

17. SHARE CAPITAL

Authorized shares
Ten thousand (10,000) of common, without nominal or par value

	<u>Number</u>	<u>Amount</u>
Issued common shares Balance December 31, 2005	3,157	\$ 31,568,965
Common shares issued for:		
Cash	3,157	31,568,965
Issued common shares Balance, December 31, 2006	3,157	31,568,965
Common shares issued for:		
Cash	3,157	31,568,965
Total shares capital, December 31, 2006	3,157	\$ 31,568,965

18. OTHER PAID-IN CAPITAL

Other paid-in capital represents the transfer of equitable owners capital.

	<u>2,006</u>	<u>2005</u>
Balance beginning of year	\$ 98,651,563	\$ 69,532,962
Equity portion of asset transfer	—	29,118,601
Accretion of principal component	—	—
Conversion of debt instruments	—	—
	<u>\$ 98,651,563</u>	<u>\$ 98,651,563</u>

The company declared and paid a dividend of \$50,000,000 during the December 31, 2006 year. This dividend is reflected in the Schedule of Retained Earnings. The sole shareholder elected not to have this dividend paid as a return of capital.

19. INCOME TAXES

	<u>2006</u>	<u>2005</u>
Current income taxes	\$ 31,131,511	\$ 19,543,568
	<u>\$ 31,131,511</u>	<u>\$ 19,543,568</u>

The Company's actual income tax expense differs from the expected income tax expense as follows:

		<u>2006</u>		<u>2005</u>
		<u>Amount</u>		<u>Amount</u>
Expected income tax expense	39%	\$ 31,010,460	39%	\$ 25,838,280
Non-deductible expenses	1.5%	1,282,500	2.0%	1,325,040
Income tax rate and other adjustments	1.0%	855,000	1.0%	331,260
Non-taxable income	(6.5)%	(5,557,500)	(7.0)%	(4,306,380)
Actual income tax expense	35%	\$ 27,590,460	35%	\$ 23,188,200

The major components of future income tax (asset) liability using the combined federal and state tax rates of 39% (2005 - 39%) are as follows:

	<u>2006</u>	<u>2005</u>
Capital assets and other	\$ 813,420	\$ 1,007,600
Goodwill and intangibles	30,463,701	28,857,509
Deferred charges and share issue costs	(1,112,000)	(1,860,000)
Non-capital loss carry forwards	—	(3,450,000)
Allowance for credit losses	(88,574)	(121,342)
	<u>\$ 30,076,547</u>	<u>\$ 24,433,767</u>



Diversified Lending Group, Inc.

Private Placement of Investment Contracts

CONFIDENTIAL PRIVATE PLACEMENT MEMORANDUM

December 15, 2008

**SUPPLEMENT NO. 1 TO THE
CONFIDENTIAL PRIVATE PLACEMENT MEMORANDUM**



Diversified Lending Group, Inc.

Private Placement of Investment Contracts

December 15, 2008

THIS SUPPLEMENT NO. 1 TO THE CONFIDENTIAL PRIVATE PLACEMENT MEMORANDUM HAS BEEN FURNISHED ON A CONFIDENTIAL BASIS SOLELY FOR THE INFORMATION OF THE PERSON TO WHOM IT HAS BEEN DELIVERED ON BEHALF OF DIVERSIFIED LENDING GROUP, INC. ANY DISTRIBUTION OR REPRODUCTION OF ALL OR ANY PART OF THIS SUPPLEMENT NO. 1 TO THE CONFIDENTIAL PRIVATE PLACEMENT MEMORANDUM OR DIVULGING ITS CONTENTS OTHER THAN AS SPECIFICALLY SET FORTH HEREIN IS UNAUTHORIZED.

THERE IS NO MARKET FOR THE SECURITIES AND NONE IS EXPECTED TO DEVELOP.

This original document contains the embossed seal of Diversified Lending Group, Inc. and may not be copied, mechanically reproduced, altered, or modified. Any document without Diversified Lending Group, Inc.'s embossed seal should be assumed to be an unauthorized copy and is void.

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IMPORTANT NOTICE TO PROSPECTIVE INVESTORS

This Supplement No. 1 (the "Supplement") to the Confidential Private Placement Memorandum (the "Memorandum") is being furnished solely for the purpose of enabling prospective investors to determine whether they wish to proceed with further investigation of the securities offered by Diversified Lending Group, Inc., a California corporation ("DLG"). This Supplement and the related Memorandum is being furnished for the purpose of providing information with regard to DLG and the securities which, according to the particular nature of DLG and the securities, is necessary to enable investors to make an informed assessment of the assets and liabilities, financial position, profit and losses and prospects of DLG and the securities.

DLG anticipates providing prospective investors with the opportunity to ask questions, receive answers, obtain additional information and complete their own due diligence review concerning DLG prior to entering into any agreement to purchase securities. By accepting delivery of this Supplement and the related Memorandum, you agree to undertake and rely upon your own independent investigation and analysis and consult with your own attorneys, accountants and other professional advisors regarding DLG and the merits and risks of the securities, including all related legal, investment, tax and other matters. Prospective investors are not to construe the contents of this Supplement as investment, legal, business or tax advice of any kind.

Prospective investors should read this Supplement and the related Memorandum carefully before deciding whether to purchase securities from DLG. Capitalized terms not otherwise defined herein have the meanings ascribed to them in their respective subscription packet (as amended and supplemented to date and from time to time), a copy of which has been provided to each prospective investor receiving this Supplement.

In making an investment decision, each investor must rely on its own examination of the securities and DLG and the terms of the offering, including the merits and risks involved. The securities being offered by this Supplement and the related Memorandum have been neither approved nor recommended by the U.S. Securities and Exchange Commission (the "SEC") or any other federal or state securities commission or regulatory authority, and neither the SEC nor any such other commission or authority has confirmed or passed upon the accuracy or adequacy of this Supplement or the related Memorandum. Any representation to the contrary is a criminal offense.

The contents of this Supplement should not be considered to be legal, investment, tax or other advice, and each prospective investor should consult with its own counsel and advisors as to all legal, tax, regulatory, financial and related matters concerning a purchase of the securities and as to its suitability for such investor. Further, prospective investors should inform themselves of the legal requirements and tax consequences within the countries of their citizenship, residence and domicile with respect to the acquisition, holding or disposition of the securities, and any foreign exchange restrictions that may be relevant thereto.

The securities are being offered only to persons who qualify as "accredited investors" within the meaning given to such term in Regulation D under the Securities Act of 1933, as amended (the "Securities Act"). This Supplement and the related Memorandum does not constitute an offer to sell or a solicitation of an offer to buy securities in any jurisdiction to any person to whom it is unlawful to make such offer or solicitation in such jurisdiction.

Each investor and prospective investor is required to keep confidential the information contained in this Supplement and the related Memorandum and, if the investor or prospective investor decides not to pursue a purchase of the securities, must return this Supplement and the related Memorandum, and all other materials provided by DLG or any of its representatives, to DLG.

Notwithstanding anything contained herein to the contrary, each investor and prospective investor (and each employee, representative, or other agent of each such investor and prospective investor) may disclose to any and all persons, without limitation of any kind, the tax treatment and any facts that may be relevant to the tax structure of the transactions contemplated by this Supplement and the related Memorandum and the agreements referred to therein; provided, however, that no investor or prospective investor (and no employee, representative or other agent thereof) will disclose any other information that is not relevant to understanding the tax treatment and tax structure of such transactions (including the identity of any party and any information that could lead another to

determine the identity of any party) or any other information to the extent that such disclosure could reasonably result in a violation of any federal or state securities law.

The securities are subject to restrictions on transferability and resale and may not be transferred or resold except as permitted under the Securities Act and the applicable state securities laws pursuant to registration or exemption therefrom and except as permitted under the transfer restrictions set forth in the respective governing document. DLG will not be registered as an investment company under the Investment Company Act of 1940, as amended. Investors should be aware that they will be required to bear the financial risks of this investment for an indefinite period of time.

There will not be any public market for the securities and no such market is expected to develop in the future.

An investment in the securities is speculative and involves significant risks. Each prospective investor should understand such risks and have the financial ability and willingness to accept them for an extended period of time and the ability to sustain the loss of such investor's entire investment. No assurance can be given that DLG's investment objective will be achieved and investment results may vary substantially on a monthly, quarterly or annual basis. An investor's investment in the securities should only comprise a portion of the investor's portfolio and should serve as part of an overall investment strategy.

The distribution of this Supplement and the related Memorandum and the offer and sale of the securities in certain jurisdictions may be restricted by law. No action has been or will be taken to permit a public offering in any jurisdiction where action would be required for that purpose. The securities may not be offered or sold, directly or indirectly, and this Supplement and the related Memorandum may not be distributed, in any jurisdiction, except in accordance with the legal requirements applicable in such jurisdiction.

No person has been authorized to give any information or make any representations other than as contained in this Supplement and the related Memorandum and any representation or information not contained therein must not be relied upon as having been authorized by DLG or any of its directors, officers, employees, partners or affiliates. The delivery of this Supplement does not imply that the information herein is correct as of any time subsequent to the date on the cover hereof.

Each prospective investor is invited to meet with DLG's representatives concerning the terms and conditions of the offering of the securities and to obtain any additional information, to the extent the representatives possess such information or can acquire it without unreasonable effort or expense, necessary to verify the information contained herein. Prospective investors interested in obtaining additional information may contact DLG at (818) 905-3337.

NOTICE TO NEW HAMPSHIRE RESIDENTS ONLY

NEITHER THE FACT THAT A REGISTRATION STATEMENT OR AN APPLICATION FOR A LICENSE HAS BEEN FILED UNDER CHAPTER 421-B OF THE NEW HAMPSHIRE REVISED STATUTES WITH THE STATE OF NEW HAMPSHIRE NOR THE FACT THAT A SECURITY IS EFFECTIVELY REGISTERED OR A PERSON IS LICENSED IN THE STATE OF NEW HAMPSHIRE CONSTITUTES A FINDING BY THE SECRETARY OF STATE OF NEW HAMPSHIRE THAT ANY DOCUMENT FILED UNDER RSA 421-B IS TRUE, COMPLETE AND NOT MISLEADING. NEITHER ANY SUCH FACT NOR THE FACT THAT AN EXEMPTION OR EXCEPTION IS AVAILABLE FOR A SECURITY OR A TRANSACTION MEANS THAT THE SECRETARY OF STATE HAS PASSED IN ANY WAY UPON THE MERITS OR QUALIFICATIONS OF, OR RECOMMENDED OR GIVEN APPROVAL TO, ANY PERSON, SECURITY OR TRANSACTION. IT IS UNLAWFUL TO MAKE, OR CAUSE TO BE MADE, TO ANY PROSPECTIVE PURCHASER, CUSTOMER OR CLIENT ANY REPRESENTATION INCONSISTENT WITH THE PROVISIONS OF THIS PARAGRAPH.

RECENT DEVELOPMENTS

This Supplement is intended to update certain specific information described in the Memorandum to reflect events and changes with respect to such information since the date of the Memorandum. This Supplement does not update any information except as specifically described herein. To the extent, and only to the extent, that the information contained herein conflicts with information contained in the Memorandum, the information contained herein will supersede such prior information. Capitalized terms not otherwise defined herein shall have the meaning ascribed to such terms in the Memorandum.

Management

Bruce Friedman founded DLG and has served as our Chief Executive Officer and a member of our board of directors since May 2004. Prior to founding DLG, Mr. Friedman transitioned into real estate investment, creating investment pools and mortgages. Mr. Friedman has a Bachelor of Arts degree in Political Science from U.C.L.A. In or around 1981, Mr. Friedman was convicted by the State of California for grand theft of personal property and was incarcerated for approximately two years. In or around April 1993, due to some business transactions involving a family member, Mr. Friedman was forced to file for personal bankruptcy protection under Chapter 7 of the United States Bankruptcy Code. Mr. Friedman obtained a discharge by order entered in August 1993. In 2000, the U.S. Attorney's Office for the Southern District of New York filed against Mr. Friedman a criminal complaint made by a U.S. Postal Inspector alleging a violation of 18 U.S.C. § 1343 (Wire Fraud) in connection with a payment Mr. Friedman received for providing finance-related services. The complaint was dismissed without any trial or plea.

State Inquiries

On May 6, 2008, we received a written inquiry from the Michigan Office of Financial and Insurance Regulation seeking information from us pertaining to the offer and sale of our investment products within the State of Michigan. We provided our responses to the Michigan Office of Financial and Insurance Regulation's inquiry on June 3 and June 6, 2008. On November 21, 2008, the Michigan Office of Financial and Insurance Regulation issued an order finding that DLG had offered and sold unregistered securities in the State of Michigan in violation of Section 301 of the Michigan Uniform Securities Act and ordering DLG to cease and desist from violating Section 301 of the Michigan Uniform Securities Act. In addition, the order required DLG to offer rescission to all Michigan citizens owning the investment contracts, to pay a \$10,000 civil fine and to refrain from any other securities offerings in the State of Michigan absent compliance with the registration requirements of the Michigan Uniform Securities Act.

On June 12, 2008, we received a written inquiry from the Arkansas Securities Department, or ASD, seeking information from us concerning the offer and sale of our investment products within the State of Arkansas. We replied to this inquiry on June 16, 2008.

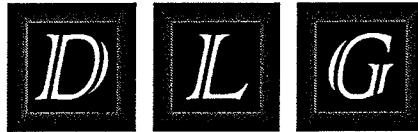
In addition, we received a written inquiry dated July 2, 2008 from the Wisconsin Department of Financial Institutions, Division of Securities, or WSD seeking information from us regarding the offer and sale of our investment products within the State of Wisconsin. We provided our response to the inquiry on July 28, 2008. By letter dated August 20, 2008, we made a rescission offer for the investment contracts that were sold to residents of the State of Wisconsin. On that same date, DLG executed an Assurance of Discontinuance, agreeing not to sell unregistered and nonexempt securities within the State of Wisconsin and to refrain from any further conduct that would violate the Wisconsin Uniform Securities Law. On October 15, 2008, the WSD notified us that they had concluded the matter and closed their file.

We intend to cooperate fully with any additional inquiries from the respective regulators.

Independent Auditor

In mid-2008, we engaged Deloitte & Touche LLP as our independent auditor to audit our financial statements for fiscal year 2008. Deloitte & Touche LLP has recently informed us that they will not conduct an audit

of DLG. We cannot provide any assurance that we will be able to obtain audited financial statements for 2007, 2008 or any future period.



Diversified Lending Group, Inc.

Private Placement of Investment Contracts

***SUPPLEMENT NO. 1 TO THE
CONFIDENTIAL PRIVATE PLACEMENT MEMORANDUM***

December 15, 2008

DECLARATION OF DAVID W. CALLAGHAN

I, David W. Callaghan, declare as follows:

1. I am a principal with LECG, LLC, financial advisor and forensic accountant employed by the duly appointed Permanent Receiver (the "Receiver") for Diversified Lending Group, Inc. ("DLG"), Applied Equities, Inc. ("AEI"), and related affiliates (collectively "Diversified"), pursuant to the Order Granting Motion of Receiver for Instructions Re: (1) Notice Procedures, (2) Procedures for the Use, Sale or Other Disposition of Assets; (3) Employment of Legal Counsel, Accountants, Appraisers, Auctioneers and Brokers; and (4) Payment of Priority Wage Claims, signed and entered on May 4, 2009, in Securities and Exchange Commission v. Diversified Lending Group, Inc., et al., Case No. 2:09-cv-1533-R-JTL (the "SEC Action"), pending in the United States District Court, Western District of California. I have been assigned by LECG to this engagement.

2. Except for those facts alleged on information and belief, I have personal knowledge of the facts in this declaration and, if called as a witness, I could competently testify to these facts.

3. In order to identify Diversified's sources and uses of cash, we have undertaken a massive forensic accounting project. We have compiled and analyzed bank records and other documentation related to more than one hundred separate bank accounts in an attempt to reconstruct books and records for Diversified. Our work creating a consolidated transaction database to identify and categorize each of Diversified's cash receipts and disbursements is ongoing. To date, we have identified and analyzed more than 30,000 cash transactions. We continue receiving, identifying, and considering relevant information. Our findings to date are preliminary and subject to change based on further analysis and additional information that is identified or becomes available.

1 4. This extensive analysis and creation of a complete database is necessary
2 because Diversified did not maintain typical, complete, or accurate financial records.
3 Diversified did not maintain a general ledger or utilize an effective accounting
4 system. Diversified did not prepare financial statements, such as an income
5 statement, balance sheet, or statement of cash flow on a monthly, quarterly, or annual
6 basis. Management and employees stated that basic financial statements were not
7 prepared or maintained for Diversified's individual operating units or on a
8 consolidated basis for the related entities. We have not located or identified
9 company prepared financial statements or supporting documents that appear to be
10 accurate, consistent, or reliable. It became immediately clear during our
11 investigation at the company's offices that even basic documentation supporting
12 Diversified's interests in assets was either poor or did not exist.

13 5. Due to the state of Diversified's records and accounting information, it
14 was not possible to easily obtain accurate information. Simple questions, such as;
15 "How much money had investors deposited with Diversified?" or "What are
16 Diversified's assets?" could not be answered with confidence.

17 6. In order to obtain independently prepared, accurate, and reliable
18 transaction information, we have used Diversified's bank account records and
19 transaction documentation as the foundation and basis for our analysis. We have
20 worked with numerous financial institutions and the Securities and Exchange
21 Commission staff to gather necessary documentation. During this process, we
22 identified approximately one hundred separate bank accounts belonging to
23 Diversified and related parties that were not disclosed during our meetings and
24 discussions with company management and employees.

1 7. To date, the results of our ongoing analysis of Diversified's sources and
2 used of cash are summarized in the following table:

3
4 Receivership of Diversified Lending Group, Inc.
5 Summary of Cash Receipts and Disbursements
6 2005 through 2009

Cash Receipts	(\$ millions)
Investor deposits	\$222.6
Income	4.8
Recovery of principal invested by Diversified	11.6
Additional documentation / analysis	<u>16.5</u>
Total	\$255.5
Cash Disbursements	
Investments - equity and loans	\$116.2
To or for benefit of investors	52.0
Business expenses	29.7
To or for benefit of insiders	21.5
Additional documentation / analysis	<u>36.0</u>
Total	\$255.4

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14 8. We were also responsible for a variety of business termination issues.
15 We communicated with vendors to terminate services and close accounts. We spoke
16 with investors that came to Diversified's offices. We responded to the inquiries of
17 former employees. We traveled to other locations to collect records and evaluate
18 assets. We participated in moving Diversified's offices to an alternate location. We
19 secured and cataloged Diversified's electronic data and paper records and files.

20 9. In order to preserve potentially important electronic data, such as
21 electronic mail communications and other data files, we completed a number of
22 tasks. We secured the company computer hardware. This included desktop
23 machines, laptop computers, files servers, and additional hardware located at offsite
24 locations. As appropriate, we prepared forensic images of these machines. We
25 compiled data extracted from company machines and provided by the Securities and
26 Exchange Commission staff and other sources to facilitate broad analysis of
27 Diversified' activities. We also collected, organized, and indexed a large volume of
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1 paper records and files that were maintained at the Diversified's offices and offsite
2 storage.

3 10. We have addressed a variety of Federal and State income and payroll
4 tax issues. We prepared extensions and amendments for income tax returns. We
5 have been working with the IRS to identify and complete unfiled returns and respond
6 to audits of Diversified's previously filed returns. We interviewed Diversified's
7 prior tax preparer and analyzed the company's prior tax work and filings. We
8 prepared required payroll tax returns and have been working to address and correct
9 significant payroll tax errors related to periods pre-dating the appointment of Mr. Gill
10 as Receiver.

11 11. At the inception of the Receivership, the Diversified employee
12 responsible for payroll and payroll taxes advised me that accurate payroll tax returns
13 had been filed for prior periods. She also stated that all payroll taxes had been paid
14 to the appropriate taxing authorities on a timely basis. In fact, Diversified had not
15 made a Federal payroll tax deposit related to 2008. This payroll tax payment was
16 overdue at the inception of the Receivership. It was paid by the Receiver after the
17 amount due was determined.

18 12. Additionally, numerous assessments have been received from Federal
19 and State authorities related to unpaid payroll taxes for periods predating the
20 Receivership. These assessments generally relate to previously filed Federal and
21 State employment tax returns that were inaccurate, incomplete, or incorrect. To date,
22 assessments for additional payroll taxes of more than \$100,000 related to the years
23 2006 through 2008 have been received. The assessments appear to result from errors
24 such as incorrectly classifying employees as contractors, failing to report income,
25 and failing to pay employer taxes on employee compensation. The assessments have
26 included significant penalties and accrued interest. I expect that Diversified may
27 receive additional payroll tax assessments in the future.

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PROOF OF SERVICE

I, Cindy Cripe, declare:

I am employed by the law firm of DANNING, GILL, DIAMOND & KOLLITZ, LLP, in the County of Los Angeles, State of California. I am employed in the office of a member of the bar of this court at whose direction the service was made. I am over the age of 18 years and am not a party to the within action. My business address is 2029 Century Park East, Third Floor, Los Angeles, California 90067-2904.

On August 14, 2009, I served the following document(s): **RECEIVER'S SECOND REPORT; DECLARATIONS OF DAVID A. GILL AND DAVID W. CALLAGHAN** on the interested parties addressed as follows:

[SEE ATTACHED SERVICE LIST.]

(By Mail) I placed the document for collection and deposit in the mail. I am familiar with this firm's practice for the collection and processing of correspondence for mailing. Under that practice, the document would be placed in a sealed envelope and deposited with the U.S. Postal Service on that same day with postage thereon fully prepaid at 2029 Century Park East, Third Floor, Los Angeles, California 90067-2904, in the ordinary course of business. The documents served were placed in sealed envelopes and placed for collection and mailing following ordinary business practices.

I declare under penalty of perjury under the laws of the State of California and of the United States of America that the foregoing is true and correct.

Executed on August 14, 2009, at Los Angeles, California.

Cindy Cripe

(Type or print name)

Cindy Cripe

(Signature)

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SERVICE LIST

Attorneys for U.S. Securities Exchange Commission

Melissa Grant, Esq.

John M McCoy, III, Esq.

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