

**BLACKBURNE & SONS REALTY CAPITAL
CORPORATION AND AFFILIATE
FINANCIAL STATEMENTS
SEPTEMBER 30, 2015 AND 2014**

**BLACKBURNE & SONS REALTY CAPITAL CORPORATION
AND AFFILIATE**

September 30, 2015 and 2014

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INDEPENDENT AUDITOR'S REPORT

To the Boards of Directors
Blackburne & Sons Realty Capital Corporation
and Affiliate
Sacramento, CA

Report on the Financial Statements

We have audited the accompanying financial statements of Blackburne & Sons Realty Capital Corporation and Affiliate which comprise the balance sheets as of September 30, 2015 and 2014, and the related statements of income and retained earnings and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness on the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Blackburne & Sons Realty Capital Corporation and Affiliate as of September 30, 2015 and 2014, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Boden Klein & Sneesby

BODEN KLEIN & SNEESBY
Certified Public Accountants
Roseville, California

December 17, 2015

**BLACKBURNE & SONS REALTY CAPITAL CORPORATION
AND AFFILIATE**

Balance Sheets
September 30, 2015 and 2014

ASSETS

	<u>2015</u>	<u>2014</u>
Current assets:		
Cash	\$ 4,146	\$ 6,663
Mortgage servicing rights	623,235	552,425
Prepaid expenses	37,634	6,749
Prepaid income taxes	-	2,950
Other receivables	<u>32,404</u>	<u>26,351</u>
Total current assets	<u>697,419</u>	<u>595,138</u>
Property and equipment, net	<u>14,130</u>	<u>17,556</u>
Other assets:		
Investment in partnerships	65,148	64,982
Intangible asset, net	91,152	99,652
Other receivables - net of current portion	26,800	11,000
Mortgage servicing rights - net of current portion	<u>767,486</u>	<u>474,594</u>
Total other assets	<u>950,586</u>	<u>650,228</u>
TOTAL ASSETS	<u><u>\$ 1,662,135</u></u>	<u><u>\$ 1,262,922</u></u>
Borrower and investor custodial accounts (segregated in special accounts - excluded from corporate assets)	<u><u>\$ 964,672</u></u>	<u><u>\$ 1,441,340</u></u>

See notes to financial statements.

**BLACKBURNE & SONS REALTY CAPITAL CORPORATION
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Balance Sheets
September 30, 2015 and 2014

LIABILITIES AND STOCKHOLDERS' EQUITY

	<u>2015</u>	<u>2014</u>
Current liabilities:		
Accounts payable	\$ -	\$ 28,069
Other payable	108	858
Accrued expenses	74,766	25,365
Income taxes payable	5,740	5,135
Deferred income taxes	133,325	109,138
Line of credit	57,500	67,000
Notes payable - current portion	<u>-</u>	<u>59,402</u>
Total current liabilities	271,439	294,967
Non-current liabilities:		
Deferred income taxes - net of current portion	<u>185,269</u>	<u>115,302</u>
Total liabilities	<u>456,708</u>	<u>410,269</u>
Stockholders' equity:		
Common stock - no par value, authorized, issued and outstanding, 100 shares	312	312
Additional paid-in capital	100	100
Retained earnings	<u>1,205,015</u>	<u>852,241</u>
Total stockholders' equity	<u>1,205,427</u>	<u>852,653</u>
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	<u>\$ 1,662,135</u>	<u>\$ 1,262,922</u>
Borrower and investor custodial accounts (segregated in special accounts - excluded from corporate assets)	<u>\$ 964,672</u>	<u>\$ 1,441,340</u>

See notes to financial statements.

**BLACKBURNE & SONS REALTY CAPITAL CORPORATION
AND AFFILIATE**

Statements of Income and Retained Earnings
For the Years Ended September 30, 2015 and 2014

Revenues:	2015	2014
Servicing fees	\$ 817,440	\$ 686,386
Loan commissions	856,631	642,172
Property management fees	88,898	152,479
Amortization of mortgage servicing rights	363,702	123,258
Fund management fees	58,000	69,982
Software licensing fees	247,098	154,402
Video and manual sales	34,898	14,871
Total revenue	2,466,667	1,843,550
 Expenses:		
Salaries	859,462	686,645
Salaries - George Blackburne	291,728	250,488
Salaries - Francisca Blackburne	53,328	53,328
Marketing	134,664	138,536
Outside consultants	131,508	66,293
Retirement plan contributions	84,996	25,167
Payroll taxes	83,772	71,319
Employee benefits	72,209	81,713
Other expenses	65,337	58,525
Legal	53,042	91,495
Insurance	37,267	36,515
Office expense	36,707	29,557
Office rent	33,252	33,041
Tax and license	28,769	28,977
Telephone and utilities	21,478	23,888
Loan arrangement fees	16,710	19,069
Accounting	12,510	13,254
Depreciation	11,926	12,715
Maintenance and repairs	8,294	6,603
Travel	7,383	13,959
Automobile	5,157	10,681
Equipment lease	3,668	2,417
Education	2,734	878
Total expenses	2,055,901	1,755,063
Income from operations	410,766	88,487

See notes to financial statements.

**BLACKBURNE & SONS REALTY CAPITAL CORPORATION
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Statements of Income and Retained Earnings
For the Years Ended September 30, 2015 and 2014

	<u>2015</u>	<u>2014</u>
Income from operations (continued)	\$ 410,766	\$ 88,487
Other income (expense):		
Interest expense	(5,994)	(6,073)
Income (loss) from partnerships	166	(1,549)
Other fees and income	<u>47,128</u>	<u>48,018</u>
Total other income (expense)	<u>41,300</u>	<u>40,396</u>
Income before income taxes	452,066	128,883
Income tax expense	<u>99,292</u>	<u>22,887</u>
NET INCOME	352,774	105,996
Retained earnings, beginning of year	<u>852,241</u>	<u>746,245</u>
RETAINED EARNINGS, END OF YEAR	<u>\$ 1,205,015</u>	<u>\$ 852,241</u>

See notes to financial statements.

**BLACKBURNE & SONS REALTY CAPITAL CORPORATION
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Statements of Cash Flows
For the Years Ended September 30, 2015 and 2014

	2015	2014
Cash flows from operating activities:		
Net income	\$ 352,774	\$ 105,996
Adjustments to reconcile net income to net cash provided (used) in operating activities:		
Depreciation	11,926	12,715
Amortization & impairment of mortgage servicing rights	730,222	598,881
Additions to mortgage servicing rights	(1,093,924)	(722,139)
(Income) loss from partnerships	(166)	1,549
Deferred income taxes	94,154	20,255
Changes in operating assets and liabilities:		
Prepaid expenses	(30,885)	5,247
Prepaid income taxes	2,950	(2,950)
Other receivables	(21,853)	(26,992)
Accounts payable	(28,069)	28,069
Other payable	(750)	713
Accrued expenses	49,401	(26,759)
Income taxes payable	605	-
Net cash provided (used) in operating activities	66,385	(5,415)
Cash flows from investing activities:		
Net (purchase) of property and equipment	-	(3,916)
Cash flows from financing activities:		
Net change in line of credit	(9,500)	32,000
(Principal payments) on notes payable	(59,402)	(22,894)
Net cash (used) provided by financing activities	(68,902)	9,106
Net (decrease) in cash	(2,517)	(225)
Cash, beginning of year	6,663	6,888
CASH, END OF YEAR	\$ 4,146	\$ 6,663

See notes to financial statements.

**BLACKBURNE & SONS REALTY CAPITAL CORPORATION
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Notes to Financial Statements
September 30, 2015 and 2014

NOTE 1 - STATEMENT OF SIGNIFICANT ACCOUNTING POLICIES:

a. Organization -

Blackburne & Sons Realty Capital Corporation (formerly Blackburne & Brown Mortgage Company, Inc.) (the Company) was incorporated in 1980 in the state of California. The Company is engaged in the origination and servicing of real estate loans secured by deeds of trust throughout the United States.

b. Principles of consolidation -

The consolidated financial statements include the accounts of Blackburne & Sons Realty Capital Corporation and its affiliate, C-Loans, Incorporated. All material inter-company transactions have been eliminated in consolidation.

c. Standards of reporting -

The Company prepares its financial statements using the accrual method of accounting. Revenues are recognized when earned and expenses are recognized when incurred. Loan servicing and origination revenue represents fees earned for servicing and originating mortgage loans. Servicing and origination revenue is recognized as earned, unless collection is doubtful.

d. Use of estimates -

In preparing financial statements in conformity with generally accepted accounting principles, management must make estimates based on future events that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

e. Financial instruments -

The carrying amounts of the Company's financial instruments, including cash and cash equivalents, accounts receivable and accounts payable, approximate their fair values.

f. Cash equivalents -

The Company considers all highly liquid investments purchased with original maturities of three months or less to be cash equivalents.

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g. Mortgage servicing rights, amortization and impairment -

The Company recognizes as separate assets the rights to service mortgage loans for others based on their relative fair values. Amortization of mortgage servicing rights (MSRs) is based on the ratio of net servicing income received in the current period to total net servicing income projected to be realized from the MSRs. Projected net servicing income is in turn determined on the basis of the estimated future balance of the underlying mortgage loan portfolio, which declines over time from prepayments and scheduled loan amortization. The Company estimates future prepayment rates based on current interest rate levels, other economic conditions and market forecasts, as well as relevant characteristics of the servicing portfolio, such as loan types, interest rate stratification and recent prepayment experience. MSRs are periodically assessed for impairment, which is recognized in the statement of income during the period in which impairment occurs as an adjustment to the corresponding valuation allowance. For purpose of performing its impairment evaluation, the Company analyzes its portfolio on the basis of certain risk characteristics including loan type and note rate.

h. Property and equipment -

Property and equipment are stated at cost. The policy of the Company is to provide for depreciation over the estimated useful lives of the assets using the straight line method. The estimated useful lives range from five to seven years.

Maintenance and repairs are charged to expense when incurred. Expenditures for additions and improvements, where significant in amount, are capitalized.

i. Income taxes -

The Company accounts for income taxes under generally accepted accounting principles, which require recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements or tax returns. Deferred tax assets and liabilities result from temporary differences in reporting for tax purposes and financial purposes. Deferred tax assets and liabilities are identified separately as current or noncurrent based on the classification of the related asset or liability. A deferred tax asset or liability not associated with an asset or liability for financial reporting purposes is classified as current or noncurrent according to the expected reversal date of the temporary difference.

The Company adopted accounting for uncertainty in income taxes as of October 1, 2010 and thereafter recognizes the tax benefits from uncertain tax positions only if it

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is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such positions are measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. There was no impact to the Company's financial statements as a result of the implementation of this principle.

The Company files tax returns in the United States federal jurisdiction and in the state of California. The Organization's federal income tax returns for the tax years 2011 and forward remain subject to examination by the Internal Revenue Service. The Company's California income tax returns for the years 2010 and forward remain subject to examination by the Franchise Tax Board.

j. Advertising -

The Company's policy is to expense advertising costs as they are incurred.

k. Borrower and investor custodial accounts -

Borrower and investor custodial accounts consists of trust fund cash accounts which are segregated from other corporate assets and maintained by the Company in accordance with Sections 2830 and 2834 of the Regulations of the California Real Estate Commissioner.

NOTE 2 - PROPERTY AND EQUIPMENT:

Property and equipment consists of the following:

	2015	2014
Furniture and fixtures	\$ 37,674	\$ 37,674
Equipment	44,279	44,279
Computer equipment	19,028	19,028
Vehicles	51,005	51,005
Software	55,832	55,832
Total	207,818	207,818
Less: accumulated depreciation	193,688	190,262
Net property and equipment	\$ 14,130	\$ 17,556

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NOTE 3 – INTANGIBLE ASSET:

Intangible asset consists of internet domain names with a cost of \$127,500. Management reviews the intangible asset for impairment annually. Impairment losses are recorded in other expense on the income statement.

NOTE 4 - MORTGAGE SERVICING RIGHTS:

The activity in MSR's was as follows:

	2015	2014
Balance at beginning of period	\$ 1,027,019	\$ 903,761
Additions	1,093,924	722,139
Scheduled amortization & reduction due to early loan payoffs	(730,222)	(598,881)
Reserve for impairment	-	-
	<hr/>	<hr/>
Mortgage servicing rights, net	\$ 1,390,721	\$ 1,027,019

The estimated fair value of recognized MSR's for the years ended September 30, 2015 and 2014 was \$1,390,721 and \$1,027,019, respectively. The fair value was determined by discounting estimated net future cash flows from mortgage servicing activities using appropriate discount and prepayment rates. The gross amount of expected future servicing revenue (net of related servicing costs) before applicable discounting for the years ending September 30, 2015 and 2014 was approximately \$2,045,000 and \$1,880,000, respectively.

NOTE 5 - LINE OF CREDIT:

The Company has a \$150,000 available line of credit with First Northern Bank, which is due May 5, 2016. Interest is payable monthly at the bank's base commercial loan rate (4.75% at September 30, 2015) plus 1.25 percent. The line is secured by receivables and equipment of the Company. The balance outstanding as of September 30, 2015 and 2014 was \$57,500 and \$67,000, respectively.

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NOTE 6 - NOTES PAYABLE:

Long-term debt consists of the following:

	2015		2014
Note due in monthly installments of \$1,631 including interest at 6.5%, maturing in September 2015.	\$	-	\$ 18,838
Demand note payable to related party, interest at 6%, no stated maturity date.		-	40,564
			59,402
Total		-	59,402
Less: current portion		-	59,402
Amount due after one year	\$	-	\$ -

NOTE 7 - TRANSACTIONS WITH RELATED PARTY:

During the years ended September 30, 2015 and 2014, the Company received servicing revenue of \$100,611 and \$93,882, respectively, and collected management fees, including shared expenses, in the amount of \$58,000 and \$66,800, respectively from Blackburne & Brown Mortgage Fund I (the Fund). The Fund is a California limited partnership, whose general partner is the Company. The Company's capital balance with the fund was \$58,925 and \$63,509 at September 30, 2015 and 2014, respectively, and is included on the balance sheet as Investment in Partnerships.

The Company has an ownership interest in Blackburne & Brown Mortgage Fund II (Fund II), a California limited partnership, and provides various management services to Fund II. No management fees were paid to the Company for these services for the years ended September 30, 2015 and 2014.

The Company has a profits and loss interest in Blackburne & Brown Equity Preservation Fund, LLC (LLC), manages the LLC and receives various fees for services performed. The Company received management fees of \$0 and \$3,182, respectively, for the years ended September 30, 2015 and 2014 from the LLC.

The Company had an unsecured note payable due on demand to the principal officer and shareholder. The note was paid in full during the year ended September 30, 2015.

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Notes to Financial Statements
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NOTE 8 - INCOME TAX EXPENSE (BENEFIT):

The provision for income tax expense (benefit) consists of the following components:

	2015	2014
Current		
Federal	\$ 3,224	\$ 1,502
State	1,914	1,130
	5,138	2,632
Deferred		
Federal	57,185	12,302
State	36,969	7,953
	94,154	20,255
Total income tax expense (benefit)	\$ 99,292	\$ 22,887

Deferred income taxes are recognized for tax consequences of "temporary differences" by applying enacted statutory rates, applicable to future years, to differences between the financial reporting and the tax basis of existing assets and liabilities. The tax effects of temporary differences that give rise to the deferred tax liability results from the use of accelerated methods of depreciation of property and equipment and the cash basis of accounting for tax purposes.

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Notes to Financial Statements
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NOTE 9 - COMMITMENTS:

The Company leases its main office space under an operating lease with monthly base payments of \$2,788 expiring on December 31, 2020. Additionally the Company leases office space in Indiana under a month to month lease from the Company's sole shareholder, with monthly payments of \$1,200. Office rent expense was \$45,252 and \$45,041, respectively for the years ended September 30, 2015 and 2014.

The Company subleases a portion of its Indiana office to unaffiliated parties. Sublease income was \$12,000 for the years ended September 30, 2015 and 2014. Sublease income is netted with office rent expense in the income statement.

The estimated minimum lease commitments for the succeeding years are as follows:

<u>Year Ended September 30,</u>	
2016	\$ 33,105
2017	33,456
2018	34,456
2019	37,059
2020	<u>40,084</u>
 Total	 <u>\$ 178,160</u>

NOTE 10 - RETIREMENT PLAN:

On October 1, 1993, the Company established a profit sharing plan that covers substantially all employees. The Company may contribute to the plan an amount designated by the Board of Directors to the extent permissible under the Internal Revenue Code. The Company contributed \$50,000 and \$0 to the plan for the years ended September 30, 2015 and 2014, respectively.

On October 1, 2006, the Company adopted a 401(k) defined contribution plan. The plan covers all employees meeting certain eligibility requirements. The Company contributes an amount, (i.e. safe harbor contribution) determined by the Internal Revenue Code. For the years ended September 30, 2015 and 2014, the Company contributed \$33,252 \$23,653, respectively, to the plan.

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Notes to Financial Statements
September 30, 2015 and 2014

NOTE 11 - CONCENTRATIONS OF CREDIT RISK:

The Company originates and services loans secured by real estate. The Company performs credit evaluations of the potential borrowers and, generally, requires no additional collateral from them.

NOTE 12 - CASH FLOWS:

For purposes of the statement of cash flows, interest paid by the Company was \$5,994 and \$6,073 for the years ended September 30, 2015 and 2014, respectively.

Additionally, the Company paid \$8,241 and \$4,280 in income taxes for the years ended September 30, 2015 and 2014, respectively.

NOTE 13 - CONTINGENCIES:

The Company is involved in various lawsuits in the normal course of business. Management cannot predict the outcome of the lawsuits or estimate the amount of any loss that may result. Accordingly, no provision for any contingent liabilities that may result has been made in the financial statements. Management believes that losses resulting from these matters, if any, would be covered under the Company's insurance policy and would not have a material effect on the financial position of the Company.

NOTE 14 – SUBSEQUENT EVENTS:

Management has evaluated the potential for subsequent events through the available for issuance date of the financial statements, December 17, 2015.