarding the personal assets of the members. Conversely, for individuals holding IP in their name, the boundaries blur. A lawsuit directed towards the IP potentially exposes their homes, bank accounts, and other personal assets to risk.

Beyond the legal protections, operational efficiencies also weigh in favor of LLC-held IP. Ownership of IP by an LLC centralizes its management. Licensing negotiations, royalty tracking, contractual revisions, and even disputes are handled uniformly and within the structured framework of the business. This organizational clarity reduces the likelihood of internal conflicts over IP management and revenue distribution. Moreover, from an accounting perspective, revenues and expenses tied to the IP are cleanly recorded under the business's ledger. This clear delineation can simplify tax filings and ensure adherence to financial compliance requirements.

In the competitive world of business financing and mergers and acquisitions, the ownership of IP by an LLC can be a game-changer. As IP assets bolster the tangible and intangible valuation of a company, potential investors, venture capitalists, or acquisition-minded corporations often view them as strong indicators of long-term viability and growth potential. When an LLC owns a sought-after patent or other desirable IP, it doesn't just represent a potential revenue stream—it embodies innovation, market leadership, and brand strength. Such assets, when under the LLC's umbrella, can be more effectively leveraged in funding pitches, negotiations, or sale discussions.

Cons

However, there are tax implications to consider when deciding whether to own IP through an LLC. In the U.S., the majority of LLCs operate as tax pass-through entities. This means that the LLC doesn't pay federal income tax directly. Rather, any income or losses get channeled to the tax returns of individual members and are taxed based on their respective tax brackets. So, if the LLC's intellectual property yields income, members will report this income on their personal tax returns.

Additionally, the collective decision-making nature of LLCs might be democratic, but it's not always desirable, especially for IP creators. Once IP is nested under the LLC, it is subject to the decision-making protocols of the organization. This could mean board votes, member consensus, or decisions by designated management. For the original innovator or creator, this can be particularly stifling. Their vision for the IP's evolution, licensing strategies, or potential collaborations can be overridden by collective decisions, potentially diluting the original intent or value of the IP.

Private Ownership of IP

Pros

When it comes to private ownership, the allure of autonomy is undeniable. Private ownership of IP places the reins firmly in the hands of the creator or owner. Whether it's entering into licensing deals, initiating sales, or evolving the IP, decisions can be made swiftly without the bureaucratic layers of organizational consensus. This can be particularly advantageous in rapidly changing industries where timely decisions can make or break opportunities.

Beyond control, there's also the fiscal advantage. With private ownership, all revenues generated from the IP flow directly to the individual. There's no sharing with other members or waiting for organizational distribution. This direct revenue stream can be a significant financial boon, especially if the IP becomes highly lucrative.

Cons

However, unlike the protective shield offered by LLCs, private IP ownership exposes the individual to direct legal challenges. Any litigation targeting the IP could jeopardize the owner's personal assets, from properties to bank accounts.

Further, while autonomy is a perk of private ownership, it can also be its pitfall. If an IP is privately owned but utilized by an LLC or another entity, it necessitates a clear delineation of terms. This can manifest in convoluted licensing agreements, revenue-sharing contracts, or royalty negotiations. Additionally, any perceived inequity can sow seeds of discord, leading to internal disputes or legal challenges.

Conclusion

Ultimately, the avenue chosen for IP ownership — whether under an LLC or privately — hinges on the specific aspirations and situations of the LLC members or the individual. It's a delicate balance between protection and control, fiscal advantages, and potential liabilities. Given the weightiness of the decision, seeking insights from legal and financial experts is indispensable. Their guidance can illuminate the nuances, helping stakeholders navigate this complex decision-making landscape.