

A CHECKLIST FOR "REASONABLE" DUE DILIGENCE "THE SCORECARD"

Mason Alan Dinehart III RFC¹

Broker/Dealer due diligence on private placements, direct participation programs, real estate syndications and Tenant-In-Common (TIC) interests is a critical and fundamental step necessary for brokerage firms to determine whether to offer a security to its clients. Unlike publicly traded securities, there are no analyst or ratings agency reports available for review. Further, unlike publicly traded securities, rarely are there any standard corporate filings publicly made with the Securities and Exchange Commission. As such, when an investor is solicited to invest in a private offering by a broker/dealer, it is the obligation of the broker/dealer to have performed reasonable and independent due diligence on the offering. Whether the offering is a "non-conventional investment,"² a hedge fund,³ TIC,⁴ or Regulation-D private placements,⁵ due diligence is an obligation advisors and their firms have to the investing public.

In 1972, I had been with a real estate syndication firm known as Carlsberg Securities, Inc. for three years. I was the Branch Manager and Director of Due Diligence and Compliance. We syndicated all forms of real estate. Publicly, we specialized in mobile home parks and distributed our offerings through well-known wire-houses including Walston & Co. and Francis I. Dupont & Co. We were, in fact, the second real estate syndicator on Wall Street, preceded only by Pacific Plan in Northern California and immediately followed by Con-Cap and Prudential Bache. Privately, we

1. Mason Dinehart, III, RFC has been a securities industry professional since 1969. He has served as a FINRA/NASD arbitrator on ten cases and has also been retained as an expert witness by both investors and securities industry member firms in hundreds of FINRA/NASD, JAMS, AAA, NYSE, and PSE arbitrations. He has also been retained as an expert witness in California state and federal court. Mason currently holds the Series 7, 24, 63, 65, 79, and 99 licenses, and previously held the Series 27 license.

2. *See* FINRA NOTICE TO MEMBERS 03-71.

3. *See* FINRA NOTICE TO MEMBERS 03-07.

4; *See* FINRA NOTICE TO MEMBERS 05-18.

5. *See* FINRA REGULATORY NOTICE 10-22.

marketed raw land along with income properties including industrial, multi-family apartments and commercial office buildings. With regard to private placements, we were always sure to provide private placement memoranda (PPMs) to accredited investors with full treatment of all material facts (private offerings are exempt from registration, not disclosure) and to avoid any general solicitation (i.e., dropping PPM's out of helicopters).

Earlier that year, I was contacted by the Practising Law Institute (PLI) to request my participation in a five-person panel to be made up of four securities attorneys and myself, the only non-attorney on the panel. Its purpose was to travel to five U.S. cities to introduce and explain real estate syndication to members of the bar and bench. Included on the panel was Brad Cook, then Chairman of the SEC. My participation was requested to provide PLI attendees with an evaluation tool or arithmetic system to quantifiably evaluate and analyze the working aspects and deal points of a real estate syndication offering to better understand what could go wrong with these sponsored programs. After we returned from traveling, PLI asked me to write an article for the Fall 1972 issue of Real Estate Review on Real Estate Syndication. The article is titled "Selling Syndication Shares Successfully."

The article was about "due diligence," a relatively amorphous industry term which has no objective definition. This is especially important since the Securities Act provides no specific definition other than to call it a "reasonable investigation," which is, in turn, defined by the statute as including: 1) a high degree of care; 2) an investigation of facts; 3) identification of all facts material to the investor; and 4) non-reliance on management representations.⁶ FINRA adds that the investigation must be "reasonable."⁷ My definition is this:

Due-diligence is the process of reasonable investigation that independently evaluates and verifies a sponsor's accuracy, competency, financial strength and organizational depth. It is adversarial in nature and utilizes quantitative and intuitive means. It includes a comprehensive analysis that challenges the deal points,

6. 15 U.S.C. § 77k (2006); *see also* Distribution by Broker-Dealers of Unregistered Securities, Exchange Act Release No. 33-4445, 1962 WL 69442 (Feb. 2, 1962); 15 U.S.C. § 77k(c) (2006); 15 U.S.C. § 771(a)(2) (2006); *Escott v. BarChris Constr. Corp.*, 283 F. Supp. 643, 696-97 (S.D.N.Y. 1968); *Feit v. Leasco Data Processing Equip. Corp.*, 332 F. Supp. 581, 582 (E.D.N.Y. 1971); *The Obligations of Underwriters, Brokers and Dealers in Distributing and Trading Securities*, Securities Act Release No. 33-5275, 1972 WL 125474 (July 26, 1972).

7. *See* FINRA NOTICE TO MEMBERS 05-18.

assumptions and projections used in each direct participation program (OPP) examined. The process examines and determines the probability of the transaction achieving its stated objectives.

This definition has gone largely unchanged since I began performing due diligence on private offerings and real estate deals in 1969.

When it comes to securities industry due diligence, it is important to identify what independent due diligence is not. Independent due diligence is not a collection of third party due diligence reports.⁸ This is because these reports are paid for by the Sponsor, and on their face are not independent. One provider of these reports, Snyder Kearny, LLC, stated as a disclaimer in one of its reports,

[w]e specifically note that given the limited scope of our representation, we may not have independently verified factual statements contained in the PPM. Further our review is subject to the budgeted hours and may or may not be sufficient to consist of a 'reasonable investigation' or 'reasonable care' as such terms are defined in Sections 11 and 12 of the Securities Act of 1933, as amended. Unless expressly indicated in a separate legal opinion identified as such, we will not provide any opinion or legal advice regarding the adequacy of any investigation performed by us or the adequacy of the Offering disclosure.

With such disclaimers, broker-dealers should never rely solely on these firms to visit the property and examine the financial statements. Further, in an administrative proceeding, the SEC held that relying solely on third party reports constituted recklessness.⁹ Rather, the firms considering offering these deals should do it themselves. Further, these reports are outsourced and as such are not considered to be part of the broker-dealer's reasonable independent investigation.

So, I took the opportunity given to me at PLI, in analyzing Real Estate Direct Participation Programs, to develop the Real Estate ScoreCard (Exhibit A). As a securities expert witness, I have been using the Scorecard in arbitrations and mediations to evaluate literally hundreds of private placement limited partnerships, LLCs, TICs, non-traded REITs, along with numerous types of Public Offerings including REITs and L.P.'s. In addition to real estate offerings, I discovered it works very well for equipment leasing and oil and gas programs as well. I have found that an arbitration panel has a

8. See FINRA REGULATORY NOTICE 10-22 at 6-7.

9. See *Stires & Co.*, 67 S.E.C. Docket 1716, 1998 WL 462230 *7 (1998).

much better and more organized grasp of the offering by walking them through the Scorecard.

The Scorecard naturally breaks down into two sections. The first section – deal points 1 to 3 – evaluates the Sponsor or program manager. The next section – dealpoints 4 to 15 – analyzes the structure of the offering itself. Each of the deal points analyzed by the Scorecard are points that find their support in various FINRA/NASD Notices, SEC Releases, or from personal experience. Of the 15 deal points or questions, each one has five possible answers, with up to five points possible for each, or 75 total points possible. Each deal point is graded with five points being best and one point being worst as shown on the Scorecard master template. After the grading, the points are added up. A passing grade is 52 points or 70% of the possible 75 points. Passing is to say, that based upon the PPM or Prospectus, any supplements, and marketing brochures, the program qualifies to enter the formal due diligence process. In other words, the deal passes muster to the extent that it should meet "reasonable basis suitability" pursuant to FINRA Rule 2111, which means the offering could be suitable for at least some investors.¹⁰ It is important to note that scoring high on the Scorecard is difficult. In fact, the majority of deals fall in the 52-60 point range, with offerings rarely exceeding 60 points.

Importantly, the Scorecard is a precursor to formal due diligence, not a substitute for it. It is the initial independent due diligence that should be performed by the broker-dealer. If an offering fails to meet the minimum grade, the Scorecard should be forwarded to the sponsor in order to improve the program so that it can be approved and qualify to enter the formal due diligence process at some future date. The truth is, to conduct a full due diligence review on every direct participation program that comes in the door would be a very inefficient process. Only those that, on their face, have a chance to succeed should enter that process.

With that background in mind, the following is a question by question review of the Scorecard.

QUESTION 1-SPONSOR/MANAGER EXPERIENCE

Here, the sponsor or manager's syndication experience is analyzed. While it is helpful to know that the principals of the sponsor have "cumulatively" had many years of productive real estate experience, there

10. See FINRA REGULATORY NOTICE 10-22 at 4.

simply is no substitute for a promoter's direct experience dealing with acquisition and financing of properties in a packaged program where investors pool their capital and receive tax-deferred cash flow, equity buildup, and growth of principal. Further, it is helpful to know whether the syndicator has had experience dealing with a large number of investors and reporting on the program's progress from an investor services perspective. Specifically, it is very important to know how the sponsor has handled problems in the past.

Important to this analysis are the number of years a sponsor or manager has in syndicating, acquiring, financing, managing and selling direct participation programs for investors. This kind of experience rises well above merely buying and selling properties. It takes twenty years to earn five points in Question Number 1. One point can be added to the score of this deal point with some extensive personal real estate acquisition and management experience of one or more of the key principals of the company.

QUESTION 2 -FINANCIAL STRENGTH

With this deal point, the tangible net worth of the sponsor or manager backing the deal is examined. It is important to note, little credit should be given to would-be sponsors who are undercapitalized affiliates of a separate, main company sponsor, or parent company, which is not backing the deal but has simply loaned money to the affiliate in the form of a note to inflate the would-be sponsor's net worth. Again, what is measured here is the tangible net worth of a sponsor on a GAAP basis, where 20% or more of its assets are liquid and not an empty shell number. To meet this requirement, many sponsors provide financial statements that are not audited. This is true especially in private placements. However in the mid-2000's when deals by the carload were being offered, several large sponsors did provide audited financials during that time period. Examples include American Realty Capital, Vertical Financial Group (Mortgage Funds), DMMS and Argus. Interestingly enough, noted Ponzi schemes like Provident (Shale Royalties), Medical Capital and DBSI provided unaudited financials only. While audited, certified or reviewed financial statements help, they are no guarantee against fraudulent activities. But audited financials are better to have than not, and it should be mandatory for sponsors raising millions of dollars to provide them. Note that it takes \$15 million of tangible net worth to obtain five points on the ScoreCard. As a rule of thumb, the sponsor should have a net worth of no less than 10% of the sum it has raised in outstanding deals to date, including the one under consideration.

QUESTION 3-RESALE ACTIVITY

Here, the sponsor's track record of re-sales and refinancing is reviewed. What is usually listed in the profile of weaker sponsors is the number of programs, the number of investors and the total dollar amount of monies raised along with the cash flow distributions of prior programs and the cumulative number of years of experience of the firm's principals. Clearly, these items do not constitute "track record." Track record breaks down to two items only: re-sales and refmancing of the properties syndicated as shown in the PPM, nothing more. It is always helpful to list the re-sales and re-financings of the principals and one point can be added when warranted. Please note that it takes 30% of the sponsor's properties syndicated to have been sold or refinanced to warrant the top score of five points.

QUESTION 4-SPONSOR/MANAGER COMPENSATION

In this question, the sources of compensation the sponsor receives is analyzed and the amount is reviewed for reasonableness. To that end, subordinations are critical to this analysis. It is not necessarily the amount of compensation a sponsor or manager receives. Rather, it is the timing of this compensation. Does the Sponsor get paid before the investors? If the Sponsor's compensation is deferred pending investor payments, it's called subordinated compensation. While profits to the offering are usually subordinated, most other fees are not. It is refreshing when a sponsor subordinates some of its compensation to the projected investor return.

Sponsor compensation can take many forms in private offerings, including selling comm issions, leasing comm issions, construction management fees or asset management fees. The offering should get a higher score if the sponsor requires a cash distribution target to be met before receiving its share of compensation.

QUESTION 5-LOAD FACTORS

Question Five seeks to primarily determine what percentage of capital raised from investors is actually invested in the property or program. This can usually be found in the "Use of Proceeds" section of the offering document. Many sponsors want to define "load" as only the dollars that go directly to the sponsor. One sponsor of a large REIT, in the "Use of Proceeds" section, failed to show any acquisition fees in the front-end load.

This was because the deal was a "blind-pool" and the acquisition fees (6%) would only be incurred when the sponsor actually purchased the properties later on. Hence, all acquisition fees were shown as ongoing operational expenses. This is nonsense. These acquisition fees are clearly one-time, front end load expenses and would be incurred on every property purchased. They are not like management fees that are paid annually.

"Load" typically includes the following: sales commissions, organization and offering costs, non-accountable marketing and due diligence expenses, acquisition fees, loan placement and other fees, including closing costs. The remaining money raised goes into the property. One chairman of an arbitration panel once asked me if large wire houses were selling these private placement TIC real estate deals. I explained that they did not because of the loads involved. Typically, it is the independent broker-dealer community that sells these deals whereby only 73-76% of dollars raised goes into the property(s). The public funds like REIT have lower loads whereby 84-88% goes into the ground. Total compensation (commissions plus non-accountable marketing and due diligence fees) is in the 5-6% range for public funds versus a 7-9% range for the private offerings the independent broker/dealers sell. (Exhibit B)

QUESTION 6-GUARANTEES

In looking for some kind of operational guarantee for the property(s), a Master Lease would be an example. Then there is the repurchase account. In larger funds, for example, after one year or 18 months, the program will accept repurchase requests, in writing, of up to 5% of the capital raised on a first come, first served basis. Then there is the small print buried deep in the PPM: It will say under no uncertain terms that the sponsor will honor these requests only if they will not endanger the program financially. Further, this repurchase account may be terminated at any time by the sponsor. Clearly, these types of accounts are illusory at best and should never be counted on, especially in emergencies. You can be sure that if there are any clouds on the horizon, the repurchase account will vanish in a heartbeat.

QUESTION 7-SELF-DEALING

This question is about conflicts of interest. It is critical to know how many services the sponsor is selling to himself. At the top of the list is a sponsor that purchases properties from itself or its affiliates. This is

especially egregious if there is a mark-up on these purchases. Then, some sponsors will have an insurance subsidiary who sells property and casualty insurance to the program at inflated rates. Finally, if the original property acquisition comes from an independent third party seller, it is important to know what the percentage mark-up is to the investors. Typical mark-ups range between 10%-12% but markups as high as 25%-30% are not unheard of.

While the numbers are usually disclosed in the PPM, only by subtracting the third-party purchase price from the loaded cost (equity raised plus the debt) will you know the true total of the mark-up. Finally, unsubordinated compensation is a conflict, and the tax opinion backing the offering must have at least a "should" opinion by counsel. In an LLC, the weakest of opinions is "more-likely-than-not" and a "will" opinion is best. The minimum standard is that the offering "should" not be treated as a real estate partnership, from a tax perspective.

QUESTION 8-INVESTOR VOTING RIGHTS

While the investors are passive and have no real voice in management, there are always some voting rights reserved even for passive investors. TICs, for example, require unanimous consent of all the investors for most voting rights. An example of a "passive investor" voting right would be the percentage required to remove the LLC Manager. The real question to determine is, whether the LLC Manager can only be removed "for cause." This is usually very difficult to prove. Typically, willful misconduct must be demonstrated. Bad faith, fraud, or gross negligence of the manager under the definition of cause are examples and must be demonstrated as well.

Short of being a convicted felon, the manager is probably going to be able to tie the investors up in extended litigation for many years if they try to remove him. The best of all scenarios is to have an offering that only requires a simple majority to amend the operating agreement, approve the sale of all or substantially all of the properties, approve any "roll-up," approve any change in the deal's investment objectives, approve any refinancing of the property or fire the manager. In offerings where unanimous consent is required, the investors should be able to remove the LLC Manager without cause.

QUESTION 9-LEVERAGE

Most importantly, the percentage of leverage is the debt related to the original purchase price from the third party seller. That is actual leverage at the real estate level. Then of course there is the "loan to value," the debt divided by the appraised value, which also should be determined. On the Scorecard, an all-cash purchase or debt of no more than 39% would achieve a top score of five.

QUESTION 10-FINANCING

Here the terms of the loan are reviewed. Fixed, 30-year loans are virtually non-existent in real estate offerings currently. The best loans available are typically 7-10-year loans with as many years of interest only payments as possible will receive the best score. The ability to prepay the loan after some period is additionally important. Further, cross default or cross collateralization requirements by the lender on the part of the sponsor should be reviewed because it is preferable to avoid dealing with the sponsor's problems related to other properties that could affect the offering's property(ies). Finally, the "bad-boy" carve-outs (recourse guaranty) on any non-recourse loans obtained should be reviewed. These provide for personal liability against the borrower and principals of the borrower upon the occurrence of certain enumerated bad acts committed by the borrower and its principals.

QUESTION 11- VALUATION RATIO

This important question deals with the percentage of the appraisal amount to the loaded cost of the offering. Take the "as-is" appraisal amount and divide it by the loaded cost to the investors (equity raised plus the debt). Frequently this ratio is at or below 8%, which is unacceptable. So, if this is the case for the deal being reviewed, it must be scored down. What is preferred is a ratio of 95% to 100% appraisal to loaded cost which is the fairest to the investors. This ratio is one of the most important elements on the Scorecard. Finally, always be sure that the appraisal is honest and straight forward and not "made as instructed" (MAI).

QUESTION 12 - ASSUMPTIONS

This question is the very heart of the Scorecard. First, it tests the projections by determining if any CPA, legal or accounting firm signed off on them, or if they were simply not reviewed and prepared by the sponsor. The latter is usually the case. A classic assumption is the yearly rental rate increases, which typically go unsupported in the PPM but go to the core of the ultimate success or failure of the property. Are the yearly rental rate increases realistic? A projection of annual rental increases of 50¢ every year is abnormally high and unrealistic.

The next issue to examine is the cap rate on acquisition. That percentage is determined by taking the projected first year Net Operating Income (NOI) and dividing it by the loaded cost. It is not uncommon to find a cap rate below 6% at acquisition. Given the speculative nature of most real estate offerings, this number should be at least 2-3 percentage points higher than a quality corporate bond rate due to the high risk involved. Next, review the terminal cap rates on resale. It is fundamental that these should be the same as the purchase cap rates, but they rarely are. They are backed into by sponsors many times. Since the lower the cap rate, the higher the price, lower terminal cap rates differing from the purchase cap rates are often chosen which are unrealistic. This is especially true when interest rates are clearly projected to rise over the next 7-10 years.

The next issue to examine is the holding period. Extra points are given to a sponsor that puts a limitation on the number of years for reinvestments during the holding period. An example of a "good deal" for investors pertaining to the holding period is, after seven years the reinvestment period ends. In other words, no additional reinvestments in new properties with sales and refinancing proceeds, i.e., capital events, are allowed. The deal stops here. After seven years, all monies from capital transactions begin to be distributed back to the investors in a self liquidating fashion. This arrangement is the fairest to the investors and warrants a higher score. Further, it is in accord with the NASAA Guidelines.¹¹

Finally, search for any "yield enhancements" or financial engineering used by sponsors. Examples of financial parlor tricks would be interest rate buy-downs, deferred management fees, rental credits, negative master lease spreads, sponsor leased-back space/units, paying cash flow from reserves or

11. See NASAA OMNIBUS GUIDELINES (*adopt.* Mar. 29, 1992, *amend* May 7, 2007), available at http://www.nasaa.org/wp-content/uploads/2011/07/If-Omnibus_Guidelines.pdf.

an unsupported basis for projections/assumptions. These games played by sponsors are exposed on the Scorecard.

QUESTION 13- PERCENTAGE OF SUPPLY TO DEMAND

This question begins with determining what percentage of leases with tenants would expire within the next five years, six years, and so on. Then it is important to analyze tenant termination options for lease stability. Most important is to check with local real estate brokers to learn the actual vacancy rate for the same type of property you have within the specific sub-market the offering is located in. Many sponsors tend to pick a number off a bus in stating what the occupancy percentage is, both current and projected. Finally, it is critical to determine what the competition is with respect to the type and location of the property you have. From the answers to these questions, you can easily determine a percentage grade for the offering you're analyzing.

QUESTION 14 -CONSIDERATION PER SQ.FT.VS.THE COMPETITION

This is a simple comparison. A direct real estate investor, considering buying this same property in the offering, would buy it for a simple negotiated real estate commission, i.e., 5% on average. However, an investor in a syndicated offering is buying a direct participation program through a broker-dealer, and is paying a load of much more than that. Simply add the load from Question #5 to 100% and you have your answer. If the load is 25%, the offering scores 1 point (125%) on the Scorecard compared to 105% in the direct real estate marketplace.

QUESTION 15-RISK FACTORS

Unquestionably, there is risk in every real estate transaction. The question here is whether the risks in this particular transaction are magnified above the norm. Examples of high-risk factors include an extraordinarily high mark-up on acquisition, an abnormally high load, unrealistically aggressive assumptions, investor credit impairment, a below 85% appraisal amount to loaded cost ratio along with an extraordinarily high percentage of leases coming due in five years. If some or all of these attributes described above exist, plus there are a number of items of unsubordinated

compensation to the sponsor, the deal will probably score close to one point on the Scorecard.

This entire evaluation method is really a due diligence check list; a quantifiable tool to evaluate direct participation program offerings. Of course this method is not perfect. In using it hundreds of times since 1972, my experience with the Scorecard reflects an overall 76% success ratio. In other words, over 75% of the time, when I have scored an investment offering below 52 points, the offering has eventually failed. This means the property has been foreclosed upon by the lender; the sponsor has been declared fraudulent; the loan is in default; or it has been classified as a Ponzi scheme; or has stopped providing cash distributions with no hope of restoration.

The same is true of offerings that have passed the check list. For the balance of the 24%, it is too early to tell in many cases whether the programs will ultimately succeed. Something to really keep in mind at this time is that all those ten year "due and payable" loans issued from 2005 through 2007 will now be maturing in 2015-2017. This necessarily will place a great deal of refinancing pressure on lenders in the real estate marketplace as well as finalizing many outstanding real estate deals. Some other programs have recovered somewhat, but may be wavering a bit with the final results still undetermined. I only count in the 76% the programs whereby a resolution has been finalized.

Since a PPM or prospectus is hundreds of pages in length, the Scorecard breaks the deal down into five or six pages in a logical format that the trier of fact can understand and appreciate. It makes it much easier for an arbitrator or mediator to verify the deal points of the program by hearing the Scorecard presentation and then referencing the Table of Contents in the offering document.

In preparing this article, I reviewed a private placement deal much of PIABA is quite familiar with, Medical Capital. As you can see from the review attached as Exhibit C, the Medical Capital IV offering failed the Scorecard miserably, scoring only 30 points out of 70. Thus, Medical Capital IV should have never made it past the first level of due diligence compliance and certainly should have never been offered to investors because the offering failed the basic reasonable basis suitability test.

F E N D

**Mason A. Dinehart
5529 Bedford Avenue
Los Angeles, CA 90056**

Description

Limited Liability Company ScoreCard

Name of Offering:

Name of Sponsor:

*THE FOLLOWING INFORMATION IS ONLY INTENDED FOR REVIEW BY
BROKER DEALERS AND NOT AUTHORIZED FOR DISTRIBUTION TO THE PUBLIC*

LLC MANAGER - SPONSOR

1. LLC Mgr. Experience _____

(# yrs in this business)

- a) 20 years or more (5 pts)
- b) 15 - 19 years (4 pts)
- c) 10 - 14 years (3 pts)
- d) 6 - 9 years (2 pts)
- e) 2 - 5 years (1 pts)

2. Net Worth Consideration (GAAP): _____

(Assumes 20% or more = liquid)

- a) Greater than \$15 million (5 pts)
- b) \$10 to \$15 million (4 pts)
- c) \$5 to \$10 million (3 pts)
- d) \$2.5 to \$5 million (2 pts)
- e) \$1 to \$2.5 million (1 pts)

3. Resale Activity: _____

(% of properties sold or refinanced)

- a) More than 30% (5 pts)
- b) 20% to 29% (4 pts)
- c) 10% to 19% (3 pts)
- d) Less than 10% (2 pts)
- e) None (1 pts)

OFFERING STRUCTURE

4. Compensation: _____

(mgmt fees/cash flow/RE comm/
sale profits)

- a) Fees subordinated in all 4 areas (5 pts)
- b) Fees subordinated in 3 areas only (4 pts)
- c) Fees subordinated in 2 areas only (3 pts)
- d) Fees subordinated in 1 area only (2 pts)
- e) Fees not subordinated (1 pts)

5. Load Factors: _____

- a) Less than 20% (5 pts)
- b) 20% to 21.9% (4 pts)
- c) 22% to 23.4% (3 pts)
- d) 23.5% to 25% (2 pts)
- e) More than 25% (1 pts)

6. Guarantees: _____

- a) Mgr. will advance fund to the LLC without creating debt to the LLC (5 pts)
- b) Mgr. will loan funds which are fully subordinated (4 pts)
- c) Mgr. provides a 3 yr or more operational guarantee (3 pts)
- d) Mgr. will loan funds, but they are not subordinated (2 pts)
- e) Mgr. makes no representation about funding (1 pts)

7. Self-Dealing: _____

(buying properties owned by the Mgr. w/mark-up: taking loans points; liability insurance or leasing commissions; unsubordinated real estate commissions)

- a) "arms length" transactions or none of the above (5 pts)
- b) Mgr. pays himself using 1 of the above items (4 pts)
- c) Mgr. pays himself using 2 of the above items (3 pts)
- d) Mgr. pays himself using 3 of the above items (2 pts)
- e) Mgr. compensates himself using all 4 of the above (1 pts)

8. LLC Member Rights: _____

(replace Mgr. amend LLC agreement; approve sale or refinance; permit the Mgr. to resign*)

- a) Majority vote only required on all key items (5 pts)

- b) majority vote on 3 key items; more on 4th item (4 pts)
- c) majority vote on 2 key items; more on items 3-4 (3 pts)
- d) majority vote on 1 key item; more on items 2-4 (2 pts)
- c) more than majority vote needed on all key items (1 pts)

PROPERTY ACQUISITION

9. Leverage: _____

(consistent with the quality of the property, tenants and the objectives of the LLC defined as loan divided by 3rd party purchase price.)

- a) All cash to 39% (5 pts)
- b) 40% to 50% (4 pts)
- c) 51% to 60% (3 pts)
- d) 61% to 70% (2 pts)
- e) 71% and above (1 pts)

10. Financing: _____

- a) Current pay loan due in 15 or more years (5 pts)
- b) Current pay loan due in 11-15 years (4 pts)
- c) Deferred pay loan due in 6-10 years (3 pts)
- d) Deferred pay loan due in 5-8 years (2 pts)
- c) Deferred pay loan due in less than 5 years (1 pts)

NOTE: Deferred pay = accrued interest or zero coupon loan

11. Valuation Ratio: _____

(MAI appraisal divided by the LLC consideration: p/c = debt + capital raised)

- a) MAI is greater than 100% of p/c (5 pts)
- b) MAI is 96% to 100% of p/c (4 pts)
- c) MAI is 90% to 95% of p/c (3 pts)
- d) MAI is 85% to 89% of p/c (2 pts)
- e) MAI is less than 85% of p/c (1 pts)

PROPERTY PERFORMANCE/COMPETITION

12. Assumptions: _____

(Forecasts/Projections)

- a) "Big 5 Forecast: Rent/Inflation increases at or under 3%; 7.5% - 8.0% loaded cap rates on acquisition sale (5 pts)

- b) Conservative forecast 3% - 4%
Rent/Inflation increases 7.0% - 7.5%
Ld. cap rates on acquisition and sale (4 pts)
- c) Conservative projections 4% - 5%
Rent/Inflation increases 6.5% - 7.0%
Ld. cap rates on acquisition and sale (3 pts)
- d) Aggressive projections 5% - 6%
Rent/Inflation increases 6.0% - 6.5%
Ld. cap rates on acquisition and sale (2 pts)
- e) Aggressive projections 6% or more
Rent/Inflation increases 5.5% - 6.0%
Ld. cap rates on acquisition and sale (1 pts)

13. Percentage of Supply to Demand: _____

- a) 90% (5 pts)
- b) 95% (4 pts)
- c) 100% (3 pts)
- d) 110% (2 pts)
- c) 120% (1 pts)

14. LLC Consideration per sq. ft. _____

vs Competition: (Loaded vs Unloaded)

- a) 105% (5 pts)
- b) 110% (4 pts)
- c) 115% (3 pts)
- d) 120% (2 pts)
- e) 125% (1 pts)

15. Risk Factors (% of normal risk) _____

- a) 80% (5 pts)
- b) 90% (4 pts)
- c) 100% (3 pts)
- d) 110% (2 pts)
- e) 120% (1 pts)

TOTAL POINTS _____

NOTE: A minimum of 52 points is required for consideration. Most of our approved programs fall between 55 and 60 points. However, a score of "1" in any category may cause the offering to be rejected.

ScoreCards

Reproduction, photography or incorporation into any information retrieval system / or external or internal use is prohibited unless permission is obtained from the publisher. www.fend.com

F & N D

Mason A. Dinahart

5529 Bedford Avenue

Los Angeles, CA 90056

Description

Non-Traded REIT ScoreCard

Name of Offering:

Name of Sponsor:

**THE FOLLOWING INFORMATION IS ONLY INTENDED FOR REVIEW BY
BROKER DEALERS AND NOT AUTHORIZED FOR DISTRIBUTION TO THE PUBLIC**

REIT SPONSOR - MANAGER

1. Sponsor/Mgr. Experience
(# yrs in this business) _____

- a) 20 years or more (5 pts)
- b) 15 - 19 years (4 pts)
- c) 10 - 14 years (3 pts)
- d) 6 - 9 years (2 pts)
- e) 2 - 5 years (1 pts)

2. Net Worth Consideration: (GAAP):
(Assumes 20% or more = liquid) _____

- a) Greater than \$15 million (5 pts)
- b) \$10 to \$15 million (4 pts)
- c) \$5 to \$10 million (3 pts)
- b) \$2.5 to \$5 million (2 pts)
- b) \$1 to \$2.5 million (1 pts)

3. Resale Activity:
(% of properties sold or refinanced) _____

- a) More than 30% (5 pts)
- b) 20% to 29% (4 pts)
- b) 10% to 19% (3 pts)
- b) Less than 10% (2 pts)
- b) None (1 pts)

OFFERING STRUCTURE

4. Compensation:
(mgmt fees/cash flow/RE comm/
sale profits) _____

- a) Fees subordinated in all 4 areas (5 pts)
- b) Fees subordinated in 3 areas only (4 pts)
- b) Fees subordinated in 2 areas only (3 pts)
- b) Fees subordinated in 1 area only (2 pts)
- b) Fees not subordinated (1 pts)

5. Load Factors: _____

- a) Less than 12% (5 pts)
- b) 12% to 12.9% (4 pts)
- c) 13% to 13.9% (3 pts)
- d) 14% to 14.9% (2 pts)
- e) More than 15% (1 pts)

6. Guarantees: _____

- a) Mgr. will advance fund to the CO. without creating debt to the CO. (5 pts)
- b) Mgr. will loan funds which are fully subordinated (4 pts)
- c) Mgr. provides a 3 yr or more operational guarantee (3 pts)
- d) Mgr. will loan funds, but they are not subordinated (2 pts)
- c) Mgr. makes no representation about funding (1 pts)

7. Self-Dealing: _____

(buying properties owned by the Mgr. w/mark-up: taking loans points; liability insurance or leasing commissions: unsubordinated real estate commissions)

- a) "arms length" transactions or none of the above (5 pts)
- b) Mgr. pays himself using 1 of the above items (4 pts)
- c) Mgr. pays himself using 2 of the above items (3 pts)
- d) Mgr. pays himself using 3 of the above items (2 pts)
- e) Mgr. compensates himself using all 4 of the above (1 pts)

8. Stockholder Rights: _____

(replace Mgr. amend operating agreement; approve sale or refinance; permit the Mgr. to resign*)

- a) Majority vote only required on all key items (5 pts)

- b) majority vote on 3 key items; more on 4th item (4 pts)
- b) majority vote on 2 key items; more on items 3-4 (3 pts)
- b) majority vote on 1 key item; more on 2-4 (2 pts)
- b) more than majority vote needed on all key items (1 pts)

PROPERTY ACQUISITION

9. Leverage: _____
 (consistent with the quality of the property, tenants and the objectives of the REIT defined as non-recourse loan(s) divided by purchase price)
- a) All cash to 39% (5 pts)
 - b) 40% to 50% (4 pts)
 - c) 51% to 60% (3 pts)
 - d) 61% to 70% (2 pts)
 - e) 71% and above (1 pts)

10. Financing*: _____
- a) Current pay loan due in 15 or more years (5 pts)
 - b) Current pay loan due in 11-15 years (4 pts)
 - c) Deferred pay loan due in 6-10 years (3 pts)
 - d) Deferred pay loan in 5-8 years (2 pts)
 - e) Deferred pay loan due in less than 5 years (1 pts)
- NOTE: Deferred pay = accrued interest or zero coupon loan

*Notice to Stockholders of Mgrs. interest to incur secured or unsecured debt

11. Valuation Ratio: _____
 (MAI appraisal divided by the REIT consideration: p/c = debt + capital raised)
- a) MAI is greater than 100% of p/c (5 pts)
 - b) MAI is 96% to 100% of p/c (4 pts)
 - c) MAI is 90% to 95% of p/c (3 pts)
 - b) MAI is 85% to 89% of p/c (2 pts)
 - b) MAI is less than 85% of p/c (1 pts)

PROPERTY PERFORMANCE/COMPETITION

12. Assumptions: _____
 (Forecasts/Projections)
- 1) "Big 5 Forecast: Rent/Inflation increases at or under 3%; 7.5% - 8.0% loaded cap rates on acquisition sale (5 pts)

- b) Conservative forecast 3% - 4% Rent/Inflation increases 7.0% - 7.5% Ld. cap rates on acquisition and sale (4 pts)
- c) Conservative projections 4% - 5% Rent/Inflation increases 6.5% - 7.0% Ld. cap rates on acquisition and sale (3 pts)
- Rent/Inflation increases 6.0% - 6.5% Ld. cap rates on acquisition and sale (2 pts)
- e) Aggressive projections 6% or more Rent/Inflation increases 5.5% - 6.0% Ld. cap rates on acquisition and sale (1 pts)

13. Percentage of Supply to Demand: _____
- a) 90% (5 pts)
 - b) 95% (4 pts)
 - c) 100% (3 pts)
 - d) 110% (2 pts)
 - e) 120% (1 pts)

14. REIT Consideration per sq. ft. vs. Competition: (Loaded vs Unloaded) _____
- a) 105% (5 pts)
 - b) 110% (4 pts)
 - c) 115% (3 pts)
 - d) 120% (2 pts)
 - e) 125% (1 pts)

15. Risk Factors (% of normal risk) _____
- a) 80% (5 pts)
 - b) 90% (4 pts)
 - c) 100% (3 pts)
 - d) 110% (2 pts)
 - e) 120% (1 pts)

TOTAL POINTS

NOTE: A minimum of 52 points is required for consideration. Most of our approved programs fall between 55 and 60 points. However, a score of "1" in any category may cause the offering to be rejected.

ScoreCards

Reproduction, photocopying or incorporation into any information retrieval system / or external or internal use is prohibited unless permission is obtained from the publisher. www.fend.com

EXHIBIT B

FEES AND USE OF PROCEEDS

Syndication Fees

		Percentage
<i>Offering Size</i>	\$5,300,000	100%
B/D Sales Commission	\$318,000	6.00%
Due Diligence Allowance	\$26,500	0.50%
Organization (legal, syndication)	\$106,000	2.00%
Wholesale Fees & Exp	\$79,500	1.50%
Total Syndication "Load"	\$530,000	10.00%

Other Fees

Closing Costs	\$150,000	2.83%
Sponsor Acq Fee (Pd. by Seller)	\$300,000	5.66%
Lender Underwriting	\$70,000	1.32%
Lender Req. Reserves (RenQ)	\$50,000	0.94%
Total Other Costs	\$570,000	10.75%
 Available for Purchase	 \$4,200,000	 79.25%

PROMISSORY NOTE - PRIVATE PLACEMENT SCORECARD

Name of Offering – MEDICAL PROVIDER FINANCIAL CORP. IV, a NV Corp.; Private Placement Memorandum - Dtd. May 2, 2007

Size – \$150,000,000 – Series II Redeemable Secured Notes – 150,000 notes will be issued in denominations of \$1,000 with a minimum investment of \$50,000 per investor and increments of \$1,000, thereafter. Accredited Investors, only, through Section 4(2) of the Securities Act and Rule 506 of Regulation D.

Sponsor Medical Capital Holdings, Inc. Anaheim, CA. The Administrator/Loan Underwriter is Medical Capital Corporation, an affiliate; Loan Servicer – Medical Tracking Services, Inc. ("MediTrak"), an affiliate; Trustee – Bank of New York The proceeds from the sale of our notes will be used to (a) purchase healthcare receivables; (b) make loans secured by assets (c) purchase businesses and interests in businesses; (d) provide funds for general operating purposes, including paying the fees of the trustee and fees associated with maintaining the lockbox accounts; and (e) pay principal and interest on the notes.

Description – The Company is in the business of purchasing non-recourse medical receivables at a discount and collecting 100% of the proceeds for a pre-determined rate of profit. Receivables are typically purchased in batches valued at between \$25,000 and \$1,250,000. Each batch is treated separately with regards to the 25% reserved account limit. All principal and interest payments on purchased receivables are deposited into a lock box unique to the seller or borrower. The Lock Box is in the name of the Special Purpose Vehicle (e.g. MPFC IV). Purchases come from payors such as U.S. government entities, insurance companies and large self-insured corporations along with receivables from physicians and physician groups, smaller hospitals, medical equipment distributors and other health industry providers. This predetermined rate of profit is based upon the assumption that 100% of the purchased receivable is in fact, collectable. The notes will have a term of three and seven years and will be sold in classes and will have the following terms:

which has been in business since 1996. MCH acts as a holding company for 4 major operating subsidiaries, all of which are engaged in healthcare related businesses. The Administrator, Medical Capital Corporation, runs the day to day operations of the Company in terms of administration, underwriting and originating healthcare receivables purchase and performing marketing, sales and client support functions. Medical Capital has been in business since 1994 and has administered over \$2.5 billion in accounts receivables on behalf of affiliated companies to date. The Servicer, MediTrak has been facilitating the manual and electronic tracking of healthcare receivables since 1997.

SCORE : 3

2. Net Worth Consideration – No financial statements are contained in the PPM, whatsoever. The company indicates that the unaudited consolidated financial statements for Medical Capital Holdings, Inc. and Subsidiaries for the years ending December 31, 2004 and 2005, respectively, and reviewed by Mayer Hoffman McCann P.C., a lesser known local CPA firm, reflect a net worth of \$11.6 million for 2004 and \$15.6 million for 2005. However, the debt to equity (net worth) ratio increased from 27.0 to 1 in 2004 to 36.3 to 1 in 2005 (\$313 million of debt in 2004 to \$567 million of debt in 2005). This increase in negative debt to worth ratio added to unaudited financial statements indicates a company that is significantly overleveraged and apparently unwilling to provide the usual and customary required transparency (audited financials) for a company that was raising \$250,000,000 in 2007. 2006 financials were not yet available!

SCORE : 1

3. Resale Activity (Track Record) – With respect to prior performance, none of the prior programs of MCH has gone full cycle. However MCH has raised \$1,800,000,000 in institutional and private securities offerings, and based upon public records and representations of MCC management, neither MCH, the Company, nor any affiliate has ever defaulted on a contractual repayment of principal or interest payment.

SCORE : 3

4. Compensation – Medical Capital will receive an unsubordinated Administrative Fee equal to the amount in the Trust Account that exceeds the amount needed for the collateral coverage ratio to equal 100%, after all

required payments of the trustee, servicer and lockbox fee and all principal and interest then due on the Notes. As a servicing fee, MediTrak, an affiliate receives \$3.00 per receivables claim item, a monthly minimum fee of \$200.00 per provider, \$2,000 per seller as a one-time set-up fee and \$2,000 per seller as a one-time data interface fee, all unsubordinated. In addition, the Company receives a Discount Fee of approximately 7.0% to 8.0% of the Expected Net Receivables (ENR), on average on each receivables purchase. This fee may be adjusted for future purchases. This fee is paid to the Company, unsubordinated, and includes referral affiliate fees of undisclosed amounts.

SCORE: 1

5. Load Factors – Sales Comm. – 6.00%; Org. and Offering costs – 0.13%; Acquisition (discount) fee – 7.0% - 8.0% of ENR on each receivables purchase; for a total of 13.63%.

SCORE: 5

6. Guarantees -The Note Agreement does not require a sinking fund for payment of the Notes or require the maintenance of any particular financial ratios to better ensure future repayment of the Notes. The sponsor may loan funds but they are not subordinated.

SCORE: 2

7. Self-Dealing (Conflicts of Interest) – The Company has conflicts of interest that may result in its taking actions that are not in the investor's best interest. A common management group directs the activities of the companies in the affiliated group that provide services to it. These companies have also engaged in financing transactions similar to the sale of the notes. One of its affiliates, Medical Capital Corp. the administrator, determines which affiliate will fund the purchase or financing of accounts receivable and other assets from a given seller or borrower based on various factors including transaction size relative to size of the purchasing or financing affiliate and amounts currently committed by each affiliate versus each affiliate's funds available for the purchase or financing of accounts receivable and other assets. Another criterion is maintaining diversification within each affiliate's portfolio. From time to time, these criteria may cause Medical Capital Corp. to direct the sale of accounts receivable and other assets from one affiliate to another. Sales of accounts receivable and other

assets among affiliates are generally priced at the sum of the total amount advanced to the seller of the transferred accounts receivable plus the unearned portion of the discount fee, less any collections already received on the accounts receivable, or in the case of a transfer of a debt obligation owed by a borrower, the principal amount outstanding under the related financing agreement. These conflicts which arise may not be resolved in the best interests of investors.

Medical Capital Corp. is the administrator for the accounts receivable. The amount that the fact value of an account receivable is discounted when the account receivable is discounted when the account receivable is purchased will be determined by the administrator based on the underwriting criteria it has established. The Company could be adversely affected if the administrator requires the seller's accounts receivable to be discounted at higher rates than those the seller is accustomed to receiving. This could result in sellers being unwilling to sell, or discouraged from selling all, their accounts receivable to the Company. Finally, the Company expects to purchase some healthcare accounts receivable from its parent Medical Capital Holdings. The purchase price for these transactions is determined by Medical Capital Corporation. There are no specific criteria established to guard against the price being greater or less than the fair market value of the receivables at the time of the transaction.

SCORE :2

8. Investor Rights – As a noteholder, investors have very limited rights to vote on actions involving the company. There seemingly are no typical investors rights to sell all or substantially all of the loan assets, terminate the program or fire the Administrator, Medical Capital Corporation. If an event of default occurs, either the trustee or the noteholders of more than 50% in principal amount of the outstanding notes as to which the event of default occurred may declare the principal of those notes to be immediately due and payable. Under some circumstances, the noteholders of more than 50% in aggregate principal amount due on the outstanding notes may rescind any acceleration with respect to the notes and its consequences or waive an event of default, except for a failure to pay principal and interest when due. Modification and amendment of the note agreement or the notes may be made by MCC and the trustee with the consent of the noteholders of more than 50% of the principal amount due on the outstanding notes, or the notes of a particular series if only that series would be affected. However, unanimous consent is required to (1) extend the maturity date of any note; (2) reduce the principal amount due on, or redemption price of, any note or

alter the manner or rate of accrual of interest on any note; (3) reduce the aggregate principal amount on the notes required for consent to a supplemental note agreement or a change in the note agreement; or (4) result in the creation of any lien on the collateral securing the notes other than a lien ratably securing all of the obligations under the note agreement with respect to the notes at any time outstanding except as otherwise provided in the note agreement.

SCORE 2

9. Leverage – High sponsor leverage – Debt to worth ratio increased from 27 to 1 in 2004 to 36 to 1 in 2005. The program itself of course is over 90% leveraged.

SCORE 2

10. Financing – The Company takes a first priority security interest in each receivable and files a UCC-1 financing statement covering the purchase. There is no cross-collateralization between the previously issued Series I Notes and the Series II Notes being offered. Loans are adjustable with a spread of 1.5% - 2.0% over prime and between 3 and 7 years in duration.

SCORE 2

11. Assumptions – This program is much higher risk than MPFC III, with loans that are much longer and with double the receivables (40%) that are over 90 days old and double the amount that can be invested in loans for Business Investments.

Medical Capital normally requires that:

- (1) The provider to be properly licensed and to have no unresolved legal or medical issues;
- (2) The provider to have been in business in the community for a minimum of 18 months;
- (3) The seller to demonstrate credit-worthiness as determined by assessment of credit reports, past receivables, financing history, bank references, financial statements, accounting firm comments and UCC-1 searches;
- (4) The seller to pledge all of its receivables, existing and future, as additional collateral, and to establish up to a 25% reserve account; and

(5) One or more principals of the seller to guarantee performance by the seller of its covenants under the receivables purchase agreement.

Since the program operates totally without a sinking fund, and with no ability to redeem or transfer Notes, one would hope that the loan criteria would be iron clad. However, with words like "normally" and "up to" (25% reserves) this is clearly not the case. The expected holding period of the loans is shorter (generally 9 - 12 months per management discussions). Further, exposure to a single payor is limited to 15% and exposure to Medicare and Medicaid is limited to 50% of receivables. Approximately 80%, but no more than 90% of the Expected Net Receivable amount is paid to the seller immediately. The remainder of the purchase price, net of the discount fee, is deferred and allocated to the reserve account. Funds in excess of 25% of uncollected receivables are released to the seller

The Company has not obtained nor does it intend to obtain an opinion of counsel with respect to the tax consequences of purchasing, owning, or disposing of the Notes. If the Notes were to be treated as equity investments rather than indebtedness for federal income tax purposes, income might be significantly different in amount and character than interest income on the Notes. Once again, the Company fails to spend necessary money on a qualified tax opinion. Finally, none of the directors of MPFC IV noted on page 32 - 33 of the PPM are independent, which could cause significant problems given the myriad of related and conflicted transactions and contractual relationships by and among the Company, MCC, MCH and MediTrack and is very troubling.

SCORE: 1

12. Percentage of Supply to Demand - The Company encounters significant competition in its healthcare finance business from numerous commercial banks, diversified finance companies, secured lenders and specialty healthcare finance companies. Many of these competitors have greater financial and other resources than MPFC III and may have significantly lower cost of funds because they have greater access to insured deposits of the capital markets. Moreover, some of these competitors have significant cash reserves and can better fund shortfalls in collections that might have a more pronounced impact on companies such as MPFC III. They also have greater market share.

In addition, accounts receivable sellers often seek alternative sources of financing from a number of sources, including venture capital firms, small business investment companies, suppliers and individuals. As a result, the Company competes with a significant number of local and regional sources

of financing and several large national competitors. Some of these companies may also have greater experience and more efficient collection methods than MPFC III might develop. If the Company unable to successfully compete with these companies, its business could be adversely affected.

SCORE 2

13. Note Program Consid. v. Competition - 113.6%

SCORE:2

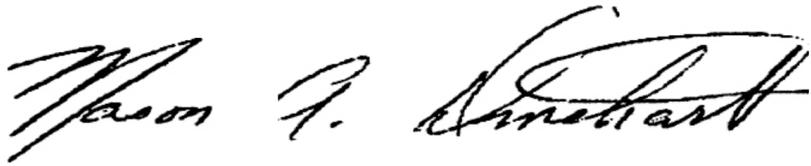
14. Risk Factors (% of Normal Risk) – 1) Liquidity risk; 2) High risk of loss and chance to lose the entire investment; 3) Limited operating history in the healthcare field; 4) Concentration risk in the healthcare field; 5) Limited experience outside the healthcare field; 6) Limited experience in making loans; 7) Collectability problems; 8) If default remedies are inadequate, the Company may not have sufficient funds available to pay the notes when they come due; 9) Conflict of interest risks; 10) Tax risk; 11) Government regulation risk; 12) Liability under HIPAA laws; 13) Lack of a sinking fund; 14) Lack of any independent directors; 15) Investments may lose value; 16) The Company may be required to rescind sales of some notes; 17) Lack of audited financial statements; 18) High debt to worth ratios for the Company; 19) Unsubordinated fees to management; 20) No minimum offering requirement; 21) No prior loan programs have gone full cycle.

SCORE 2

*Minimum Acceptable - 49 of 70 = 70% Total Score -30 of 70 = 43%

14 areas are analyzed and rated 5 points for best to 1 point for worst. A 70% passing grade is required to have the program enter the due diligence process. A score of "I" in any one category may cause the offering to be rejected. Question 11 (Appraisal to loaded cost) is eliminated since there is no evaluation.

A score of 30 is 19 points below the minimum needed to be qualified to enter the due diligence process. Finally, since this program fails to meet reasonable basis suitability, it should not be recommended to any investor.

A handwritten signature in black ink, appearing to read "Mason A. Dinehart III". The signature is fluid and cursive, with a large, stylized initial 'M'.

Mason A. Dinehart III, RFC
Securities Expert Witness
FINRA Arbitrator # A30388
Register Principal Due Diligence
Silber Bennett Financial, Inc.