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SEVEN BIG PAYOFFS FOR INVESTORS (WITHOUT AN IPO)

Selling shares of a company was once the best way to reward early investors in a firm. But the IPO (initial public offering) just isn't what it used to be. Even though the number of IPOs spiked in early 2006, only a handful of all companies choose to go public. Which suggests that except for the Googles of the world, IPOs may have all the appeal of old socks with holes in the toes.

The shift is the result of SOX. That's the financial industry's nickname for the Sarbanes-Oxley Act of 2002; legislation that aggressively rewrote the rules of the IPO, making it far too painful for most companies to even consider. Thanks to SOX, going and staying public costs dramatically more than before. Plus, in order for an IPO to pencil out, the value of a company must be much, much higher than before.

Yet start-up companies still need early investors. And those investors expect to be rewarded within a reasonable timeframe. Company founders, therefore, have found alternate ways to attract and reward investors. Here are seven of them:

1] SELLING TO A LARGER COMPANY

This option is probably the easiest to manage. Which explains why more than half of start-up companies prefer this route to financial reward. A primary requirement is that both firms—buyer and seller—must be doing business in related industries, so that the fit makes sense. Early investors will want to know who the likely buyers might be, because they want to see their exit right from the start. Whether it's a merger or an acquisition, those investors can be literally cashed out, or they can receive stock in the buying company, or maybe some warrants that entitle them to buy shares later on.

2] SELLING TO A PRIVATE EQUITY FIRM

Though obviously quite similar in appearance to the method described above, selling to a private equity firm is distinguished by the fact that the buyer need not be doing business in the same industry as the seller. This approach is on the rise. And leading the way are such famous buyout names such as Kohlberg Kravis Roberts, Carlyle, Ripplewood Holdings and Pincus Warburg. KKR is renowned for spending billions of dollars on long-term investments in attractive companies, whose early investors clearly benefit.

3] FRANCHISING IS GOOD AGAIN

Remember back when franchising was all the rage? Then remember how the concept fell from favor? Well, franchising is resurging, and it has more to do with changing perceptions than changing realities. The idea simply looks more attractive as other options (yes, the IPO) become less attractive. You still develop a single business concept and roll it out to other geographic locations. You still receive franchise fees and other revenue from your franchisees. Only now, you use those new proceeds to reward early investors.

4] THE STOCK BUY-BACK

Here's one for the staunchest of independents. Rather than seek outside funding to reward your early investors, you develop a plan by which the firm can buy stock back from those investors, thus allowing you to retain control of the firm. Prerequisite, of course, is the financial wherewithal to fund such a program. As with IPOs, only a small percentage of all companies ever manage a stock buy-back.

5] MAKE A MARKET FOR YOUR STOCK

For entrepreneurs who thrive on shaping their own world, there's the option of actually creating a private market in which early investors can sell their shares. The idea centers on giving individual investors an opportunity to reap their returns via "a market" with limited access. It could be as simple as a bulletin board on a restricted Internet site. However, there are significant securities restrictions to consider.

6] THEN THERE'S THE LICENSING AGREEMENT

Some companies find success by licensing their product or service to other companies in exchange for huge fees (if their products command them), which can be used to reward early investors. For instance, funds raised through licensing fees can conceivably be used to launch a stock buy-back program. W.L. Gore is a fine example of a company that licenses its product—Gore-Tex®—to other manufacturing firms. Their waterproof membrane is used by scores of outdoor brands.

7] THE NON-PROFIT THAT PAYS WELL

There's a trend today that sees start-up firms structured as non-profit organizations. It's sounds counterintuitive. But there's no law saying employees of a non-profit can't be paid handsomely. Public relations issues aside, then, an option for rewarding early investors who are part of the business is simply to make them employees and then pay them a bundle. It's not exactly what you'd call an exit strategy. Yet some people consider a nice living to be a reasonable return on their investment.

Shed no tears if the IPO is DOA. Most companies have only to move beyond the "old thinking" to embrace some of the cash-out ideas being used as alternatives. And the truly good news is this: There's plenty of investment money out there to be had right now.