



Nicholas Schorsch Cheated Investors in Recent Nontraded REIT Mergers

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Roll-ups

Recently we posted *More Non-traded REIT Perfidy: The Roll-up Grift* available [here](#).

To re-cap: Non-traded REITs are required by state securities regulators to include language in their bylaws which closely tracks the 2007 North American Securities Administrators Association's *Statement of Policy Regarding Real Estate Investment Trusts* (available [here](#)).¹

NASAA guidelines protect shareholders in REITs which have not been trading for at least 12 months before being rolled-up. The protections include the requirement for a contemporaneous independent appraisal of the nontraded REIT and the option for the nontraded REIT investors who vote against a proposed roll-up to receive their pro rata share of the appraised value in cash.

January 20, 2012, Mr. Schorsch Refines His Nontraded REIT Scam

American Realty Capital's Nicholas Schorsch has been a pioneer in the nontraded REIT industry. On January 20, 2012, Mr. Schorsch signed six Certificates of Correction for all six of the nontraded REITs he controlled. The six Certificates of Correction can be downloaded by clicking on the hyperlinks below.

[American Realty Capital Daily Net Asset Value Trust, Inc.](http://www.sec.gov/Archives/edgar/data/1501745/000144530512000528/v304180dnv33.htm) (January 20, 2012)

[American Realty Capital Healthcare Trust, Inc.](http://www.sec.gov/Archives/edgar/data/1499875/000144530512000532/v304182hc33.htm) (January 20, 2012)

[American Realty Capital - Retail Centers of America](http://www.sec.gov/Archives/edgar/data/1500554/000114420412009708/v302696_ex3-3.htm) (January 20, 2012)

[American Realty Capital New York Recovery REIT, Inc.](http://www.sec.gov/Archives/edgar/data/1474464/000144530512000541/ex34-arcnx1231201110k.htm) (January 20, 2012)

[American Realty Capital Trust](http://www.sec.gov/Archives/edgar/data/1410997/000114420412028152/v304866_ex3-1.htm) (January 20, 2012)

[American Realty Capital Trust III, Inc.](http://www.sec.gov/Archives/edgar/data/1503828/000144530512000525/arctiii12312011ex34.htm) (January 20, 2012)

¹ We have extensively researched non-traded REITs and concluded that these illiquid direct participation programs have cost investors \$50 billion compared to more liquid investments in traded REITs. Our *Fiduciary Duties and Non-traded REITs* (available [here](#)) provides a good overview of the problems with non-traded REITs and a summary of our empirical results. *An Empirical Analysis of Non-Traded REITs* (available [here](#)) contains a more detailed explanation of our research. Our previous blog posts on individual non-traded REITs are available [here](#).

With each Certificate of Correction, a passage in an American Realty Capital nontraded REIT's Corporate Charter which read as follows

“ROLL-UP TRANSACTION” means a transaction involving the acquisition, merger, conversion or consolidation either directly or indirectly of the Company and the issuance of securities of a Roll-Up Entity to the holders of Common Shares. Such term does not include:

(a) a transaction involving securities of the Company that have been for at least twelve (12) months listed on a national securities exchange; or...

was changed to read

“ROLL-UP TRANSACTION” means a transaction involving the acquisition, merger, conversion or consolidation either directly or indirectly of the Company and the issuance of securities of a Roll-Up Entity to the holders of Common Shares. Such term does not include:

(a) a transaction involving securities of a company that have been for at least twelve (12) months listed on a national securities exchange; or...

You can be forgiven for missing the change.

Mr. Schorsch changed “the Company” to “a company”. With this innocuous form, intended to be used to fix typos and other drafting errors, Mr. Schorsch eliminated shareholder protections he promised to investors as they were being duped into buying his nontraded REITs.

These Certificates of Correction were not immediately filed with the Securities and Exchange Commission as stand-alone documents attached to a Form 8-K where they might be noticed. Instead, they were referenced in exhibit lists at the end of four lengthy Form 10-K filings, one S-3 Registration Statement and one post-effective amendment to an S-11 Registration Statement, filed with the SEC, on average, 50 days after these highly consequential changes were made.

Mr. Schorsch is a Trailblazer; Cole Capital and Others Followed more than a Year Later

It took a while even for the other studied practitioners of the REIT gift to catch on to what a brilliant move Mr. Schorsch had made. A year later, on January 25, 2013 Cole Capital's D. Kirk McAllaster, Jr. signed Certificates of Correction for all five Cole Capital nontraded REITs as their Executive Vice President, Chief Financial Officer and Treasurer which were virtually identical to the ones Mr. Schorsch signed a year earlier. The Certificates changed “the Corporation” to “a corporation” in the REITs' Corporate Charters, eliminating shareholder protections required by NASAA as if he were correcting a typo.

None of the five Cole Capital Certificates of Correction were filed as stand-alone documents attached to a Form 8-K. All were referenced in exhibit lists at the end of lengthy Form 10-K filings, filed with the Securities and Exchange Commission on average 50 days after the change was made.

Cole Corporate Income Trust (January 25, 2013)

www.sec.gov/Archives/edgar/data/1490626/000149062613000027/ccitex3412312012.htm

Cole Credit Property Trust II. Inc. (January 25, 2013)

www.sec.gov/Archives/edgar/data/1308606/000130860613000004/ccptiexhibit3-5.htm

Cole Credit Property Trust III. Inc. (January 25, 2013)

www.sec.gov/Archives/edgar/data/1425923/000142592313000003/ccptiii12312012ex35.htm

Cole Credit Property Trust IV, Inc. (January 25, 2013)
www.sec.gov/Archives/edgar/data/1498547/000149854713000024/ccptiv12312012ex36.htm

Cole Real Estate Income Strategy (Daily NAV), Inc. (January 25, 2013)
www.sec.gov/Archives/edgar/data/1498542/000149854213000021/cinav1231201210kexhibit3-4.htm

Four more nontraded REITs played the Certificate of Correction sleight of hand in March and May 2014.

Industrial Income Trust Inc. (March 19, 2014)
www.sec.gov/Archives/edgar/data/1464720/000119312514110223/d697219dex31.htm

Industrial Property Trust Inc. (March 19, 2014)
www.sec.gov/Archives/edgar/data/1558441/000119312514145963/d713283dex34.htm

Dividend Capital Diversified Property Fund Inc. (March 26, 2014)
www.sec.gov/Archives/edgar/data/1327978/000119312514116702/d698902dex31.htm

Griffin-American Healthcare REIT II, Inc. (May 1, 2014)
www.sec.gov/Archives/edgar/data/1455271/000145527114000027/gahcr3form8k050114exh31.htm

Nontraded REIT Investors Have Suffered Real Harm as a Result of Mr. Schorsch's Abusive Innovation.

Seven of the nontraded REITs that “corrected” away shareholder protections were subsequently involved in a Roll-ups.

American Realty Capital Trust III, Cole Corporate Income Trust, Cole Credit Property Trust II and Griffin-American Healthcare REIT II were acquired in stock or stock and cash mergers while still nontraded REITs.

American Realty Capital Healthcare Trust, American Realty Capital Trust and Cole Real Estate Investments were acquired in stock or stock and cash mergers after they became listed REITs but before they had been listed for 12 months.

If the Sponsors for these seven REITs had not eliminated the Roll-up protections they committed to as a condition for registering securities for sale with abusive Certificates of Correction, shareholders would have been entitled to have an independent appraisal of the REIT they owned. Also, nontraded REIT shareholders who voted “No” would be entitled to receive their pro rata share of the appraised value in cash if the merger went ahead.

The problem with these seven mergers is not just that more of the consideration investors received would have been paid in cash rather than stock if the abusive Certificates of Correction had not been invoked. “Correcting” away the shareholder protections changed voting incentives. With the protections in place, a “No” vote would have given the voting shareholder the option to receive cash if the merger went forward. Without the protections, shareholders receive the same outcome regardless of how they vote. Shareholders thus have less of an incentive to vote “No” if the Sponsor eliminates the protections than if the protections are in place. Without the protections in place, the nontraded REIT shareholders might vote “Yes” because they prefer a less-than-equitable merger over no merger. However, that does not mean the shareholders would have voted the same way if the protections had allowed the shareholders the additional choice of an equitable cash merger.

Mr. Schorsch's Abusive Innovation Took \$100 Million at the Further Expense of Duped Investors

Mr. Schorsch has reportedly become a billionaire organizing and selling nontraded REITs through the third-tier, independent broker dealer network to trusting, unsophisticated, often elderly investors. That would certainly have been enough for most, but Mr. Schorsch is no run-of-the-mill grifter.

It's difficult to disentangle the web of affiliated entities controlled by Mr. Schorsch and figure out how much he took as a result of the questionable mergers identified above. The proxies for the mergers involving American Realty Capital Trust and American Realty Capital Trust III reflect that while Mr. Schorsch had only de minimus investment in these two REITs, Mr. Schorsch and AR Capital, a company he controlled, took at least \$139 million out of the merger proceeds otherwise available to investors in the nontraded REITs.

The proxy statement for the American Realty Capital Trust III merger (available [here](#)) shows on page 10 that the nontraded REIT's advisor received approximately \$59 million as a result of the merger. Page v names the advisor as American Realty Capital Advisors III, LLC, "wholly owned by AR Capital, LLC."

The proxy statement for the American Realty Capital Trust merger (available [here](#)) spells out Mr. Schorsch's personal payoff even more clearly. On page 9, the proxy reports that Mr. Schorsch owned 63.6% of AR Capital, and thus received \$40.2 million of a \$63.2 million fee paid to AR Capital. Page 11 lists another \$16.8 million Mr. Schorsch personally received because of the merger.