Company Business Owners and Managers Should Use Royalties When Raising Capital ©

Arthur Lipper

Businesses need capital to expand. The general belief is that increased business revenues will result in increased profits.

The capital for business expansion can come from retained earnings or from external sources. Traditionally, capital is raised by selling a percentage or the company's ownership, as debt is unlikely to be available to companies initially, or possible only on unattractive terms.

The sale of a company's stock creates the necessity for the controlling shareholders, usually through a board of directors, to make all management decisions based on what is best for all shareholders, without favoring any specific shareholders. Once shares are sold to investors, the original directors of the company effectively become fiduciaries representing the interests equally of all of the shareholders.

This means that executive compensation, health and retirement plans, acquisitions, terms of many contracts regarding the sale of products, and services or assets must be viewed in terms of what's best for all of the shareholders. Questions will arise, such as: What are the policies regarding client entertainment and travel reimbursement policies? Should the company be providing expensive cars -- or any cars -- to executives, etc. ?

How much information about the company and its finances must be made available to investors in the company? Should the investors be "represented" specially by one or more members of the board of directors?

Numerous perks favoring owners could or will be forsaken when investment in the company is solicited and accepted in the form of equity.

Reduced ownership by founders and controlling shareholders, resulting from equity dilution, is unnecessary and too high a price to pay for success.

Revenue-sharing agreements are called revenue royalties, and these royalties can be sold to investors. Royalty investors do not vote, nor do

they have any ownership in the royalty issuing company. Royalties are simply an agreement by the company to sell to investors a percentage of defined revenues, for an agreed period, on agreed terms.

There are investor protection clauses and arrangements which are made in the royalties we structure and advise companies and investors to accept. There are also rights of redemption we suggest be included which give royalty issuing companies an ability to terminate the royalty on pre-agreed terms.

The royalty issuing company submits to the investor Projected Revenues, which are not, unless guaranteed, more than estimates, based on which, using our REX calculators, the results of the terms negotiated can be studied and assessed.

Our approaches, some of which are patented, to using royalties in the financing of companies include the following;

REX-Basic.com The simplest approach of a royalty paid on revenues, for an agreed period.

REXdebt-shareRoyalties.com In which case an amount is loaned, on fair terms, combined with a royalty with a modest royalty rate, commencing on the repayment of the loan.

REXScaledRoyalties.com An approach facilitating the ability of the royalty issuing company to benefit from exceeding projected results in a defined period and be penalized if failing by an agreed percentage of the projection. This “carrot and stick” approach encourages royalty issuers to be conservative in their revenue projections.

REX-RIAR.com The Royalty Issuer Assured Return approach allows an issuer to justify a lower royalty rate by assuring minimum returns. It facilitates the use of assurances based on multiple of investor cost in agreed periods and also introduces the concept of Credited Royalties, in which the issuer pays a higher royalty rate for the temporary retention of the royalties due the investor, with full payment being made at the end of the royalty payment period.

Royalties can be designed to accommodate the needs of both investors and issuers.

Royalties are the better way of both investing in and financing of privately owned and early sage companies.

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