THE ROAD LESS TRAVELED

The story of

REVENUE ROYALTIES

The better way to finance innovative business

Published by

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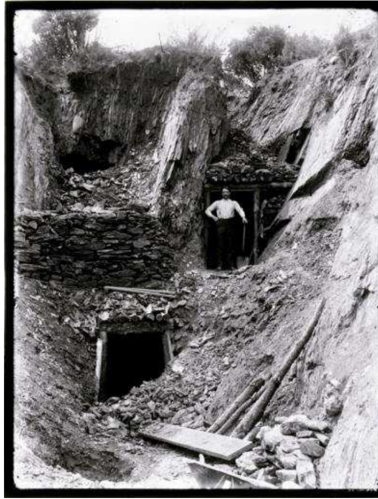
Dear innovator:

- Do you wonder how to identify and reach the right investors for your business?
- Have you found that investors think your company is currently worth a lot less than you do?
- Do you want to hold onto your equity as long as possible, until your company is worth a lot more in the marketplace?
- Do you worry that investors will control you and eventually control the company?
- Do you worry about your privacy and freedom to operate, with investors involved in every decision?
- Would you like your investors to be company boosters instead of in continual conflict with you (a win-win relationship with you)?

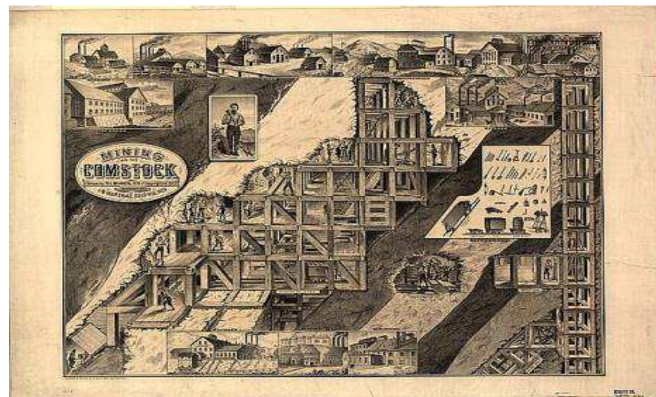
Do any of these issues sound familiar to you? If so, join us on a brief journey through space and time to a funding conversation that might have happened:

The place was the eastern slope of Mount Davidson, near Ophir, Nevada, and the year was 1859. Gold and silver had been found in rich deposits underground that resembled plums in a plum cake, sweet and thick. The earliest mining

claim was pursued by Henry T. P. Comstock. The find is known as the Comstock Lode.



"The miners who discovered the mines, and the investors who bought their claims, did not know whether they had made a small or large strike. The size, richness and cost of exploiting a buried ore body is very hard to estimate even today. All of them knew they did not have the money or expertise to investigate the strike thoroughly."



Ultimately, the Comstock mines went thousands of feet deep (over 1000 meters) involving intricate underground wooden structures to shore up the loose soil.

"The size of the strike and its potential value would take many years of extensive work by thousands of miners and the investment of millions of dollars—which none of them had. Weighing the chances of gain and loss as they stood in 1859 the prospectors had no cause to reproach themselves with lack of foresight."

They also lacked financial experience. Comstock couldn't find financing to dig deeply so, "Henry later sold all of his Ophir holdings to Judge James Walsh for $11,000. ...In September 1870, … he committed suicide with his revolver." Most other early owners suffered similar fates.

We want to help you avoid disappointment like this.

Later, "Comstock's silver mines were criticized for the way that their share prices were manipulated on the San Francisco stock exchanges, and for the way that insiders skimmed the profits to the detriment of the common shareholders. … Mining company managers also issued contracts to themselves for timber, and water. Ore from the mines was commonly processed by ore mills owned by the

company insiders, who were accused of keeping part of the silver they extracted for themselves, and refusing to make an accounting."

Citation: Comstock Lode. (2015, February 5). In Wikipedia, The Free Encyclopedia. Retrieved February 26, 2015.

So this whole method of financing, selling and trading ownership shares in the mining companies, turned out to be disastrous for most concerned. Had Henry Comstock a crystal ball he would have had the following conversation with an investor:

> Henry: "In exchange for your financial help to acquire the equipment and labor I need, I'll grant you a 25% ownership in my mining claim."
>
> Investor: "I believe there's gold and silver here, but I don't have any way to predict how deep it goes or how rich it is, and I don't really know what it will cost to mine deep underground here, what with the loose soil, dripping water, and all. I'll need 45% ownership or I walk."
>
> Henry: "That's ridiculous. I'm going off to see Mr. Wells, the banker. He's got more sense than you."
>
> Investor: "But don't you understand? This mine could very well cost you more to dig than the revenues from sale of gold and silver

ore. So the claim would be worthless. We might never be able to sell it. Even Mr. Wells would feel the same. I've got to have a large enough share to really win, to compensate for the chance of losing everything.

Henry: "But you don't understand, there's no chance you'll lose your money."

Investor: "If you'd seen all the sure-things I've invested in, you wouldn't say that. The problem is that I've just got to wait so long before you can sell the mine. It could be many years. I won't know for all that time if I'm making any money at all. If there was only some way to get paid back all along the way, like a loan, but only if you find and sell gold and silver. Then I wouldn't worry whether you ever sell the mine. But that's not what you're offering. In fact, on reconsideration, I'll need 65% ownership."

Henry (thinking): "Greedy SOB."

Investor (thinking): "Stupid fool."

Henry: "I know the mine is worth a lot in the end. I just know it. I'll never stop digging until I make a profit. So I can't see giving away 45% let alone 65% to anyone, for all my work and sweat. Not a chance."

Investor: "Ok, then, let me make you another offer. For the same amount of money, let me share in the gross revenues, whatever they are, all along the way. Then we're in this together."

Henry: "What exactly do you mean?"

Investor: "For example, I'll give you my financial backing for the amount you need. Then you simply pay me say 10% of the gross revenue you receive from sale of gold and silver ore every day."

Henry: "Hmmm. Let me think 'bout that."

Investor: "While you're thinking, remember that with that plan, I won't be much worrying about the salary you're taking or the rich deal you give your buddy for mining equipment and lumber. I'll only care about the gross sale of ore."

Henry: "So, you won't be bothering me much?"

Investor: "I'll leave you alone, so long as the ore sales go through Mr. Wells' bank over there. He'll just pay me my share each day and we'll stay out of each other's way."

Henry: “So you’ll do this deal today? I won’t have to keep shopping around for financial support for months, while other miners undercut my claim?”

Investor: “I’ll do it and let you get back to mining.

Henry: “Yahoo!”

Investor: “And one more thing, since my share comes off the top line revenues, I’ll go visit with some ore buyers tomorrow who will give you a higher price than most. You’ve given me good reason to help in this way.”

Henry: “Sounds good. I can use your help in that way.”

Investor: “Don’t worry. I’ll be making a lot more if I help get you a better price.”

Henry: “OK, then one last thing. I’ll pay you 10% for the first five years, and then, when the mining starts getting both really expensive and really large, I’ll reduce the revenue share to 5% for the next five years, and then 2% for the next 20. With that kind of plan, you’ll be able to sell the whole agreement to Mr. Wells after five years and retire. Will you accept that?”

Investor: “You’re smarter than you look young man. OK, it’s a deal.”

Now, so far as we know, that conversation never took place. However, it should have and ones like it are now commonplace in the mining industries and in oil and gas extraction. Most players in the so-called “extraction” game have learned their lessons from those early days of folly.

These lessons learned in the world of mining and drilling are now seeping into the worlds of high technology, life sciences and other innovative businesses areas. Since many new businesses today command high profit margins, the lessons learned from financing mines and oil wells are ever more applicable.

To access a summary of the main points this book, click here: Summary.

What follows is written from our perspective as both entrepreneurs and as investors. We’ve sat on both sides of the table – a frustrated entrepreneur and a wary, untrusting investor. It was that very experience of sitting on both sides of the table that led us to discover “Revenue Royalties” – the proven funding method that bridges the divide between entrepreneurs and investors once and for all.

Let us emphasize the word “discover” rather than create. The author of this eBook began to advocate an idea named Revenue

Participation Funding about five years ago as a member of Tech Coast Angels and as a blogger. This grew out of his frustration as an investor unable to get liquidity for a decade after buying equity in startups, and also frustrated by the continuous conflicts with founders over valuation, dilution, exit timing and strategy.

More recently, Intelliversity discovered that Wall Street legend Arthur Lipper had been advocating this solution since the 1980's for innovative businesses. You can find it described in Mr. Lipper's landmark book, Financing and Investing in Private Companies (Probus Publishing, 1988.) In 2010, he received a U.S. patent on key methods of implementing this method, now called Revenue Royalties (or Revenue Royalty financing) as a powerful investment vehicle. So "discovery" is an accurate description of Intelliversity's relationship with Revenue Royalties. We hope you have the same joy of discovery while reading this short guide.

Before explaining Revenue Royalties, it's important to understand why selling equity in your company might not work.

Why selling equity (aka stock or ownership) often does not works.

Most entrepreneurs believe the ideal way to finance their company at an early stage, before bank loans are readily available, is to sell stock or equity – that is, to sell a percentage of the ownership of the company. You can still do

this in cases of very fast growing companies in some niches such as computer software. To do this, your investors have to be confident you have a good chance to sell the company (or take it public) within a relatively short period of time, typically three to five years. In other words, investors have to believe your "exit strategy". This gives them a shot at a "home run" – i.e. very large returns on their investment.

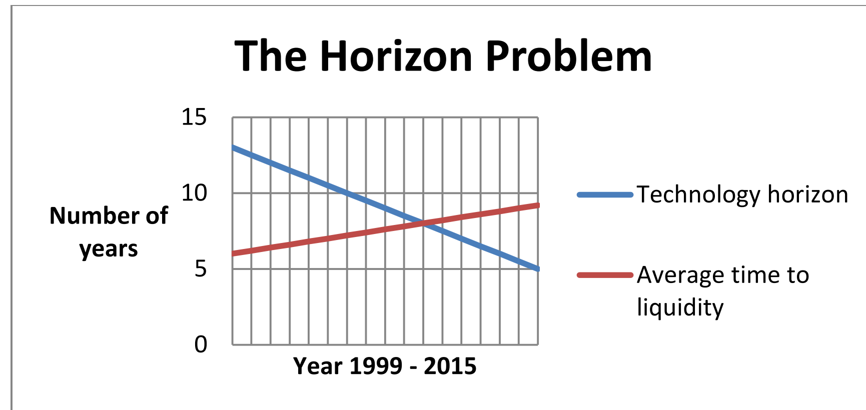
This still works in some sectors, the ones typically funded by venture capital funds today. Will it work for you and your business? Quoting Forbes Magazine, July 22, 2013, by Dileep Rao:

> "The reality is that most ventures do not qualify for venture capital and never will. According to the Small Business Administration, about 600,000 new businesses are started in the U.S. each year, and the number of startups funded by VCs was about 300. This means that the probability of an average new business getting VC is about 0.0005, and it also means that 99.95 percent of entrepreneurs will not get VC.
>
> Are your odds better if you are an existing venture? It does not seem to change much. More entrepreneurs may get VC, but the proportion seems to be about the same. Most VCs like to invest in ventures after the potential has been proven. In the first quarter of 2012, only three percent of VC funding went to startups. So about 97 percent goes to ventures on a post-startup basis, and the number of ventures funded increases to about 3,000-3,500."

What about financing by angels (high net-worth individuals)? These statistics vary widely, so we'll speak from our direct experience as members of Tech Coast Angels, San Diego chapter. (Both founders of Intelliversity have been members.) Over a period of years, we helped review about 30 deals a month or about 600 deals over two years. Total number of deals funded during that time by the chapter were about 20 -- or 3%. 97% had to find funding elsewhere or never found funding beyond family, friends and personal resources. My guess is that no more than 10% of the companies that applied eventually found outside financing from some source, but it could be as low as 5%. Very few companies get angel financing from people they don't already know, let alone VC financing.

There is a way out of this quandary for many innovative companies (Revenue Royalties), but before explaining it, it's useful to answer the question, was this difficulty in getting outside financing for young companies always true? We can say from experience that these statistics were somewhat more favorable to entrepreneurs prior to the dot-com bust in 2000. What changed?

The change in the economy since then is not just a couple of recessions. It's more fundamental than that and more permanent.



The above graph represents our subjective experience, but we've verified this through countless discussions with other investors. The problem is simply that technology is changing more rapidly every year. The rate of change of technology is accelerating.

Think about it. Twenty years ago in 1995 (if you were of thinking age at that time), you were probably comfortable (right or wrong) imagining the world ten years ahead in say 2005. The Internet was a dial up modem. Mobile phones were bricks. Most of us imagined these tools smaller and faster in 2005, but not fundamentally different.

Fast forward to 2015. Are you comfortable imagining the world in the year 2025? Robots everywhere building homes and fixing potholes? Cell phones replaced by inplants? We'll bet you're not comfortable betting on the world in 2025.

Yet, the average number of years it takes to secure a liquidity event (acquisition or public offering) has increased to nine years now and

may continue to increase. Some companies are purchased quickly for their strategic value (think Instagram) but most are forced to prove themselves. Usually, they're not purchased for their technology (as it's changing too fast) but for their customer base and their teams. Most new companies are never acquired; they become lifestyle businesses, which is fine for their owners and managers, not so good for investors.

So the bottom line is, investors can't predict when a company will be acquired, if ever. Most important for you, investors now know this. They know that buying equity in a company is usually a crap-shoot. Here's what the author recently wrote in an article for Angel Investor News:

> "Knowing this, investors are increasingly insecure about every investment and compensate by assembling large portfolios and follow increasingly rigid standards of selection. We ignore most businesses presented to us because the odds of an exit seem too long. Then we demand large shares of ownership, knowing that most will never pay at all. In the end, your business probably does not receive funding. You're dreams lie in tatters.
>
> "The answer is to stop selling equity. Start selling a share of revenue - a share of the future top-line revenues of your company.

Selling your future revenues instead of equity is known as "Revenue Royalties," "revenue participation," "revenue sharing," "synthetic royalties" or "revenue-based finance." This structure is now increasingly well accepted in the angel and fund communities.

"Why does it work in today's fast-paced world? With Revenue Royalties, investors appreciate that:

1) liquidity (i.e. cash coming back) begins almost immediately, and

2) liquidity does not depend on an exit event that may never occur.

"It's all about liquidity. Liquidity is built into the plan. Through built-in liquidity, Revenue Royalties turn long-term uncertainty into near-term certainty. This makes a real difference to investors.

"I've recommended Revenue Royalties to a number of companies in the last few years and more than half have succeeded in raising all of the capital they needed, and quickly. This can't be a coincidence. Investors do sit up and notice.

"In conclusion, purchasing equity in all but the most explosive or proven companies seems like a highly

speculative gamble to most smart investors today. So they avoid it or offer unattractive terms to you, resulting in no funding at all._ Most investors want a way to:

1) Reduce the likelihood of losing their investment, AND,
2) Get the cash flowing back to them swiftly."

The conclusion you may draw from the above article is simple: many investors need and want to invest in Revenue Royalties. Your company can benefit from this movement.

You may not be convinced that this movement is large enough yet to put cash into your coffers. The primary alternative for most young businesses is selling equity (stock or ownership.) For that reason, before we present the details of Revenue Royalties as a way to obtain financing, consider the other reasons why selling equity in your business may be a problem for you now:

More problems with selling equity

Problem #1: Valuation

When they purchase equity, investors have to agree with you on what the company might be worth if sold at some future date, and what the chances are of being sold at that price. This is

one key element that determines the current value of the company. Figuring this out is a process called “valuation.” The problem is that this agonizing process can take four to six months even after you have located interested investors, and quite often you will never agree on the valuation. While they haggle, you and your team starve.

More times than you can imagine I’ve seen entrepreneurs who believe their company is worth about $10,000,000 right now, just after launch, while investors believe the company is worth only $2,000,000 or less. It takes a long time, if ever, to bridge the difference. Why the huge difference? See Problem #2.

Problem #2: Percentage of ownership

Ownership percentage has two main meanings to investors: 1) it gives investors some control over major company decisions, such as when to sell the company or take in other investments; and 2) it can give investors a big win on sale of the company, to compensate for the many deals that never perform as expected, and companies that never get sold. For these reasons, they want a significant share of ownership, usually above 20% and often 40% or more, and usually a seat on the Board of Directors as well. Do you want to give away that much now?

For the above reasons, investors typically know in advance what percentage of a company they want to own. This affects the valuation. If an investor wants to own only 10% of your company for $1,000,000, they will tell you the company valuation is $9,000,000 before the investment (the "pre-money" valuation.) However, if an investor wants to own 25% for their $1,000,000, then the pre-money valuation is only $3,000,000. This is why pre-money valuations seem to be much lower than what you think the value should be.

There is a natural disagreement about the percentage of your company investors should get: <u>If they get more, you get less.</u> If you have less, you have less to sell to future investors if you ever need them. You have less to share with key team members, and, most important, when you eventually sell the company, there is less of a reward to you at the end of the hard-fought game. <u>It's natural to want to hold onto as much equity as possible, or even all your equity, until later.</u> So you may resist the unattractive deals offered to you, and this will delay or prevent receiving the funds you need.

The way around this disagreement is to offer alternative forms of investment that don't involve selling equity at all, at least until the company is further along in growth. Selling Revenue Royalties is an attractive alternative. <u>Selling Revenue Royalties allows you to retain</u>

company stock until such time as you can attract investment without giving up a large percentage of equity – i.e. until such time as the company's perceived valuation is much higher.

Revenue Royalties is a solution

A faster path to funding

The offer of Revenue Royalties attracts investors to companies, projects and non-profits that can't sell equity, or can't sell it at a price acceptable to you. Even if you can sell equity, Revenue Royalties eliminates the battles and the conflict. It eliminates the valuation process. Even if you can sell stock, it's faster and easier to find interested investors. They get repaid quickly and with reduced risk of losing their principal. You get the money needed to survive and grow – win-win. Here then are the main reasons why investors often prefer Revenue Royalties over purchasing equity:

Reason 1: **"Built-in liquidity" -- Investors start receiving payments right away**

Payments usually begin in the first few months or the first year or two, depending on agreement and when revenues begin to flow. We call this "built-in liquidity."

Reason 2: **Investors experience less fear of loss**

There's a lower probability that the principal investment will be lost because the investor does not have to wait for sale of company or public offering, which may never occur or which may take a decade or more. When investing in Revenue Royalties, the investor typically receives back the principal in a relatively short period of time, often three to five years.

That is a shorter time in which the investor's capital is exposed to loss, and his exposure decreases each time he receives a royalty payment.

Reason 3: **Investors need only believe your revenue projections**

Investors need only believe your potential to generate revenues (or contributions and grants for non-profits.) They don't have to believe that you can sell your company or go public. They don't have to believe your exit strategy. You don't even need an exit strategy. Investors don't even have to believe you can make profits any time soon, though they do have to believe that you can sustain a revenue-generating operation; significant margins are needed to pay the royalties along with all your other expenses.

Reason 4: **Investors do not need to agree on valuation or percentage of ownership**

You will more than likely actually find investors with terms you can live with. With Revenue Royalties, you are not giving a percentage of the company, not 10%, not 40% -- no percentage of ownership of the company at all. You hold onto 100% of the ownership of the company. So there's no need to agree on the percentage of the company the investor is buying or the value of the company.

This is assuming you are already generating revenue or have a very good reason to believe you will in the future. If so, chances are you can find investors who'll be interested in participating in a portion of your revenue. You don't have to be a rock star in your industry. All you need is revenues -- now or on the horizon -- and a believable plan to make them grow with financing. This means that your search for investors will probably be short, sweet and rewarding.

A caution of about profit margins: they need to be significant, in order for revenue royalties to work well. Paying a 5% royalty on gross revenues will cut directly into your operating margin, so a sound practice is to be certain that the investment you receive will more than recover the profit margin you sacrifice.

This could be achieved in many ways -- for example through increased efficiency, expanded markets, through the development of new

products and technologies, through acquisition of a competitor.

A company with very narrow operating margins that cannot easily be expanded should probably not consider revenue royalties as a method of financing.

Reason 5: **If you do sell your company, investors get a home-run anyway**.

Every Revenue Royalty agreement should contain a home-run clause, often called a "redemption" clause. This allows owners to sell the company with compelling returns both to founders and royalty investors. More on this later.

Selling Revenue Royalties is easier

Vince Lombardi is considered the greatest football coach of all time. Interestingly, Lombardi's Packer teams ran about ten offensive plays. That's it! Yet they won five NFL championships and two Superbowls. Lombardi believed – and proved – that completely mastering a few simple plays – running them to perfection – would be more effective than trying to be merely "good" and run many, many more plays. Lombardi's Packers ran the same few plays over and over, daring the other teams to stop them. Most couldn't, even when they knew exactly what was coming.

Selling Revenue Royalties as a funding method is like that. It's not complicated. But to be effective it needs to be done correctly. Master a few fundamentals and you'll be on your way to the financial goal line. Selling stock and other types of complex funding mechanisms might work for you someday. Selling Revenue Royalties is simple and fun once you master the game.

We've spoken to a number of investors who put money regularly into companies based on Revenue Royalty financing. We've also spoken to a number of companies who have received investment using this method. All agree. The Revenue Royalties process is faster, easier and lighter than selling stock even if you could. One such fund tells us they regularly complete investments in two to six weeks through an automated process. It can be that fast, though there are no guarantees.

What do you have to gain?

If you take action now, and learn how to sell Revenue Royalties for your company:

- Your business, project or non-profit will have the funds you need to promote your brand and grow
- You'll have the space and time to grow and fulfill your dreams and those of your family and team.

- You'll be able to hire the additional team members you need to take some of the burdens off your back.
- You'll be able to expand the business nationally or globally and get the exposure you deserve.
- You'll be able to develop and introduce the many new ideas you're itching to share with the world.
- Your creations will have the chance to see the light of day and achieve the recognition they deserve.

The future can be bright. The point we're making is that, unless your company is one of the highly unusual few, we believe you're more likely to gain the above benefits by selling Revenue Royalties and you'll get them faster.

To go directly to learning how to make an offer to investors, click here: Offer

Later in this eBook, we'll describe a number of other reasons why raising capital by means of Revenue Royalties may be a better choice. For now, we'll sum up with sound advice for most companies:

***STOP* SELLING EQUITY**

***START* SELLING REVENUE ROYALTIES**

Who we are

You can have confidence that the team at Intelliversity knows what they are talking about and cares that you succeed.

Intelliversity is a not-for-profit 501(c)3. We call it "The Leadership Academy for Entrepreneurs – Led by Investors." The founder and president, Robert Steven Kramarz and co-founder Ravi Bhola are investors as well as longtime entrepreneurs in technology. More recently, Wall Street luminary Arthur Lipper joined the team as Intelliversity's Chairman of the Board of Advisors. Our backgrounds are found at the end of this eBook for your reference.

We also have experience as investors in, and managers of, venture capital firms and other investment funds. We've each been on the boards of a number of successful non-profits. In addition, we each have extensive experience in leadership consulting for both businesses and non-profits. We understand the dynamics of the relationship between founders and investors. We are saddened by the frequent animosity or just inability to work together to build their enterprises. <u>We want to see investors and executives working together to promote their companies, not working against each other.</u>

Most important, we care about the future of entrepreneurship and entrepreneurs like you. We are alarmed by the fact that no more than 3% of companies that seek financing from angel groups or venture capital funds ever get funded, and only about 10% of those ever sell their company and pay their investors back. And even for those that do, far too much time and struggle is expended raising capital rather than growing the business and inventing new products or services or changing the world. This is not a formula for real prosperity. We want to see you, your company, your family, and your community win. Now you have the tools to enable you to win.

Intelliversity began to write about "Revenue Participation Funding" on its popular blog in 2011. (Originally, we called it "Participation Funding.") Arthur Lipper, as we've said earlier, has been recommending this method of financing since the 1980's, now calling it "Revenue Royalties" which is the name we have now adopted as well.

We have continued to write about, develop, refine, and document cases of successful use of Revenue Royalties, under any name, ever since. We have also begun to see investors and funds nationwide popping up and investing in many projects over the past few years using revenue sharing plans of one sort or another. The ideas have been developed further by consultants and

attorneys whose work has been collected by us. You can now take advantage of this new movement in financing innovation and growth.

How does Revenue Royalty financing work?

With Revenue Royalties, your investors provide you with a certain amount of capital. In return, they receive a pre-defined percentage of future top-line sales revenues (or contributions in the case of non-profits.) Your investors continue to receive that pre-defined percentage of revenues for a pre-defined amount of time or until a certain amount of money has been paid back. There are other formulas that we'll get to in a moment.

You don't have to share all revenues. You can limit the sharing to particular products, particular projects, or particular revenue-generating events. There are many possibilities. Usually, for simplicity and to make investors most comfortable, companies offer simply a percentage of top line revenues. This way, if your sources of revenue change later, investors have confidence they will still be paid.

The use of Revenue Royalties to finance a business is similar to many licensing agreements.

To illustrate, suppose you were to license a patent from an inventor intending to market it.

Normally, the inventor would request, and you would grant them, a pre-defined percentage of the revenues that would result, say 2%, 5%, 10% or whatever you agree to. Chances are you wouldn't give them any ownership in your company. You might offer the inventor a percentage of the profits resulting from marketing the patent. It's therefore customary for inventors to request and receive a percentage of topline revenues.

Revenue Royalties are handled in the same way, except that instead of a product or a book, the other party is providing capital for your company to grow. You pay them back as a percentage of total revenues rather than revenues from a particular product. (This is why this system is called "Revenue Royalties.")

In the next section, we get into more detail about the elements of a Revenue Royalties agreement.

The Elements of a Revenue Royalties Plan

There are four essential points in any Revenue Royalty plan and agreement: That's great to know, you may think, but how do I determine the right amounts for each of these?

- The investment amount;
- The royalty percentage;
- The length of time that royalty payments occur;
- What (if anything) investors hold as security.

The following comments will help you make the right decisions:

The right investment amount:

Investors will usually expect to hear that funds they invest are sufficient to enable your company to generate the amount of revenues that you project. So ask for enough.

If you believe that you will probably need an additional round of investment to achieve the projected revenue, we recommend you disclose that fact.

We strongly advise you ask for enough to reach cash flow break-even – where the cash coming in is regularly larger than the cash going out each month. This ensures that, if no additional capital can be found, the company can continue operations.

Unless otherwise agreed, you will control how money is spent. However, it's fair to say that investors will expect that you use their funds primarily for revenue-generating activity, unless otherwise agreed.

The right royalty percentage(s)

The amount of money paid back to investors each year is the agreed royalty percentage multiplied by total topline revenues during that year. You anticipate that revenues will be growing, so the amount of money paid back to investors in each subsequent year will be growing also.

Select a royalty percentage that: 1) your company can live with (within its available profit margins), and 2) that will pay the investor(s) back their entire principal over the number of years that many investors find attractive, often between three to five years.

After you've paid back the principal amount invested, the royalty payments continue because that is how the investors make a return on their investment. However, you have the option, regarding those later years, to agree in advance to a lower royalty percentage.

Thus, you and investors can agree to a series of two or three declining royalty percentages that last many years, as long as reasonably foreseeable, say 10 to 20 years. The

question of how long should the royalty agreement run is covered below. Here is a sample though not necessarily recommended plan:

Year	Royalty Percentage
1	5%
2	5%
3	5%
4	5%
5	3%
6	3%
7	3%
8	2%
9	2%
10	2%

The right amount of time for royalties to run:

The amount of time over which royalty payments continue is subject to negotiated agreement. If you agree to pay investors for a long period of time, say 11 to 20 years, investors should be willing to accept a lower royalty percentage because there is a longer opportunity for recovery of capital and payment of a return, and they expect your revenues to grow over that length of time. You benefit with a lower royalty percentage.

A longer time period may also give the investor the opportunity to sell the remaining years of the Revenue Royalty agreement to another investor, and cash-out. For all the above reasons, we suggest a relatively long time period to pay royalties, say 20 years.

Important: This does NOT stop you from selling the company earlier. Most owners of innovative companies want to and plan to sell their companies in a few years. A 10 or 20 year royalty agreement should allow an early sale and even facilitate an early sale. We explain how this is done later.

In the first example below, we've created a proposed 10 year royalty plan:

Year	Projected Revenues $	Royalty Rate	Royalty Distribution $	Cumulative Royalties $	Percent Or Multiple of Cost	Compound Annual Rate of Return	IRR - Internal Rate of Return
1	500,000	7%	35,000	35,000	3.50%	-96.5%	-96.5%
2	1,000,000	7%	70,000	105,000	10.50%	-67.6%	-71.73%
3	2,000,000	7%	140,000	245,000	24.50%	-37.43%	-42.31%
4	4,000,000	7%	280,000	525,000	52.50%	-14.88%	-17.52%
5	7,000,000	7%	490,000	1,015,000	1.02X	0.3%	0.36%
6	10,500,000	5%	525,000	1,540,000	1.54X	7.46%	9.68%
7	15,750,000	5%	787,500	2,327,500	2.33X	12.83%	17.19%
8	23,625,000	2%	472,500	2,800,000	2.8X	13.74%	19.92%
9	29,531,250	2%	590,625	3,390,625	3.39X	14.53%	22.22%
10	36,914,063	2%	738,281	4,128,906	4.14X	15.23%	24.16%

There are a few key points to make about this plan that illustrate how to design any revenue royalties plan:

Your revenues should be credible for your business model and industry. In this example we anticipated a doubling of revenue within the first 4 years, then settling down to a 50% revenue growth rate for 3 years, followed by 25% revenue growth for the last 2 years.

The column "% or multiple of cost" represents a common way that investors think about their results. At the end of the 10th year, the investors will have received a cumulative amount of $4,128,906, which is a little more than 4X their proposed original investment of $1,000,000. If the investors are satisfied with 4X received over a 10 year period, given whatever risks there are with this company, then the investors might buy this plan.

The second column from the right, labeled "Compound Annual Rate of Return," is another way of stating the same results. This column gives the compound annual interest rate that would be needed to generate the same

financial result by putting the invested $1,000,000 into a fixed-interest bearing financial instrument. In other words, if you want to start with $1,000,000 and end with $4,128,906 in the bank after 10 years, a compound annual interest rate of 15.23% will do the trick. This is considered a high rate of return for most investment funds.

The last column gives the “Internal Rate of Return” (IRR). This illustrates one of the inherent advantages of a Revenue Royalty investment. The IRR at the end of 10 years is over 24%. Note the 24.16% IRR is higher than the 15.23% Rate of Return in the adjacent column. This is because the IRR takes into consideration that returns were paid to investors continuously over 10 years, not as a balloon payment at the end. The IRR reflects the fact that liquidity is achieved continuously during the plan years. Therefore, the IRR is a more accurate statement of the actual projected returns on investment of this plan.

Now suppose we create a plan that runs 20 years instead of 10. The results might look like:

Year	Projected Revenues $	Royalty Rate	Royalty Distribution $	Cumulative Royalties $	Percent Or Multiple of Cost	Compound Annual Rate of Return	IRR – Internal Rate of Return
1	500,000	7%	35,000	35,000	3.50%	-96.5%	-96.5 %
2	1,000,000	7%	70,000	105,000	10.50%	-67.6%	-71.73%
3	2,000,000	7%	140,000	245,000	24.50%	-37.43%	-42.31%
4	4,000,000	7%	280,000	525,000	52.50%	-14.88%	-17.52%
5	7,000,000	7%	490,000	1,015,000	1.01X	0.3%	0.36%
6	10,500,000	5%	525,000	1,540,000	1.54X	7.46%	9.68%
7	15,750,000	5%	787,500	2,327,500	2.33X	12.83%	17.19%
8	23,625,000	1%	236,250	2,563,750	2.56X	12.49%	18.63%
9	29,531,250	1%	295,313	2,859,063	2.86X	12.38%	19.97%
10	36,914,063	1%	369,141	3,228,203	3.23X	12.43%	21.2%
11	42,451,172	1%	424,512	3,652,715	3.65X	12.5%	22.23%
12	48,818,848	1%	488,188	4,140,903	4.14X	12.57%	23.09%
13	56,141,675	1%	561,417	4,702,320	4.70X	12.65%	23.82%
14	64,562,926	1%	645,629	5,347,949	5.35X	12.72%	24.43%
15	74,247,365	1%	742,474	6,090,423	6.09X	12.8%	24.94%
16	85,384,470	1%	853,845	6,944,268	6.94X	12.88%	25.38%
17	98,192,140	1%	981,921	7,926,189	7.93X	12.95%	25.75%
18	112,920,961	1%	1,129,210	9,055,399	9.06X	13.02%	26.06%
19	129,859,105	1%	1,298,591	10,353,990	10.35X	13.09%	26.34%
20	149,337,971	1%	1,493,380	11,847,369	11.85X	13.16%	26.57%

Because of the longer period, the proposal allows for a 1% royalty during the later years instead of a 2% royalty.

This plan pays a slightly lower return in the first 10 years, but makes up for that with an extended period of steady returns in excess of 20% per year.

Even this way of explaining returns does not express the full benefit to the investor, at very low cost to the company. In this case, the investor is receiving an amount about equal to

their original investment back in each of the last five years, having already received the original investment back in full by the 5th year. This is a huge opportunity for the investor, at very low cost to the company.

The above illustrations were carried out using calculation tools supplied by British Far East Holdings, Ltd., under the management of Arthur Lipper. These tools make easy work of experimenting with a variety of plan variables (rates, length of time, etc.) as well as modifying revenue projections, in order to create plans attractive to investors that meet company financial needs. These calculation tools, along with coaching in use, are available through Intelliversity training programs.

The right security

What investors hold for security is also subject to negotiation. Very often, the only asset worth holding for security is intellectual property (IP) such as patents and trademarks. Suggestions for handling security of this kind are available through Intelliversity training programs.

There is also security in how you agree to pay investors. You will probably agree to pay investors on a daily, monthly or quarterly basis, not annual basis. More frequent payments will be perceived as more secure.

Use of a "lockbox" or similar arrangement will be perceived as providing security. In such an arrangement, your company's bank is instructed to pay royalties directly to the investors, deducting the royalties from revenues received. This can be done on a daily basis creating continuous liquidity for the investors and a great deal of confidence. A unique effect of this arrangement is that the royalty investors receive their payments before any lender or vendor, which is attractive to investors in revenue royalties.

On the other hand, if investors have prior history with company management and are comfortable with a more relaxed relationship, you may agree to make payment of royalties on a monthly or even quarterly basis. This allows your company more flexibility in managing cash flow. Examples of language used in Revenue Royalty agreements will be found in other educational material provided by Intelliversity.

How do you provide credible revenue predictions?

At the heart of any Revenue Royalties investment is your ability to predict future revenues so that investors find your projections credible. To the degree that investors are confident in your projections, there is less perceived risk. Investors will then accept a lower return on investment.

If investors accept a lower return on investment, then the desired royalty percentage will be lower; more money will stay in the company and less will go to investors to cover their risk. That's why this section is important.

There are a number of factors that affect the credibility of your revenue projections. These factors differ from investor to investor. Here are typical factors that most investors will find important:

- The stage of development of your company affects confidence in your revenue projections. The further along in this process, the more confidence investors will have in your projections of revenue.
- For pre-launch companies, taking steps such as market research and product testing will increase confidence.
- Being in a market sector or industry that is large and growing increases confidence in revenue projections.
- A strong team increases confidence. Team strength is in the "eye of the beholder", so the following are generalities that in our experience apply to most investors. A team with C-level executives with a track record

of successful experience in the same market sector will increase confidence in your revenue projections. Particular strength and experience in marketing and sales on the management team will also have this effect.

- For many investors, it is acceptable to include key team members who are named in the business plan but not yet hired. Whether hired or not, it's better to have a team where the members have been working together for some time.

- Barriers to entry (barriers that prevent or delay other companies from competing) increase confidence in revenue projections. Most believable barriers are patents, trade secrets and exclusive alliances or business relationships that ensure a leading position for years.

- The degree of innovation of the product or service provided by your company may increase confidence in revenue projections, if other factors are also in place.

- The presence of a clear problem that your company addresses and solves may increase confidence. In contrast,

companies whose product or service is optional for the consumer, and therefore driven by fashion, taste or popularity, such as entertainment ventures, inspire less confidence in revenue projections.

- Relatively high gross profit margins may also increase confidence in revenue projections, as this leaves room for increased expenditures on marketing if necessary.
- Writing a business-plan which justifies revenue projections on a “bottom-up” basis increases confidence. “Bottom-up” refers to a plan that describes in detail how sales, support, production, and marketing can be ramped up month by month to achieve the projected level of revenue.
- The support of experienced advisors (business attorney, patent attorney, investment banker, accountant, market researcher, regulatory expert) will increase confidence.

The most important factor in the credibility of revenue projections is the size and rate of growth of revenues relative to other companies at similar stages, in the same industry. You increase credibility by projecting moderate

revenue growth, in the middle range of comparable companies.

Investors experienced with Revenue Royalties would prefer revenue projections that are moderate relative to other companies because their returns will be higher if you over-achieve. This makes it easier for you to attract and close a round of investment.

It's important to observe here that generating credible *revenue* projections is MUCH easier than generating credible *profit* projections, or a believable exit strategy, exit timing and exit valuation.

Investors naturally perceive your profit and exit projections as highly speculative. Since projecting revenue is inherently less uncertain, therefore less risky, investors who invest in Revenue Royalties will require lower rates of return. This increases the long term financial rewards to you as company founder or owner.

What are the hidden benefits of Revenue Royalties to you and your company?

With Revenue Royalty financing, there are a number of compelling benefits to you and your company as compared to selling equity or obtaining a loan, assuming you could get the funds needed in these ways. Let's assume for the

moment that you can obtain financing by selling equity or getting a loan.

Larry and Barry are two fictitious business owners created by our advisor, Arthur Lipper, to illustrate financial ideas. What follows is a sample dialog:

Larry and Barry tell why business owners are better advised to sell royalties than selling stock or incurring debt

Larry: If we can get some additional cash we could either buy our biggest competitor or invest the money to seriously out-market him.

Barry: Things are going OK now. We are profitable and growing steadily.

Larry: Sure but we could grow a lot faster and get much bigger if we had the capital.

Barry: But the banks won't make us a term loan as we are privately owned without a personal guarantee, and our personal net worth won't support a sizable loan.

Larry: Are there other lenders we could go to?

Barry: The other lenders are big enough to borrow from banks at reasonable interest rates and then mark up the interest rates to finance company rate levels, and we don't want expensive money, especially not with all the negative covenants usually required.

Larry: Ok, so it's not practical or even possible for us to borrow on attractive terms. What about selling stock in our business?

Barry: We don't have enough time for me to tell you all the reasons we don't want investors as shareholders in our company, even if we could find some who would buy our stock at a fair value, one which took into consideration the good things we could do with the new money.

Larry: So what's so bad about having investors in our business?

Barry: For starters, people only invest in companies believing they will be able to sell the stock purchased for a profit at some later date. Therefore, they want us to earn and declare maximum

profits every year so they can get the benefit of our reported maximized earnings when they sell.

Larry: So what? Won't we be making much more money if the money we get from the investors results in higher revenues and profits?

Barry: Yes, we can do well with the additional capital but what about the loans we have taken from the company at low interest rates to buy our homes and cars? Would the investors also approve of the bonuses or additional loans we take when we need money?

Larry: Why would they have to know or approve?

Barry: Because once we, who are the directors of the company and control the business, take in additional capital from selling stock, we become fiduciaries and are obligated to do everything in the best interest of all of the owners of the business, including the new investors.

Larry: So why would the investors care or be hurt as we are all in this thing

together, and if the company wins they win?

Barry: That is not the way they or perhaps even the law would see the things we can do for ourselves as private company owners. Remember they invested with a view to selling at a higher price and want us to declare the highest profits possible, even though that means we will be paying the highest possible taxes.

Larry: Ok, so we will have to pay ourselves more and pay the personal income taxes. What else can be problematic in having investors, who will be people we may know initially, but not necessarily if they eventually sell to other investors?

Barry: You know that new product you want us to invest in or the not yet profitable company you want us to buy or the new high priced marketing manager you want us to hire or the establishing of the new international sales company which you and I believe will be, in the long-term, great for us but will reduce our present profitability and therefore may not be favored by the investors?

Larry: What if we try to get some money from the venture capital firms we keep reading about or other professional investing groups? Won't they be more understanding of the longer-term benefits we are trying to create?

Barry: Perhaps, but they will probably want to have a seat on our board of directors and all sorts of interim and continuing financial data. They will also probably want what's called "liquidation preferences" which assure sale of the company. They may also require the inclusion of a "ratchet" term in our agreement with them, which means, if we miss the profit projections we have given to them, they will get more stock for free.

Larry: OK. So where and how can we get additional capital without sharing ownership and reducing our personal and management flexibility?

Barry: I have been reading about Revenue Royalties and am intrigued, as the concept seems to be perfectly designed for business owners. A royalty is a percentage of revenues, not profits, like a share. Therefore, all

the royalty owner cares about is payment of the agreed percentage and the growth of revenues for the period of the royalty.

Larry: Sounds great, but how much do we get, and for how much of our revenues? Also, won't these royalty payments reduce our profits?

Barry: All depends on how well we use the additional capital. We negotiate the percentage of revenues and the length of the period of the royalty. From what I understand, the royalty investor has a minimum Internal Rate of Return (IRR) objective and wants to achieve that IRR with the least risk to the investor and the business owner.

Larry: You mean the royalty owners only own the agreed percentage of our revenues which we have sold to them and do not own any of our company?

Barry: That's right. They have no ability to vote or otherwise influence or control the actions of management and have no direct interest in our reported profitability. All they want is for us to survive, prosper and continue to pay the royalties to which we are committed.

Larry: How much information are they entitled to, about what we are doing?

Barry: Only to a periodic audit of revenues and whatever else we and they agree.

Larry: Can the royalty investors to whom we have sold a royalty sell that royalty whenever and to anyone they want?

Barry: Yes, as the royalty is fully negotiable. However, they would have to sell to an accredited investor, which would probably be a tax-exempt institution and probably with other seasoned royalties in a package.

Larry: How often do we have to make the royalty payments?

Barry: In the program I have been reading about, the investors get paid whenever we get revenues. It's made to be automatic.

Larry: Can we get out of the deal if we become really profitable or someone wants to buy us?

Barry: The royalties can be made redeemable and we can also try to buy them back whenever we want and have the cash to do so. We could

also try to use debt and our stock to eliminate the royalty. It all seems open to negotiation.

Larry: Even better is that the investors cannot force us into a liquidity event.

Barry: Unless we agree to a sale, merger or going public.

Larry: Ok, let's start to learn more and make contact with the royalty investors. Also, shouldn't we consider investing in royalties of other good privately owned companies or a fund which does so for our own pension fund?

Barry: Yes and I am already doing so -- and isn't that why we are partners?

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Here are some other considerations about the advantages of financing through revenue royalties:

Additional advantages of selling Revenue Royalties as compared to selling equity

When you do sell the company, you and other founders will keep most of the cash – In contrast, if you sell equity now, you may have to

give a huge amount to the equity investors when you sell the company. With Revenue Royalties, you need only share the amount agreed in the "home-run" clause (aka "Redemption Clause") in your agreement, which is a lot less (because the investors took less risk.) Do the math. Call us if you need assistance. <u>This secret alone may save you tens of millions of dollars when and if you sell the company.</u>

> Example: You sell 40% to equity investors for a $2,000,000 investment in year 1. You then sell your company for $100,000,000 in 5 years when you reach $50,000,000 in sales. This costs you $40,000,000. With Revenue Royalties, the redemption clause may require a 5X return to the investors by year 5, which includes royalties already paid. Total cost to you is only $10,000,000. You save $30,000,000. Even if the redemption clause requires a 10X return to investors, you still save $20,000,000.

If you need to sell equity in for more capital, you hold onto your equity until it's worth more – Using Revenue Royalties, you hold onto your founder's equity until the company is worth a great deal more in the eyes of equity-buying investors. If you then choose to sell equity, you will sell a much smaller percentage of the company for the same amount of money. You may have to sell 30% or 40% of the company now to get to the financing needed, whereas if

you sell Revenue Royalties now, you only have to sell 10% or 20% of the company a year or two from now to raise additional financing. This may make the difference between losing control of the company or not in the future.

You can keep your company as long as you like -- You're never forced to sell the company or to do a public offering. You can retain control of your company as long as you require.

No debate and conflict over valuation -- There's no long drawn out, often irresolvable, debate over the valuation of the company.

No loss of control -- You retain full control over the internal operations of your company – salaries, benefits, personnel decisions and strategy. Revenue Royalty investors may not require, and often don't want, a Board of Director's seat. What's more, since they have no ownership position in the company, they don't vote or influence the choice of Board members. In contrast, venture capital firms and many professional angel investors require one or more Board seats. They will also frequently insist on "ratchet" terms in their investment agreements, which increase their ownership position to a controlling percentage if specific financial goals are not achieved.

No loss of privacy – Revenue Royalty investors are less concerned than equity investors over the details of expenses, tactics and personnel decisions.

No conflicts over use of profit – Stockholders may want your company to pay a dividend to them each year if cash flow allows it. This requires that the company retain earnings, defer expansion plans and pay income taxes on those earnings. Company management may prefer to keep investing its cash in marketing, product development, or even executive bonuses. These decisions could create conflict with stockholders. Even minority stockholders can be highly disruptive when these kinds of conflicts occur.

No fiduciary duty to investors – It's little known that companies have a fiduciary duty to stockholders when they sell equity. A fiduciary duty requires that company management and Directors act in the best interest of stockholders, even if they are minority stockholders.

To underscore this point, quoting the website of law firm Stout, Risius, Ross:

"Shareholder oppression claims are important tools available to minority shareholders. … A review of case law reveals certain common conduct that courts are likely to find oppressive... These include:

- Failing to pay dividends when the corporation has the financial wherewithal to do so
- Causing the corporation to pay the majority shareholders compensation

which is excessive and unfair to the minority and/or the corporation

- Paying the majority shareholders compensation amounting to a de facto dividend to the exclusion of the minority shareholder
- Denying shareholders participation in management of the corporation or a voice in decision-making processes …
- Using corporate funds to pay the personal expenses of other shareholders or related parties (such as family)
- Failing to provide financial statements or other information shareholders have a right to receive
- Engaging in acts designed to freeze the minority shareholder out of the corporation rather than give him his fair share of his investment
- Denying a shareholder any return on the shareholder’s equity while refusing to buy-out the shareholder’s shares for Fair Value”

See more at: http://www.srr.com/article/shareholder-oppression-fiduciary-duty-and-partnership-litigation-closely-held-companies

Selling Revenue Royalties instead of selling equity mitigates the fiduciary duty described above. This is a major, if not obvious, benefit. Your company's duties would be limited to those stated by the Revenue Royalty agreement with investors. (Note: since we are not attorneys, this document is not a legal opinion and we cannot predict what a court may rule on this subject.)

Selling Revenue Royalties as compared to obtaining a loan (debt financing)

The conventional way to solve all of the above problems is to raise capital by taking out loans. In fact, most small businesses get started with loans from friends and family, supplemented by some mix of credit cards, home loans, and personally-guaranteed business lines of credit. Even new businesses can qualify for trade financing, such as Accounts Receivable financing, factoring and purchase order financing to handle cash flow issues. After a few years in business, business owners are eligible for additional credit opportunities.

The problem is that debt financing is rarely sufficient to invest in marketing and sales campaigns to grow a business substantially.

However, let's assume for a moment that you can get all the debt financing you want to grow your business. Here are some problems with this approach to financing:

Loans have fixed payments – With rare exceptions, debt payments must be made every month without fail, even if revenues take a dip. In the case of "balloon" loans, the entire loan amount must be paid back at a pre-determined time, even if revenues are not yet sufficient.

With loans, collateral is in jeopardy – Loans that are secured by collateral (such as a home, equipment, business property or vehicles) put the collateral in jeopardy. SBA and bank loans generally often require that business owners not only personally guarantee the loan but put their own homes up as collateral. A lien is frequently placed against the business owner's home. This risk may not be acceptable to you and your family.

Loans are recorded on the balance sheet – Future lenders will be influenced by the amount of debt already in place.

Loans may require financial covenants – Very often, business loans require that a company meet certain revenue and profitability targets, or maintain certain financial ratios, terms of agreement which are called financial covenants. <u>If your business does not meet these targets, the lender can call the loan, forcing you to repay it.</u> This risk may be intolerable to a young business whose revenue and profit margins vary month to month.

With loans, the interests of the lender and borrower are opposed – Lenders have no way to assist you in your campaign for revenues; their only interest is getting paid every month on time.

In contrast, Revenue Royalty financing provides the following more relaxed and even aligned set of terms:

Flexible payments – Payments flex with revenue; they are dependent upon the amount of revenue. During periods with low revenue, payments drop in proportion to revenue. During periods of higher revenue, payments to investors increase proportionately. This is a win-win relationship. It's flexible for you and attracts investors who want you to succeed in building revenues. Unlike the rigidity of a loan, flexibility and patience is part of the deal. You will naturally attract patient investors. Isn't this the kind of relationship you really want with your investors?

If there is any collateral at all, collateral is not in immediate jeopardy – In most cases, investors who buy Revenue Royalties do not insist on collateral such as property or equipment. Revenue Royalty financing is typically subordinate to debt that is secured by such material collateral. You as company founder or owner typically do not have to worry about loss of your home, property or equipment.

Revenue Royalties agreements may specify that the company-owned intellectual property (IP) such as patents are held as security by a trustee or trusted party, to be licensed back to the company for unrestricted use at a nominal fee during the life of the royalty agreement, and to be used by the investors during a possible bankruptcy proceeding. The investor doesn't want to control the patents; that's the company's job. The purpose is to motivate company founders to a higher level of commitment to the success of their venture.

Revenue Royalty financing does not interfere in obtaining future debt financing – We are not pretending to be accountants in making this observation. Revenue Royalty finance does not appear on the balance sheet as debt and thus probably does not interfere with obtaining future debt financing. Please make sure your accountant agrees.

Note: because financing by means of Revenue Royalties require a percentage of revenue to be paid to investors periodically, it reduces profits and thus, in theory, may make future equity financing more difficult to obtain. However, if the financing is used as intended and the company's revenues and profit margins grow, this is probably a moot point.

Revenue Royalty financing imposes light-weight or no covenants at all – Points of

agreement with investors vary, but we've observed that most royalty investors do not require companies to meet revenue or profitability targets or maintain certain financial ratios, or if they do, covenants are not excessively restrictive.

Overall Advantages of Selling Revenue Royalties

Investors may become company boosters – It's worth repeating: This is a free bonus that many companies have experienced after obtaining Revenue Royalty financing. The logic is simple: investors gain immediate cash liquidity whenever revenues increase. Therefore, they are motivated to pick up the phone and influence key revenue-generating relationships such as distributors and major customers. In short, with Revenue Royalties, your investors can become your most effective promoters and evangelists. What could be better?

What matters to you and your business?

Here's an opportunity to check-off the most important reasons ***for your business*** to sell Revenue Royalties instead of selling equity or taking out a loan. Take a moment to review the above explanations if needed and to check off the top five reasons for you:

Compared to selling equity:

I want to:

- **Find investors quickly because payback begins quickly and no exit is required.**
- **Hold onto my equity until it's worth more (no sale of equity, no dilution).**
- **Sell the company in a few years and keep MOST of the proceeds, not sharing up to 40% or more with angels or VC investors.**
- **Or, run the company and enjoy it as long as possible (no exit needed).**

There's likely to be:

- **No conflict over valuation (investors may disagree with me on valuation and still invest).**
- **No loss of control (and no ratchet terms that can increase investor control further).**
- **No loss of privacy.**
- **No conflicts over use of profit.**
- **No fiduciary duty to investors**.

Compared to getting a loan:

Revenue Royalties mean:

- **Flexible payments (lower when revenues drop, higher when revenues take off).**
- **Collateral, if any, is not in immediate jeopardy.**

- **Future debt financing is not impeded.**
- **There are few or no loan covenants that cause the loan to be recalled.**

And in general:

- **Investors may become company boosters.**
- **I get a win-win rather than adversarial relationship with investors.**

What are people saying about Revenue Royalties?

Wherever we go, people want to hear more about Revenue Royalties. At an entrepreneur's conference we attended recently, more than three-quarters of the entrepreneurs who heard about the subject of revenue royalties pressed their cards into our hands. These were entrepreneurs and innovators with companies, ideas, projects, and even non-profits. At an inventors' conference, more than 50% did so. They all demanded copies of our presentations and wanted to learn more about how to actually implement Revenue Royalties.

Investors are equally interested. We know of at least six professionally-run funds that supply Revenue Royalty financing for growing companies, and there are certainly others we've

not heard about yet. There are countless private angel investors who are enamored of the concept as the benefits to investors are profound. Many we find have informally invested with repayments based on revenues, without calling this kind of contract Revenue Royalties. Alternative terms investors use are "revenue-based finance," "revenue participation," and "synthetic royalties" among others. If you google these terms you'll find many references, including Pacific Royalties (www.pacificroyalties.com) with a large library of articles on the subject. As pointed out earlier, Wall Street veteran Arthur Lipper is a clear advocate of this approach and the markets are listening. Here are his concluding remarks:

Comments on the Future of Revenue Royalties

By Arthur Lipper

My prediction is that the sale of royalties will become the primary means of financing privately owned companies. I also believe that increasingly the owners of businesses will seek to retain the full ownership when arranging financing. The recognition of the responsibilities and restrictions of becoming a fiduciary as regarding all shareholders and the surrender of the flexibility and perks of ownership make the sales of ownership interests less attractive.

Indeed, the more successful the company becomes the greater is the satisfaction and reward for the owners, especially those owners directly involved in managing and growing the business.

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Arthur Lipper, Chairman
British Far East Holdings Ltd.

Making the offer

We've reached the limit of what can be presented in an eBook format. Now that you've got the basic idea and see the advantages, there is more to know when seeking Revenue Royalty financing:

How do I compute the optimal royalty percentage?

You have to pick royalty percentages and other terms of agreement that work both for the investor's desired return on investment and for your company cash flow. This requires some experience with, and ideally mastery of, the calculation tools Intelliversity and its partners supply.

How do I determine the best sequence of multiple percentages?

A reduced percentage in the later years allows the investor to benefit from large revenue growth in later years without significantly impacting net profit – an incentive to invest with you. The problem is to figure out the various royalty percentages and when each one of them kicks in.

How do I determine how many years royalties must be paid to investors?

The longer they are allowed to run, the lower the royalty percentages can be. You'll need to play with royalty plan illustrations until you arrive at an attractive plan for both parties.

What other terms of agreement can I use to protect the company?

Royalty agreements can include any terms that the parties agree on, including 1) caps on the cumulative royalty paid, 2) caps on the length of time during which royalties are paid, 3) downward adjustment in the royalty rate or length of time if the company significantly exceeds its revenue projections, and 4) the redemption option -- the option for the company to buy back the royalty so that royalty payments cease.

What additional terms of agreement will investors sometimes request?

There are many other possible terms of agreement that help investors feel comfortable

including what happens if the company significantly underperforms, and using a loan to pay back the principal.

Where can I get sample agreements and term sheets? Where can I get sample business plans, investor pitches and PPM's that incorporate Revenue Royalties?

They are available to you through Intelliversity training programs.

How and when can I pay finders' fees to brokers or intermediaries?

This relates to whether Revenue Royalty financing are considered "securities" by the SEC. There are different opinions on this subject. Intelliversity training programs address this debate so that you can intelligently discuss the matter with your own advisors.

How do I record Revenue Royalties in company books?

This includes questions such as where do Revenue Royalties appear in the Balance Sheet and Income Statements of the issuer and the investor. Intelliversity training programs address this debate so that you can intelligently discuss the matter with your own advisors.

How do Revenue Royalties relate to other financing methods

There are many alternative methods such as crowdfunding, customer-financing, strategic partnerships, direct public offerings, accounts receivable financing, factoring, convertible notes, and so on. None of these methods listed here are the same as Revenue Royalties, but you should understand the differences.

Are there checklists and step-by-step guides?

Yes. Intelliversity training programs will provide this.

Are there attorneys, accountants and investment bankers who understand Revenue Royalties?

Yes, and they want to hear from you; we can introduce you.

Can I ask questions directly to the Intelliversity experts who wrote this eBook and provided the information in it?

Yes, see below for programs that give you this opportunity.

And the questions that every executive asks:

How do I find investors who are interested in Revenue Royalties?

There are high-net worth individuals and funds that provide financing using Revenue Royalties. Since the JOBS act was passed, there

are newly legal ways to promote investment opportunities that apply to Revenue Royalties. We cover this in Intelliversity training programs.

Get everything you need to make powerful offers to investors using Revenue Royalties:

Go to IntelliversityCampus.org and sign up for the Revenue Royalties Power Program.

To master the art of negotiating a deal that is ideal for both sides, sign up for the Revenue Royalties Mastery

Where can I get this additional assistance?

Intelliversity offers two ways forward:

The Revenue Royalty Power Program

This program gives you everything you need to make initial Revenue Royalty offers to investors. This is a self-paced program built around a series of talks and demonstrations by Arthur Lipper. It includes the online calculators he designed to help you determine the terms of agreement. It includes sample agreements, sample presentations and sample business plans. It also includes checklists to guide you through the process and suggestions for experts that can provide additional help if needed.

The Revenue Royalty Mastery Program

This is a partially self-paced and partially interactive program, like the Power Program available Internet-wide. It takes the Power

Program to the next level, giving you everything you need to control the negotiation with investors and win most favorable terms. Since it is interactive (in a group with a live expert) it is primarily concerned with the application of Revenue Royalties to each business and non-profit who attends.

The Power Program and Mastery Program are examples of “action learning” -- financial empowerment. In all of our programs, we want to see you achieve success.

In all programs and at all times, we want you to enjoy yourself and meet like-minded people on common ground. You are invited. Come, discover, learn, get into action and have a good time.

The Vision of Intelliversity

Intelliversity envisions all innovative ventures becoming unstoppable.

Its mission is to assist innovators to gain the financial and management resources needed to win. It serves innovators of all types -- business, non-profits and research.

Intelliversity's current focus is capitalizing innovative companies using “Revenue Royalties.”

Next, we take on scientific research. Intelliversity's goal is to stimulate an eight-fold increase in the private funding of science.

We believe that scientific exploration is the way forward for an intelligent species. *Science provides the most powerful incentives for collaboration and peace.* **We envision the day when scientific exploration, including the exploration of the cosmos, emerges as the shared purpose of all humankind.**

The Team behind Intelliversity

Robert Steven Kramarz, founder and Executive Director of Intelliversity was founder or C-level executive of seven successful companies in the computer industry, including acting CEO of Cordata, which was sold to Daewoo Corporation, a Korean conglomerate, and CEO of 1776 Software.

More recently he has been advising companies on formation and funding through partnership in 22nd Century Ventures and Vantera Partners. He is also a management advisor to Pacific Royalties, an advisory firm specializing in Revenue Royalties. He was for several years member of the largest angel investment network in the U.S. – Tech Coast Angels, and has invested in a number of technology and life sciences early stage ventures.

He is the lead investment advisor to his the Family Office run by his own family, responsible for a significant diversified portfolio of independently-managed investments.

Mr. Kramarz has the heart of an inventor and is a passionate supporter of science and technology. He believes that scientific exploration, especially when pursued on a large scale through private funding, can provide common purpose that can lead to peace and prosperity throughout the world.

Ravi K. Bohla is the co-founder and member of the Board of Directors of Intelliversity. Bhola has spent over 30 years investing in, building and growing technology companies and has worked extensively on an international basis in information systems, satellite

systems, information warfare and energy. Ravi's experience is both as an investor and in various aspects of general management. He has acquired, grown and sold seven companies and has invested in over a dozen early stage companies as well as co-invested in a number of early stage startups.

Throughout his career, Ravi has been very actively involved in application of new technology, methods, and processes to provide competitive advantage or completely new ways of providing higher value solutions to new and existing markets. In many cases Ravi has brought customers, investors and companies into strategic relationships that allowed entry into new markets or the undertaking of complex projects in a manner that was faster and at lower cost and risk. He has been a partner in a Venture Capital fund and is currently a partner in a boutique private asset management company with an international focus.

Arthur Lipper, Chairman of the Intelliversity Board of Advisors, is an innovator in the field of financial services. He pioneered breakthroughs in the fields of mutual fund analysis, stock index futures and mutual funds, through the Lipper Index and the international Lipper Fund Performance Awards.

Mr. Lipper formed two New York Stock Exchange member firms, Arthur Lipper Corporation and New York & Foreign Securities, and served both as Chairman. These firms specialized in serving institutional investors, and their services included the creation of mutual fund investment performance analysis. They were members of all of the major U.S. securities exchanges and a number of commodity futures exchanges, and transacted hundreds of millions of dollars of business.

Arthur Lipper Corporation invested in privately owned companies, including Venture Magazine, where Mr. Lipper served as Editor-in-Chief.

In 2007, Mr. Lipper was awarded a U.S. patent covering the Comparator service for investment managers. Comparator allowed users to uniquely review and manage portfolios based on the relative weighting of holdings. In 2010 he was awarded a patent for an approach to using revenue royalties in the financing of

companies. In 2013 he filed another patent covering the combining of debt and royalties.

He is a leader of the field of royalty finance, and has published a number of analytical tools to help investors and business owners understand their potential. Arthur is involved with a number of efforts to initiate funds, partnerships, and public securities exchanges focused on revenue royalties.