

## **Larry and Barry on: Successful, privately owned companies using Fair Revenue Participation Contracts and the Royalty Entitlement Exchange ©**

Lawrence (Larry) Lion and Bernard (Barry) Beaver have been used by Arthur Lipper to illustrate the reactions of typical growth oriented entrepreneurs. Larry and Barry first appeared in the monthly column of Arthur Lipper, as Chairman and Editor-in-Chief of Venture the magazine for business owners. Arthur Lipper's latest book is The Larry and Barry Guide to Entrepreneurial Wisdom has also been published by CITIC in Chinese and has sold well in China.

***Larry: Why would we ever want to get involved with the payment of royalties just to raise some money?***

***Barry: If we had more money to use for expansion we could move faster. Also a bunch of money would allow us to improve or even move our manufacturing operation, which is what your son-in-law has been nagging us about for years.***

**Larry: Sure. It's always nice to have a lot of extra money, but we've done alright keeping the ownership of this business in our families. A lot of people are living off the company and still we grow.**

**Barry: As our families grow there are more and more people for us to hire and we also need to grow the business just to maintain our market share as our market areas are growing so quickly.**

**Larry: We sure don't want to let our customers know how much money we are making. Also we do not want a lot of investors telling us how they think we can improve our operations or complaining when our profits are flat or we choose to report a loss.**

**Barry: That's the nice thing about these Fair Revenue Participation Contracts, we don't have to disclose our profits and the investors don't own stock so they don't have any say in how we run the business. All they get is a sliver of our revenue.**

**Larry: If they don't know our profits how can they know if we are going to survive financially so as to be able to pay them the agreed percentage of our revenue?**

**Barry: Well, we will disclose balance sheet data in the information circular at the time of the IPO and thereafter annually provide information about the value of our assets and liabilities and what, if any, debt we have. However, we won't disclose profits, just revenues.**

**Larry: How do they know we are telling the truth about the revenues?**

**Barry: All of the Directors have to personally attest as to the correctness of the quarterly revenues and annually we have to have the revenues audited.**

**Larry: And how do they enforce our royalty payment obligations?**

**Barry: One of the four points the Managing Underwriter negotiates with us is the critical assets which are transferred to their Singapore approved trustee company. The trustee company licenses us back the exclusive use of the assets, royalty free, until the end of the royalty payment period. If there is a default then the trustee company uses the assets for the benefit of the royalty entitlement holders.**

**Larry: That's pretty neat for them as without the critical assets we are out of business. What sort of assets are they talking about?**

**Barry: Buildings, land, intellectual property, equipment, brand names, etc. All important to the continuation of our business. They are not fooling around and do not expect us to do anything but what we agree to do.**

**Larry: Ok. So how much do we get and what do we give up?**

**Barry: That's something we negotiate with the Royalty Entitlement Exchange member acting as Manager Underwriter. We negotiate with them; the amount of money we get, the level of revenue percentage we pay and how long we pay the royalty.**

**Larry: I guess it's only logical the longer the royalty payment period the less a percentage of revenues we have to pay?**

**Barry: Right. That's exactly how it works. I think the range is from 5% for ten years to 1% for fifty years. It all depends on the deal we make with the Managing Underwriter.**

**Larry: Who is likely to be this Underwriter? Will they know anything about our business or industry?**

**Barry: The Royalty Entitlement Exchange member is likely to be one of the larger international financial service organizations, you know big banks and brokerage firms. They will have their own experts and analysts to use in valuing the revenue flow in which their clients and customers will participate and to prepare the Information Circular for the IPO.**

**Larry: Of course, as their customers will not be owners of the business there is no reason for us to put any of their designees on our Board of Directors as is usually the case with equity deals.**

**Barry: Right. We continue to keep all of the ownership and its prerogatives in our hands and all they have is a secured royalty entitlement.**

**Larry: I wonder if this deal would work for non-profit operations. You know that I am on the Board of the hospital which is non-profit but has revenues. The banks won't lend to us as there is always a deficit which is made up by donations. If we had some money we could add services which would bring in enough new revenue to bring us past the breakeven point.**

**Barry: I don't know but in theory the Fair Revenue Participation Contract approach should work as well with non-profits as with for-profit companies. After all, non-profits retain the services of people, why shouldn't they attract capital through revenue participation?**

**Larry: What happens when we want to recapture the royalties we would be paying to the royalty entitlement holders? I can see us achieving so much profit from the use of the money that we will not be needing the capital and will not want to continue paying out the royalties/**

**Barry: We could buy back the royalty entitlements on their exchange or tender for them. Were we to ever decide to go public we could also offer to exchange shares for the royalties. It's all a matter of negotiation.**

**Larry: What's wrong with the idea? Why wouldn't every owner of a business want to use the program?**

**Barry: What's wrong is that once we reach agreement we are committed to share revenue irrespective of our profit. It is possible that we will have a year or so where we actually lose money but nevertheless the royalty payment obligation remains and will, in effect, increase our losses.**

**Larry: What about if we and the Managing Underwriter can't reach agreement as to terms?**

**Barry: As most of the world's larger financial service organizations will be exchange members we will just have to start a negotiation with one or more of the other members.**

**Larry: Our operation is absolutely Sharia compliant in all respects. Shouldn't that allow us to get a better deal as there will be all these Sharia compliant institutions and other investors who have difficulty in finding Sharia compliant investments.**

**Barry: It seems reasonable to believe that by being recognized as being Sharia compliant a great deal of additional capital will be interested in our revenue participation opportunity with the result that we will be able to make a better deal with the Managing Underwriter.**

**Larry: Yeah. It also seems logical that there will be underwriting firms which specialize in Sharia compliant companies as well as companies in industries for which they have a special interest and knowledge.**

**Barry: Sure. Some of the exchange members will specialize in host industry companies and others in distribution companies while there will always be those who believe they have special knowledge in the medical technology dependant companies.**

**Larry: Well, as it is all getting started in Singapore and with their regulatory supervision it can't be a scam and as it sure makes more sense to us than selling equity to strangers let's try it. Of course, we could also use the same process in a new company we form just for the expansion we have been planning.**

**Barry: That's certainly something we could discuss with one of their royalty entitlement Exchange members.**

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