Why Investment Managers and Advisors Should Consider the Creation and Management of a Royalty Income Fund

Arthur Lipper

The reason to start any new business is to profit from the provision of service.

Investors are increasingly seeking risk-lessened annually increasing income.

A diversified portfolio of long term royalties, issued by privately owned companies having the prospect of increasing revenues, should provide for increased investor income and continuing daily risk reduction.

Many investment advisors are already serving the owners of privately owned businesses in the management of their personal and family investments,

Many business owners seek growth capital and are prepared to share revenues or revenue increments in return for capital not requiring an equity dilution.

Therefore, many investment managers currently have, within their existing universe of relationships, parties seeking that which royalties can provide, increasing income without a need for ownership sharing.

The patented approach to using royalties in the financing of businesses works as follows. It is really very simple and straight forward.

Assuming there is a royalty income fund, which can be a fund with shareholders or a limited partnership with partners, there is an investment manager. There are only four major areas of negotiation in a royalty transaction, though there are numerous details for each. The four areas follow.

The investment manager reviews, in confidence, data regarding a privately owned company to determine both its sustainability and prospects for increased revenues, facilitated by the acquisition of additional capital.

1. The investment manager and business owner review and agree as to the amount of money the company requires to achieve a defined objective and also the amount of money the manager is prepared to expose to risk in providing capital to the company. Assuming the objective to be increased revenues and the amount of capital reasonable in terms of the manager's diversified asset pool the next step is the negotiation of the terms of a transaction.

2. The amount to be paid for the royalty having been agreed, the next consideration is the period of royalty payment. The basic principle is that the longer the term of the royalty payment obligation the lesser can be the royalty rate paid on the defined revenues. In our examples we use a 20-year period. However, we believe that most royalty agreements should have a redemption clause so the royalty issuer knows how much, in a worst case, he will have to pay, in addition to that already cumulatively paid in royalties, to terminate the royalty.

3. Next, the percentage of defined revenues to be paid to the owners of the royalty is negotiated. Every professional investment manager has an Internal Rate of Return (IRR) objective. In our website calculators, www.REXRoyalties.com, www.REXdebt-shareRoyalties.com, www.REXComparator.com, www.REX-PV.com and finally, the patent pending www.REXScaledRoyalties.com IRR is calculated based on the projected revenues and therefore royalties. In each of the websites there are samples and instructional text.

4. Finally, in our patented approach, there is a negotiation as to how the contractual obligations of the royalty issuer are assured for the benefit of the investors who purchased the agreed percentage of the issuer's revenues for an agreed period of time. The need for the contractual obligation assurance is that in the event the issuer is reorganized and refinanced, the new company must honor and continue the royalty payments. We suggest the issuer transfer or irrevocably assign to an agreed party the ownership of the critical assets of the company, without which it cannot operate, such as

intellectual property and whatever other assets are agreed. That party grants the issuer a free, exclusive, international license to use the assets for so long as the company is in compliance with its agreements with the investors. Upon the investors receiving an agreed amount of cumulative royalties the unfettered ownership of the critical assets are to be returned to the company without cost.

The greater the confidence of the investment manager in the issuer's ability to achieve its objectives and the inherent integrity of the process, the greater the likelihood of a closing on fair terms.

In our patented approach, there is the requirement that royalties be paid immediately on receipt of revenues, so the royalty owner is never an account payable by the royalty issuer. We have developed the procedure for this royalty collection to occur. There is an annual audit of revenues.

We suggest the manager collect the royalties, as due and make a distribution to the owners of the royalties, less fees and expenses, quarterly.

As will be seen in the website calculators samples and as easily reviewable at www.Royalties.Website the returns to investors from issuer revenue increases is very satisfactory and major revenue increases, though welcome, are not necessary for the investors to reach their desired IRR objective.

In the www.REX-PV.com website calculator we address the likelihood of the original royalty purchaser(s), for tax and possibly other reasons, to wish to sell the royalty. The website calculates the amount a secondary buyer would have to pay the seller for the seller to achieve their target IRR. We also calculate the results for the new owner of the royalty in terms of capital recapture and IRR.

The www.REXComparator.com allows two different term deal to be compared using the same projected revenues.

The www.REXdebt-shareroyalties.com is the arrangement, which we believe to be best for both the early stage royalty issuer and the investor. In this patent pending approach the company is loaned

money, at favorable interest rates, for five years or less (and the loans may be prepaid without penalty) with a modest level royalty commencing on the loan repayment.

The www.REXScaledRoyalty.com facilitates the negotiation regarding changes in deal terms due to the possibility the projected revenues will either exceed or disappoint during a negotiated period.

We believe that royalties are the better way of both investing in and financing of privately owned companies and wish to be of service. PacificRoyalties.com can also be of advisory and licensing assistance.

Arthur Lipper, Chairman
British Far East Holdings Ltd.