Royalties – Questions and Answers©
By: Arthur Lipper

Preface:

The following questions and answers regarding royalties, especially royalties purchased form companies seeking to expand and increase their revenues have not been prioritized or are in common interest groups. They are simply a random listing of questions we believe could be in the minds of those not having studied royalties.

It is my hope that in reviewing the questions and answers a better understanding of the royalty process will result. We believe that royalty financings will create increasing income for investors and bigger businesses for royalty issuers. Both will enrich our society,

Arthur Lipper, Chairman
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Q Why should investors consider investing in royalties?

A Only those investors interested in receiving increasing income payments should invest in royalties.

Q Who are the sellers of royalties?

A Companies believing that having increased capital will result in their creating increased revenues and profits.

Q How safe are royalties for the investors?

A Much safer than owning shares in the royalty selling companies as royalties are only focused on the company's revenues.

Q Why don't royalty investors care about executive compensation level in the royalty issuing companies?

A Because royalties pay a percentage of revenues, not profits.

Q What protects royalty investors from loss of capital?

A Royalties can be secured by critical assets the companies selling the royalties.

Q Can royalty payments be guaranteed by independent parties?

A Royalty payments of an amount equal to the investor's net investment in the royalty can be purchased by the company.

Q What's in it for me as a business owner to sell a royalty?

A The cash you get for selling the negotiated percentage of the company's revenues over an agreed period.

Q What happens if the royalty issuing company's revenues are not as much as projected?

A Unless there are special terms, the royalty investor will receive a less amount of royalty payments than was expected.

Q Can the terms of a royalty be changed once the transaction has occurred?

A All contractual relationships can be changed if all of the parties agree.

Q Can I sell the royalty whenever I want?

A Yes, if you can find an appropriate buyer.

Q What is an appropriate buyer for a royalty?

A Royalties are financial instruments and may be deemed securities. Therefore the buyer should be "accredited" as the SEC defines the term.

Q How are royalties valued or priced for sale?

A Royalties generate payments based on the revenues of a company. Therefore, the valuation is based upon the expected royalty payments to be paid and received during the immediate and full royalty payment period.

Q Are there royalty exchanges or markets creating liquidity for royalty owners?

A Not yet, but such a development is logical.

Q Are there royalty income funds or partnerships through which investors can benefit?

A Yes and it is logical that investment managers will create such investment vehicles.

Q What are the commissions and fees associated with my buying a royalty?

A Royalty related commissions and fees are industry standard and a matter for buyer and sellers to discuss.

Q Does a business owner need anyone's permission to sell a royalty?

A Not if the business owner is the 100% owner of the business.If not then a Board of Directors and possible shareholder approval would be necessary due to the likely terms of the royalty.

Q Do royalties have to be registered with the SEC?

A The SEC registration of royalties would be required if they were being offered publicly.

Q What can go wrong and hurt the owners of royalties?

A Royalty owners will be hurt if the revenues of a royalty issuing company are less than expected or cease to exist for whatever reason. However, the periodic payment of royalties reduce the amount invested in a royalty and therefore reduce risk.

Q How much information about the company issuing the royalty does a royalty owner receive?

A The amount of information and timing of distribution is a part of the royalty payment agreement and is whatever agreed between the parties. Generally, an annual audit of, at least, revenues is required, as well as quarterly royalty payments and revenue reports.

Q Can royalties be made of shorter duration?

A Yes but the shorter the duration the higher will have to be the royalty rate to produce there IRR wanted by the investor.

Q How can a royalty issuer get rid of the royalty?

A By exercising a redemption right if there is one and by buying the existing royalties, either through direct negotiation or by making a tender.

Q Who will dislike the use of royalties in the financing of a business?

A Existing creditors will be concerned with the royalty owners deducting the agreed royalty at the time of reyenue recipe, even though the creditor's positions will be improved by the additional capital in the business and resulting expansion.

Q Why are royalties positive for the society?

A Because the additional capital in a business will result in the royalty issuing company expanding and this is good for the employees, local merchants and the local communities.

Q Can companies with royalties go public?

A Most companies, especially those involved in technology, entertainment, publishing and franchising, pay royalties as a normal part of their business. Royalties will reduce the profits of a royalty issuer in the early years of using the funds paid for the royalty, but will allow the owners of the royalty issuer to retain the full amount of their equity holdings.

Q Will a company having been financed through the use or royalties be harder to sell than the one finaced conventionally?

A A company's attraction to a buyer depends on how well the company has used the funds available to it in increasing revenues and profits. Royalties can be redeemed and otherwise terminated. Most importantly, financing through the use of royalties has allowed the owners of the business to avoid equity dilution.

Q Can royalties be convertible into the equity of the royalty issuer?

A Yes and at the option of either the royalty investor or, under agreed circumstances, by the royalty issuer.

Q Can royalties be used to reward individuals and well as groups of individuals?

A Yes, at the discretion of the managers and owners of the business.

Q Will banks lend to companies with royalties outstanding?

A This depends on the bank, the company and possibly by the cooperation of the royalty owner,
in the subordination of assets used to secure the contractual compliance the royalty issuer.

Q Do those who assist in the placement of royalties with investors get fees?

A Depends on the situation, but it is possible investment bankers will assist in making private placements for a fee.

Q Will international revenues be subject to the royalty agreement?

A Royalty agreements should carefully and fully define the present and future revenues which are to be subject to the royalty. Certain revenues sources can be excluded from the defined revenues.

Q Should the royalty issuer's customers be informed of the royalty issuer's arrangement with the royalty investor?

A This depends on the company's relationship with its customers. If the customers usually receive financial statements from the company then the royalty should be disclosed.

Q Do royalty issuing companies have to be profitable?

A No. Royalty issuing companies should either have or plan to have a substantial profit margin. Royalties should not be sold by or purchased from companies having modest profit margin once mature. Royalty payments "coming off the top" as they do by being paid without regard to the profits of the royalty issuer, should allow sufficient margin. after the payment of the royalties, with which the company can further develop and increase revenues.

Q What types of companies should not sell royalties?

A Companies in low profit margin and highly competitive industries.

Q Are early-stage pre-revenue companies good candidates for royalty-based financings?

A Royalties can be effectively used by pre-revenue companies if there is evidence that substantial revenues can be realistically projected. Investors will make their greatest percentage gains in financing early stage companies, but will also be accepting the

greatest risks of loss, as that is the nature of investing in early-stage companies.

Q How are royalty issuing companies valued by investors?

A There is no reason for the royalty investor to be concerned with guessing at the valuation of a royalty issuer, as the investor is only interested in the prospects for the company's increasing revenues. The royalty investor wants to be able to project the minimum Internal Rate of return (IRR) which is likely to be earned if the investment is completed and the projected revenues achieved.

Q What is the Internal Rate of Return most royalty investors demand?

A It all depends on the assuredness of the projected revenues being attained in the time period indicated. In the case of early-stage companies, where royalties are replacing venture capital, with the business owner benefit of being non-equity dilutive, something over a 20% IRR, achieved over the course of the royalty payment period will be required.

Q Who should buy royalties?

A The royalty buyer should be an individual investor who wishes to have increasing quarterly royalty payments during the course of the royalty payment period, reflecting the royalty issuing company/s increasing revenues. Increasing revenues, including those resulting from the effect of inflation, is the focus of royalty investors.

Q Who, other than individual investors, should be buying royalties?

A It is inevitable that tax exempt institutions such as pension and endowment funds will ultimately be the largest buyers of royalties due to their need for increasing income and wishing to avid the volatility

of securities markets. They also are able to retain more of the benefit of the increasing royalty payments due to their tax status.

Q How long should it take for a royalty-based financing to be accomplished?
A Although it is easier for a single investor to reach a decision as to the course of a company's future revenues, if the funding requires multiple investors the time required is similar to that of an equity offering, all depending on if the offering is for accredited investors or is fully registered with the SEC and then available to a public offering.

Q Where is legal advice regarding royalties available?

A The law firms presently familiar with royalties, though not necessarily revenue royalties, are those experienced in the industries where royalties havee traditionally been used, such as entertainment, music, publishing, oil and gas drilling, mining and high technology licensing and contracting. The same would be true for accounting firms.

Q Is there an approach to using royalties that works best for early-stage companes?

A Yes a combination of debt and royalty results in investors being able to achieve their IRR returns more assuredly and business owners being able to acquire funding on more favorable longer-term basis.

Q What are websites where information regarding royalties be found?

A PacificRoyalties.com, REXRoyalties.com, REXdebt-shareRoyalties.com, REX-PV.com, REXScaledRoyalties.com and REXComparator.com. In Pacific royalties the Library section contains a great deal of royalty related information.