

**BLACKBURNE & BROWN MORTGAGE
COMPANY, INC. AND AFFILIATE
FINANCIAL STATEMENTS
SEPTEMBER 30, 2006 AND 2005**

**BLACKBURNE & BROWN MORTGAGE COMPANY, INC.
AND AFFILIATE**

September 30, 2006 and 2005

Table of Contents

	<u>Page</u>
Independent Auditor's Report	1
Financial Statements	
Balance Sheets	2-3
Statements of Income and Retained Earnings	4-5
Statements of Cash Flows	6
Notes to Financial Statements	7-14

BODEN KLEIN & SNEESBY

Certified Public Accountants

INDEPENDENT AUDITOR'S REPORT

To the Boards of Directors
Blackburne & Brown Mortgage Company, Inc.
and Affiliate
Sacramento, CA

We have audited the accompanying balance sheets of Blackburne & Brown Mortgage Company, Inc. and Affiliate as of September 30, 2006 and 2005 and the related statements of income and retained earnings, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. 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 audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Blackburne & Brown Mortgage Company, Inc. and Affiliate as of September 30, 2006 and 2005, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.



BODEN KLEIN & SNEESBY
Certified Public Accountants

December 6, 2006

**BLACKBURNE & BROWN MORTGAGE COMPANY, INC.
AND AFFILIATE**

Balance Sheets
September 30, 2006 and 2005

ASSETS

	<u>2006</u>	<u>2005</u>
Current assets:		
Cash	\$ 19,242	\$ 10,596
Receivables	22,576	29,374
Mortgage servicing rights	654,398	688,339
Prepaid expenses	14,022	14,073
Prepaid income taxes	2,090	390
Advances	1,500	3,291
Investments	<u>52,832</u>	<u>43,730</u>
Total current assets	<u>766,660</u>	<u>789,793</u>
Property and equipment, net	<u>78,294</u>	<u>98,370</u>
Other assets:		
Investment in partnership	72,237	56,491
Mortgage servicing rights - net of current portion	<u>789,558</u>	<u>1,034,343</u>
Total other assets	<u>861,795</u>	<u>1,090,834</u>
TOTAL ASSETS	<u>\$ 1,706,749</u>	<u>\$ 1,978,997</u>
Borrower and investor custodial accounts	<u>\$ 614,068</u>	<u>\$ 487,203</u>
(segregated in special accounts - excluded from corporate assets)		

See notes to financial statements.

**BLACKBURNE & BROWN MORTGAGE COMPANY, INC.
AND AFFILIATE**

Balance Sheets
September 30, 2006 and 2005

LIABILITIES AND STOCKHOLDERS' EQUITY

	<u>2006</u>	<u>2005</u>
Current liabilities:		
Accounts payable	\$ 114,192	\$ 87,741
Other payable	9,197	9,197
Accrued expenses	79,791	85,727
Deferred income taxes	137,575	144,719
Line of credit	70,000	20,000
Notes payable - current portion	<u>15,000</u>	<u>15,000</u>
Total current liabilities	<u>425,755</u>	<u>362,384</u>
Non-current liabilities:		
Deferred income taxes - net of current portion	188,231	246,587
Notes payable - net of current portion	<u>5,000</u>	<u>20,000</u>
Total non-current liabilities	<u>193,231</u>	<u>266,587</u>
Total liabilities	<u>618,986</u>	<u>628,971</u>
Stockholders' equity:		
Common stock - no par value, authorized, issued and outstanding, 100 shares	100	100
Additional paid-in capital	312	312
Retained earnings	<u>1,087,351</u>	<u>1,349,614</u>
Total stockholders' equity	<u>1,087,763</u>	<u>1,350,026</u>
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	<u>\$ 1,706,749</u>	<u>\$ 1,978,997</u>
Borrower and investor custodial accounts (segregated in special accounts - excluded from corporate assets)	<u>\$ 614,068</u>	<u>\$ 487,203</u>

See notes to financial statements.

**BLACKBURNE & BROWN MORTGAGE COMPANY, INC.
AND AFFILIATE**

Statements of Income and Retained Earnings
For the Years Ended September 30, 2006 and 2005

Revenues:	2006	2005
Servicing fees	\$ 809,019	\$ 772,364
Amortization of mortgage servicing rights	(278,726)	381,924
Loan commissions	287,057	433,636
Arbitration & legal settlement fees	44,344	48,400
Fund management fees	132,000	132,000
Property management fees	33,844	74,880
Software licensing fees	868,702	673,248
Video and manual sales	220,129	158,083
Total revenue	2,116,369	2,674,535
Expenses:		
Salaries	852,279	761,304
Salaries - George Blackburne	310,783	378,494
Salaries - Francisca Blackburne	43,125	28,482
Marketing	362,085	352,561
Outside consultants	201,710	153,879
Rents	85,771	62,401
Payroll taxes	83,601	76,036
Legal	66,562	59,191
Office expense	60,922	62,893
Telephone and utilities	51,287	37,493
Other expenses	50,047	38,809
Retirement plan	50,000	50,000
Loan arrangement fees	48,749	53,184
Employee benefits	48,379	30,457
Insurance	39,301	44,922
Travel	34,292	40,710
Accounting	30,653	20,306
Depreciation	22,640	22,947
Automobile	10,708	9,875
Maintenance and repairs	10,221	2,947
Tax and license	7,251	12,587
Education	6,152	9,393
Bad debts	3,091	-
Dues and subscriptions	450	8,714
Total expenses	2,480,059	2,317,585
Income (loss) from operations	(363,690)	356,950

See notes to financial statements.

**BLACKBURNE & BROWN MORTGAGE COMPANY, INC.
AND AFFILIATE**

Statements of Income and Retained Earnings
For the Years Ended September 30, 2006 and 2005

	2006	2005
Income (loss) from operations (continued)	\$ (363,690)	\$ 356,950
Other income (expense):		
Interest income	191	78
Interest expense	(7,999)	(3,915)
Income from partnership	15,746	16,080
Other fees and income	19,629	12,206
Gain (loss) on investments	10,760	(9,286)
Total other income (expense)	38,327	15,163
Income (loss) before income taxes	(325,363)	372,113
Income tax expense (benefit)	(63,100)	130,188
NET INCOME (LOSS)	(262,263)	241,925
Retained earnings, beginning of year	1,349,614	1,107,689
RETAINED EARNINGS, END OF YEAR	\$ 1,087,351	\$ 1,349,614

See notes to financial statements.

**BLACKBURNE & BROWN MORTGAGE COMPANY, INC.
AND AFFILIATE**

Statements of Cash Flows
For the Years Ended September 30, 2006 and 2005

	2006	2005
Cash flows from operating activities:		
Net income (loss)	\$ (262,263)	\$ 241,925
Adjustments to reconcile net income (loss) to net cash (used) provided by operating activities:		
Depreciation	22,640	22,947
Amortization & impairment of mortgage servicing rights	1,059,751	560,268
Additions to mortgage servicing rights	(781,025)	(942,193)
Income from partnership	(15,746)	(16,080)
Deferred income taxes	(65,500)	128,020
(Gain) loss on investments	(10,760)	9,286
Changes in operating assets and liabilities:		
Receivables	6,798	(10,825)
Prepaid expenses	51	(131)
Prepaid income taxes	(1,700)	1,368
Advances	1,791	(2,785)
Accounts payable	26,451	34,237
Other payable	-	9,197
Accrued expenses	(5,936)	6,565
Net cash (used) provided by operating activities	(25,448)	41,799
Cash flows from investing activities:		
Net proceeds (purchases) of investments	1,658	131
Net proceeds (purchase) of property and equipment	(2,564)	(21,415)
Increase in investment in partnership	-	(105)
Net cash (used) in investing activities	(906)	(21,389)
Cash flows from financing activities:		
Net change in line of credit	50,000	(15,000)
Proceeds (principal payments) on notes payable	(15,000)	(14,010)
Net cash provided (used) in financing activities	35,000	(29,010)
Net increase (decrease) in cash	8,646	(8,600)
Cash, beginning of year	10,596	19,196
CASH, END OF YEAR	\$ 19,242	\$ 10,596

See notes to financial statements.

**BLACKBURNE & BROWN MORTGAGE COMPANY, INC.
AND AFFILIATE**

Notes to Financial Statements
September 30, 2006 and 2005

NOTE 1 - STATEMENT OF SIGNIFICANT ACCOUNTING POLICIES:

a. Organization -

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 and Brown Mortgage Company, Inc. 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.

**BLACKBURNE & BROWN MORTGAGE COMPANY, INC.
AND AFFILIATE**

Notes to Financial Statements
September 30, 2006 and 2005

NOTE 1 - STATEMENT OF SIGNIFICANT ACCOUNTING POLICIES (Continued):

g. Investments -

All securities are classified as trading securities and reported at fair market value in the balance sheet. Realized gains and losses are determined using the specific-identification method. Unrealized holding gains and losses are reported as income.

h. 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.

i. 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.

j. Income taxes -

The Company follows the provisions of Statement of Financial Accounting Standards No. 109 (SFAS No. 109), "Accounting for Income Taxes." Deferred income tax assets and liabilities are computed annually for differences between the financial statement and tax basis of assets and liabilities.

**BLACKBURNE & BROWN MORTGAGE COMPANY, INC.
AND AFFILIATE**

Notes to Financial Statements
September 30, 2006 and 2005

NOTE 1 - STATEMENT OF SIGNIFICANT ACCOUNTING POLICIES (Continued):

k. Advertising -

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

l. 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:

	<u>2006</u>	<u>2005</u>
Furniture and fixtures	\$ 37,674	\$ 37,889
Equipment	73,317	91,563
Computer equipment	33,293	30,729
Vehicles	<u>134,189</u>	<u>134,189</u>
Total	278,473	294,370
Less: accumulated depreciation	<u>200,179</u>	<u>196,000</u>
Net property and equipment	<u>\$ 78,294</u>	<u>\$ 98,370</u>

NOTE 3 - INVESTMENTS:

Investments consisted of \$0 and \$340 of options and \$52,832 and \$43,390 of mutual funds at September 30, 2006 and 2005, respectively. The following is a summary of investment earnings recognized in income for each year.

	<u>2006</u>	<u>2005</u>
Realized gains (losses)	\$ 1,559	\$ (723)
Unrealized gains (losses)	<u>9,201</u>	<u>(8,563)</u>
Gains (losses) on investments	<u>\$ 10,760</u>	<u>\$ (9,286)</u>

**BLACKBURNE & BROWN MORTGAGE COMPANY, INC.
AND AFFILIATE**

Notes to Financial Statements
September 30, 2006 and 2005

NOTE 4 - MORTGAGE SERVICING RIGHTS:

The activity in MSR's was as follows:

	<u>2006</u>	<u>2005</u>
Balance at beginning of period	\$ 1,722,682	\$ 1,340,757
Additions	781,025	942,193
Scheduled amortization & reduction due to early loan payoffs	(1,059,751)	(560,268)
Reserve for impairment	<u>-</u>	<u>-</u>
Mortgage servicing rights, net	<u>\$ 1,443,956</u>	<u>\$ 1,722,682</u>

The estimated fair value of recognized MSR's for the years ended September 30, 2006 and 2005 was \$1,443,956 and \$1,722,682, 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, 2006 and 2005, respectively, was approximately \$2,800,000 and \$3,000,000.

NOTE 5 - LINE OF CREDIT:

The Company has a \$150,000 available line of credit with First Northern Bank, which is due February 28, 2007. Interest is payable monthly at prime plus two percent. The line is secured by receivables and equipment of the Company. The balance outstanding as of September 30, 2006 and 2005, respectively, was \$70,000 and \$20,000.

**BLACKBURNE & BROWN MORTGAGE COMPANY, INC.
AND AFFILIATE**

Notes to Financial Statements
September 30, 2006 and 2005

NOTE 6 - NOTES PAYABLE:

Long-term debt consists of the following:

	2006	2005
Notes secured by vehicle - due in monthly installments of \$1,250 plus interest stated at prime plus 2 percent, maturing in January 2008.	\$ 20,000	\$ 35,000
Less: current portion	15,000	15,000
Amount due after one year	\$ 5,000	\$ 20,000

Future maturities of notes payable are as follows:

Year Ended September 30,	
2007	\$ 15,000
2008	5,000
Total	\$ 20,000

NOTE 7 - TRANSACTIONS WITH RELATED PARTY:

During the years ended September 30, 2006 and 2005, the Company received servicing revenue of \$302,503 and \$255,421, respectively, and collected management fees, including shared expenses, in the amount of \$141,000 and \$141,000 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 \$72,237 and \$56,491 at September 30, 2006 and 2005, respectively, and is reflected on the balance sheet as Investment in Partnership.

Additionally, during the years ended September 30, 2006 and 2005, the Company paid \$120,000 and \$148,000 to the Fund for promotional interest. The promotional interest was paid, as the general partner of the Fund, to help ensure the Fund would meet its expected rate of return to investors.

**BLACKBURNE & BROWN MORTGAGE COMPANY, INC.
AND AFFILIATE**

Notes to Financial Statements
September 30, 2006 and 2005

NOTE 8 - INCOME TAX EXPENSE (BENEFIT):

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

	2006	2005
Current		
Federal	\$ 800	\$ 568
State	1,600	1,600
Total current	2,400	2,168
Deferred		
Federal	\$ (39,782)	\$ 77,754
State	(25,718)	50,266
Total deferred	(65,500)	128,020
Total income tax expense (benefit)	\$ (63,100)	\$ 130,188

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 for tax purposes and the cash basis of accounting for tax purposes.

NOTE 9 - COMMITMENTS:

The Company leases its main office space under an operating lease with monthly payments of \$3,458 expiring on April 1, 2009. Additionally the Company leases office space under an operating lease with the Company's sole shareholder in Indiana expiring in November 2010, with monthly payments of \$3,000. Operating lease office rental expense was \$74,496 and \$48,181, respectively for the years ended September 30, 2006 and 2005.

The company also leases various office equipment under non-cancelable operating leases with total monthly payments of \$629.

**BLACKBURNE & BROWN MORTGAGE COMPANY, INC.
AND AFFILIATE**

Notes to Financial Statements
September 30, 2006 and 2005

NOTE 9 – COMMITMENTS (Continued):

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

<u>Year Ended September 30,</u>	
2007	\$ 77,496
2008	77,496
2009	56,748
2010	36,000
2011	<u>3,000</u>
Total	<u>\$ 250,740</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 to the plan for each of the years ended September 30, 2006 and 2005.

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 \$7,999 and \$3,915 for the years ended September 30, 2006 and 2005, respectively.

Additionally, the Company paid \$4,490 and \$5,023 in income taxes for the years ended September 30, 2006 and 2005, respectively.

**BLACKBURNE & BROWN MORTGAGE COMPANY, INC.
AND AFFILIATE**

Notes to Financial Statements
September 30, 2006 and 2005

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 on 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.