

How to Raise Capital But Preserve Your Equity: Royalty Based Crowdfunding (Interview With Arthur Lipper)

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While some might think that *royalty based crowdfunding* is a new sheriff in town, the truth is that selling a portion of a future sale (royalty) in return for an investment has been quite popular for many years in the pharmaceutical and oil & gas industries, as well as among artists, writers, movie makers and those who were pitching Friends and Family, aka non-accredited investors.

The main benefit for the investor is that he earns his regular income from gross revenues (not profits) as soon as the sale occurs and for the entrepreneur is that he is not giving up his equity while maintaining 100 per cent of an ownership.

With nowadays technology which keeps simplifying revenue management while making crowdfunding platforms as commodities (check out [Invested.in](#) if you are in desire to build your own), I believe royalty based crowdfunding is set to be one of the most

popular models in the next two-three years.

So far we have a few market players in this particular space such as [Quirky](#), [TubeStart](#), [AppsFunder](#), [RoyaltyClouds](#), [Lendpool.com](#) and [Gideen.com](#). But it looks like royalty funding is on the watch list of some of the most prominent financiers of the world.

While producing our annual [Alternative Funding Forum](#), I've been pleased to have on-board Arthur Lipper - a world renowned financier and inventor, who created innovations such as [Lipper Mutual Fund](#) Performance Analysis and stock index futures. Arthur Lipper's most recent patented innovation - royalty finance - naturally made me want to ask him a few questions.

VS: Which industries & companies in your opinion would especially benefit from royalty crowdfunding?

AL: Royalties should only be sold by companies having, or realistically projecting, a fairly high profit margin. Royalties are deducted from revenues and therefore add to the expenses of running a business. Of course, the additional capital will allow for an expansion of the business, thereby probably increasing profitability. Technology related and service businesses lend themselves to royalty

financing, as their margins tend to be higher than manufacturing companies and benefit disproportionately to increased revenues.

VS: What are the typical metrics royalty investors are claiming?

AL: We believe in longer-term royalties, or more than 10 years and as long as 20 years, in order for the percentage of the revenue paid to the royalty purchaser to be lower. In most cases, the longer the royalty payment period the lesser the percentage of revenues required to meet the demands of the investor in the royalty. Royalties should provide investors with more than a 20% Internal Rate of Return or IRR over the course of the royalty payment period. Royalties starting at say 5% can be reduced upon receipt of agreed levels of cumulative royalty payments. Investors will want to buy royalties from issuers having at least 10% annual increases in revenues.

VS: What are the Security and Exchange current requirements on royalty financing and how are we to make sure to stay within its current ruling?

AL: The SEC has not issued rulings specifically impacting the public offering of royalties. Therefore, royalties which were offered to the public would require the preparation of a prospectus describing

the royalty issuing company and all of the known risks, which could possibly harm the company or its ability to meet its contractual obligations regarding royalties, unless there was an applicable exemption. The initial activity regarding royalties will be in the creation of royalty income funds and possibly investment partnerships which will purchase royalties from privately owned companies. [Pacific Royalties](#), which I have co-founded is likely to be one of the first royalty income funds. The Library section of [PacificRoyalties.com](#) has a full range of royalty related items.

VS: Can you give a specific example of a company that has raised capital via royalty financing based on your experience?

AL: The approach I was able to patent and regarding which I have filed a subsequent patent is new and contains unique elements. The following websites provide samples and templates as well a full description of the process. [REXRoyalties.com](#), [REXdebt-shareRoyalties.com](#), [REXComparator.com](#) and [REX-PV.com](#). Eventually, there will be one or more royalty exchanges through which ownership interests in royalties may be traded. These exchanges will allow investors to receive a better and increasing level of return and a vast number of privately owned companies funding.

VS: What would be the best royalty structure and what factors should be taken into consideration?

AL: No two companies are alike and the amount, royalty duration, royalty rate and means of assuring contractual compliance are the four elements of a royalty transaction that need to be negotiated. For early stage companies I recommend the debt plus royalty approach. The royalty purchaser should be comfortable re the survival of the royalty issuing company and have a positive view as to the issuer's increasing revenues.

VS: Can you tell us more about the Royalty Exchange you are working on and what it takes to make it operational in this country?

AL: The fact that royalties are currently not generally traded on exchanges allows investors to require royalty issuers to pay a higher royalty rate than would be the case were royalties to be liquid. The lesser the royalty rates the greater the number of business owners who would be interested in selling royalties and thus investors seeking income would have a wider selection of issuers to choose from. Executives at a number of existing stock exchanges have indicated a desire to be the second exchange to trade royalties. I am still looking for the exchange, which wants to claim first mover advantage in

establishing the rules and regulations for the trading of royalties. I am involved in the process of creating a [royalties exchange in China](#) and were that to be successful it would quickly become one of the world's larger financial markets.

VS: I am a great believer in getting the general public involved in investing. What is your take on general solicitation which would allow non-accredited investors aka crowd to participate in financing private entities and the fact the [Title III of JOBS Act](#) of 2012 is not being enforced and is still in the SEC hands?

AL: I have significant reservations about allowing companies to sell stock and other investments to the non-accredited public. Underwriters play a useful role in screening and doing necessary due diligence. I question the wisdom of creating a mechanism where companies can sell securities directly to small investors without there being an approved intermediary directly involved.

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