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SUPERIOR COURT OF ARIZONA

COUNTY OF MARICOPA

Peter S. Davis, as Receiver of DenSco Investment Corporation, an Arizona corporation, Plaintiff, v. Clark Hill PLC, a Michigan limited liability company; David G. Beauchamp and Jane Doe Beauchamp, husband and wife, Defendants.	No. CV2017-013832 **DEFENDANTS' SECOND SUPPLEMENTAL RULE 26.1 DISCLOSURE STATEMENT**

Defendants Clark Hill PLC, David G. Beauchamp and Jane Doe Beauchamp (collectively, "Defendants") **supplement their** initial disclosure statement according to Arizona Rule of Civil Procedure 26.1. Defendants reserve the right to amend or supplement this disclosure statement as discovery progresses. **Supplements are in bold.**

This case is in its infancy and thus the content of this disclosure statement is preliminary and subject to supplementation, amendment, explanation, change and amplification. Because the parties have just commenced discovery, there may be information, documents, and materials related to the various allegations and defenses set forth in the pleadings of which Defendants are presently unaware. Defendants note that they do

not currently have access to all potentially relevant documents of the Plaintiff, or third parties, and that this disclosure statement is based upon information currently available to Defendants. Nothing in this disclosure statement is intended to be an admission of fact, an affirmation of the existence of any document, or an agreement with or an acceptance of any legal theory or allegation. The information set forth below is provided without waiving (1) the right to object to the use of such information for any purpose in this or any other action due to applicable privilege (including the work-product and attorney-client privileges), materiality, or any other appropriate grounds; (2) the right to object to any request involving or relating to the subject matter of the information in this disclosure statement; or (3) the right to revise, correct, supplement or clarify any of the information provided below. If any part of this statement is ever read to the jury, fairness would require that the jury be read this introductory statement and any supplementation, amendments, explanation, changes or amplifications which may occur or be filed subsequent to this disclosure statement.

Defendants also incorporate by reference into this disclosure statement all interrogatory answers, responses to requests for production, responses to requests for admission, other discovery and disclosure statements and supplements thereto in this action, and all transcripts of any deposition taken in this action and any exhibits thereto.

I. FACTUAL BASIS OF CLAIMS AND DEFENSES.

A. Retention/Scope of Work

For more than 35 years, since graduating with honors from the University of Michigan Law School in 1981, David Beauchamp has represented his clients in the areas of corporate law, securities, venture capital, and private equity with distinction and integrity.

One of those clients was DenSco Investment Corporation ("DenSco"), a company solely owned and managed by Denny Chittick. DenSco raised money from investors by issuing general obligation notes to those investors at interest rates that varied depending on the note's maturity date. DenSco then invested those funds primarily by making high interest

short-term loans to borrowers buying residential properties out of foreclosure, which loans were intended to be secured by deeds of trusts on those properties. Mr. Beauchamp started providing securities advice to DenSco in the early 2000s, while he was a partner at the law firm Gammage & Burnham. DenSco followed Mr. Beauchamp as a client when he left Gammage to join the law firm Bryan Cave in March 2008, and again when Mr. Beauchamp left Bryan Cave to join Clark Hill in September 2013.

Although the various firms' engagement letters with DenSco only specifically identified DenSco as the client, DenSco could not operate or engage with legal counsel except through its president and sole owner, Mr. Chittick. DenSco had no other employees; Mr. Chittick was responsible for all aspects of DenSco's business, and Mr. Chittick understood that Mr. Beauchamp, as an incident to Mr. Beauchamp's representation of DenSco, was also representing Mr. Chittick in his capacity as president of DenSco. The investors understood that as well. The private offering memoranda DenSco provided state that "legal counsel to the Company will represent the interests solely of the Company and its President, and will not represent the interests of any investor."

Shortly after Mr. Chittick's death, and in the midst of a chaotic time dealing with the fallout of his passing, Mr. Beauchamp stated in an August 10, 2016 letter to an Arizona Corporation Commission subpoena to Mr. Chittick that he had "not previously represented Denny Chittick" and that the ACC would need to request the personal information it sought, including Mr. Chittick's personal tax returns, from counsel for Mr. Chittick's estate. To the extent that Mr. Beauchamp's statement was not clear or that any clarification was necessary, Mr. Beauchamp averred in an August 17, 2016 declaration under oath that he represented DenSco and "Mr. Chittick as the President of DenSco." Mr. Beauchamp did not represent Mr. Chittick outside of his role as a corporate officer at DenSco.

Until mid- 2013, Mr. Beauchamp's work as DenSco's securities counsel included, among other things, drafting DenSco's Private Offering Memoranda and related investor

documents; advising DenSco regarding Blue Sky laws and state and federal securities reporting and filing requirements; advising DenSco as to the rules and regulations promulgated by state financial and lending authorities; and advising DenSco regarding the applicability of mortgage broker regulations. At times, it would also involve answering DenSco's questions regarding its Reg D filings and obligations. Although Mr. Beauchamp helped DenSco file its first set of Reg D documents in 2003, Mr. Chittick told Mr. Beauchamp thereafter that he did not want to pay a lawyer to review and file the Reg D documents, and that Mr. Chittick would take on that responsibility himself. That was not a surprising request, as Mr. Chittick repeatedly instructed Mr. Beauchamp to keep legal fees to a minimum. Consequently, although Mr. Beauchamp's paralegal initially helped Mr. Chittick understand the filing process and obtain access to the EDGAR filing site, in accordance with his client's wishes Mr. Beauchamp did not review DenSco's Reg D filings.

The scope of Mr. Beauchamp's representation of DenSco and its president was narrow. Further, the relationship was friendly, but professional. Mr. Beauchamp did not go to dinner or vacation with Mr. Chittick or his family. They did not play golf or otherwise socialize together.

Over the years, Mr. Chittick showed himself to be a trustworthy and savvy businessman, and a good client. He was devoted to his business and investors, many of whom were friends and family. Despite often complaining about the cost of legal services, Mr. Chittick appeared to follow Mr. Beauchamp's advice and provided information when asked for it. Further, Mr. Beauchamp understood that DenSco utilized an outside accountant, David Preston, to review DenSco's books and records and file its tax returns. At no point did Mr. Beauchamp serve as DenSco's general corporate counsel, nor was Mr. Beauchamp engaged to review or approve DenSco financial statements or tax returns or to investigate borrowers.

B. The Private Offering Memoranda

Mr. Beauchamp advised DenSco regarding its Private Offering Memoranda ("POMs"), which DenSco generally updated every two years. He helped draft the 2003, 2005, 2007, 2009, and 2011 POMs. The POMs, however, had similar provisions and generally described DenSco's historical performance based on information provided by Mr. Chittick; set forth Mr. Chittick's authority to determine DenSco's "major business decisions and policies", and to make, amend, or deviate from those policies in Mr. Chittick's sole discretion; and set forth DenSco's aspirational lending standards (including its intent to "maintain a loan-to-value ratio below 70%" for both individual trust deeds DenSco purchased and the aggregate loan portfolio, as well as its intent to "achieve a diverse borrower base" with no borrower comprising more than 10-15% of the portfolio).

In early summer 2013, Mr. Beauchamp advised DenSco that it needed to update its 2011 POM given the passage of time and changes in the scope of DenSco's fund raising. In particular, based on Mr. Chittick's representations to Mr. Beauchamp, DenSco either had or would soon eclipse the $50 million maximum offering set forth in the 2011 POM. Consequently, Mr. Beauchamp began drafting revisions to the 2011 POM, which included updates to the maximum offering and updates on DenSco's performance to date, among other revisions. Mr. Beauchamp, however, was never able to finalize the 2013 POM. Although Mr. Beauchamp asked for updated investment, loan and financial information regarding DenSco, Mr. Chittick stalled on providing the information, preferring to wait until after he scaled down the amount outstanding to investors. Mr. Beauchamp repeatedly advised DenSco that an update was necessary irrespective of DenSco's plans regarding the outstanding amount of its offerings, but Mr. Chittick continued to delay.

C. The FREO Lawsuit

On May 24, 2013, Easy Investments, an entity owned by Yomtov "Scott" Menaged ("Menaged"), DenSco, and Ocwen Loan Servicing, were sued by FREO Arizona, LLC

("FREO") regarding liens recorded by Easy Investments in favor of DenSco and Active Funding Corporation, on a parcel of property. In a June 14, 2013 email from Mr. Chittick to Mr. Beauchamp, Mr. Chittick explained that Easy Investments had purchased a property at a trustee's sale using a DenSco loan, which had apparently been previously purchased by FREO, leading to a dispute. A review of the partial Complaint provided to Mr. Beauchamp confirms Mr. Chittick's description. According to its allegations, the loan servicer, Ocwen, failed to cancel a trustee's sale and release the deed of trust after FREO had paid off the debt and acquired the property, thereby allowing Easy Investments to purchase the property again with DenSco's funds. Contrary to the allegations in the Receiver's Complaint, the FREO lawsuit did not concern lien priority or double lien issues. Moreover, a review of the docket reveals that Easy Investments prevailed in the FREO lawsuit when the Court granted summary judgment in favor of Easy Investments and against both FREO and Ocwen (for breach of its duties) on December 6, 2013.

Further, although Mr. Chittick forwarded a portion of the Complaint to Mr. Beauchamp, Mr. Chittick did not ask Mr. Beauchamp to represent DenSco in the litigation; nor did he ask Mr. Beauchamp to investigate the factual allegations in the Complaint. To the contrary, he expressly stated that he merely wanted Mr. Beauchamp to "be aware" of the lawsuit. Consequently, although Mr. Beauchamp ran the matter through Bryan Cave's conflict system pursuant to standard firm procedure, Mr. Beauchamp did not represent DenSco in the litigation and did not conduct any further investigation into its merits given his client's instruction not to get involved.

Mr. Beauchamp did, however, explain to Mr. Chittick that this lawsuit would need to be disclosed in DenSco's 2013 POM. In addition, Mr. Beauchamp advised Mr. Chittick, as he had done previously, that Mr. Chittick needed to fund DenSco's loans directly to the trustee or escrow company conducting the sale, rather than provide loan funds directly to the borrower, to ensure that DenSco's deed of trust was protected. Mr. Chittick, however,

explained to Mr. Beauchamp that this was an isolated incident with a borrower, Menaged, whom Mr. Chittick described in his email as someone he had "done a ton of business with...hundreds of loans for several years...."

D. Mr. Beauchamp leaves Bryan Cave, hears nothing from Mr. Chittick for months.

Mr. Beauchamp left Bryan Cave at the end of August 2013. Prior to his departure, Mr. Beauchamp had repeatedly made clear to DenSco and Mr. Chittick that they needed to update DenSco's POM. On August 30, 2013, Mr. Beauchamp and Bryan Cave sent Mr. Beauchamp's clients, including DenSco, a joint separation letter informing them that Mr. Beauchamp was joining Clark Hill effective as of September 1, 2013. The letter invited those clients to either request the transition of their files to Mr. Beauchamp or affirmatively request that the files remain at Bryan Cave. Mr. Chittick initially agreed to transfer a portion of DenSco's files to Clark Hill, but aside from DenSco's authorization letter, Mr. Beauchamp never heard from Mr. Chittick regarding the unfinished 2013 POM, or any other matter, until December 2013.

E. DenSco contacts Mr. Beauchamp in late 2013, slowly reveals scope of Menaged issues over several months

In December 2013, Mr. Chittick contacted Mr. Beauchamp for the first time in months. He told Mr. Beauchamp over the phone that he had run into an issue with some of his loans to Menaged, and specifically, that properties securing a few DenSco loans were each subject to a second deed of trust competing for priority with DenSco's deed of trust. Mr. Beauchamp reminded Mr. Chittick that he still needed to update DenSco's private offering memorandum. After briefly discussing the allegedly limited double lien issue, Mr. Chittick emphasized to Mr. Beauchamp that Mr. Chittick wanted to avoid litigation with other lenders. Mr. Chittick, however, did not request any advice or help. Accordingly, Mr. Beauchamp suggested that Mr. Chittick develop and document a plan to resolve the double liens, and nothing more came of the conversation.

Mr. Chittick vastly understated the scope of the problem. On January 6, 2014, Attorney Bob Miller at Bryan Cave sent Mr. Chittick a letter on behalf of various lenders (the "Miller Lenders"). The letter asserted that the Miller Lenders had advanced purchase money loans directly to trustees to buy more than 50 properties out of foreclosure, and had recorded deeds of trust to evidence their first position security interest. DenSco, however, had likewise recorded mortgages evidencing its purported purchase money loans for the same properties. The Miller Lenders asserted that DenSco's claimed interest was a "practical and legal impossibility since...only the Lenders provided the applicable trustee with certified funds supporting the Borrowers purchase money acquisition for each of the Properties," demanded that DenSco subordinate its alleged interests to their interests, and threatened to bring claims for fraud, negligent misrepresentation, and wrongful recordation.

It seems unlikely that the issue with the Miller Lenders was a surprise to Mr. Chittick. Although Mr. Chittick's business journals contain hearsay and present questions regarding admissibility, they suggest that Menaged had told Mr. Chittick about the double lien issue in November 2013, and had explained that the issue could affect every property Menaged had purchased using DenSco funds going back as far as 2011. Further, as set forth below, Mr. Chittick and Menaged had apparently already reached an agreement on how to deal with the double lien issue in November 2013 as well. Mr. Chittick, however, failed to provide that information to Mr. Beauchamp in December. Nor did he immediately provide Mr. Beauchamp with the full scope of the problem, or reveal the procedure he had agreed to with Menaged to resolve that problem, in December or early January.

Instead, Mr. Chittick sent the Miller letter to Mr. Beauchamp on January 6, 2014 with nothing more than a sparse request for Mr. Beauchamp to "read the first two pages." The next day, Mr. Chittick provided Mr. Beauchamp a more expansive, if incomplete, explanation. In his email, Mr. Chittick stated that he had lent Menaged a total of $50 million since 2007 and that he'd "never had a problem with payment or issue that hasn't been

resolved." Mr. Chittick asserted, however, that Menaged's wife had become critically ill in the past year, and that Menaged had turned the day-to-day operations of his companies over to his cousin. According to Mr. Chittick, the cousin would receive loan funds directly from DenSco, then request loans for the same property from another lender, including the Miller Lenders. The other lenders, who had funded their loans directly to the trustee, would record their deed of trust, as would DenSco, leaving DenSco in second position. The cousin, unfortunately, then purportedly absconded with the funds DenSco lent directly to Menaged. This "double lien" issue consequently jeopardized DenSco's secured position and its loan-to-value ratios. Mr. Chittick feared that a lawsuit with the Miller Lenders would jeopardize DenSco's entire enterprise.

According to Mr. Chittick's email, Menaged purportedly found out about his cousin's scam in November and revealed the fraud to Mr. Chittick at the time. Yet rather than consult legal counsel, Mr. Chittick worked out a plan to fix the double lien issue with Menaged. The initial plan included DenSco paying off the other lenders. That required additional capital, which Menaged and Mr. Chittick agreed would come from DenSco lending Menaged an additional $1 million and Menaged investing additional capital, including $4-$5 million from the liquidation of other assets, as set forth in a term sheet DenSco and Menaged signed after having already put their plan into effect. As the scope of the problem appeared to grow, Mr. Chittick and Menaged agreed to terms of an expanded plan, which included further investment from both DenSco and Menaged, who would also continue to flip and rent homes to raise the necessary profits needed to pay off the other lenders.

Unbeknownst to Mr. Beauchamp, and according to Mr. Chittick's January 7, 2014 email, DenSco and Menaged had already been "proceeding with this plan since November [2013]." That is corroborated by the Receiver, who asserts that Mr. Chittick lent $1 million to Menaged to further their private workout plan in December 2013. In other words, by the time Mr. Chittick approached Mr. Beauchamp with a partial disclosure of the issues in late

2013 and early 2014, Mr. Chittick had already agreed to a business plan with Menaged to work out the double lien problems, and had already advanced Menaged significant sums pursuant to that agreement. As Mr. Beauchamp explained in a February 20, 2014 email to his colleagues, Mr. Chittick "without any additional documentation or any legal advice...has been reworking his loans and deferring interest payments to assist Borrower...When we became aware of this issue, we advised our client that he needs to have a Forbearance Agreement in place to evidence the forbearance and the additional protections he needs."

1. Mr. Beauchamp tells DenSco it cannot accept new funds or roll over prior funds.

After receiving Mr. Chittick's January 7, 2014 email, Mr. Beauchamp was alarmed that DenSco may be taking on new investors or rolling over prior investments without disclosing the double lien issue or the workout to which Mr. Chittick and Menaged had agreed. Mr. Beauchamp's advice to Mr. Chittick regarding disclosures Mr. Chittick had to make to investors was immediate, clear, practical, consistent with his practice and experience, and consistent with the standard of care: (a) DenSco was not permitted to take new money without full disclosure to the investor lending the money; (b) DenSco was not permitted to roll over existing investments without full disclosure to the investor rolling over the money; and (c) DenSco needed to update its POM and make full disclosure to all its investors. Mr. Beauchamp provided this advice to DenSco starting with his January 9, 2014 meeting with Mr. Chittick, and repeated it routinely over the next few months.

Mr. Beauchamp was also concerned about the source and use of the funds needed to effectuate the Menaged-Chittick workout. Yet, as Mr. Chittick explained, the funds for the $1 million loan (which Mr. Chittick funded prior to engaging Clark Hill) and an additional $5 million loan Mr. Chittick and Menaged eventually agreed to as part of the workout, would come from (a) Mr. Chittick's investment of additional funds out of his retirement account, (b) Mr. Chittick's personal $1.5 million line of credit, and (c) DenSco's working capital

raised as loans to other borrowers paid off. Again, and at all times Mr. Beauchamp, advised Mr. Chittick that he could not obtain new investor funds or roll over prior investments without full disclosure. Mr. Beauchamp also repeatedly insisted that Mr. Chittick revise his out-of-date POM to provide disclosure to all his investors. Mr. Chittick, however, insisted that DenSco first document the forbearance agreement so that Mr. Chittick would have a plan to show his investors.

Further, Mr. Chittick assured Mr. Beauchamp repeatedly that he was making the requisite disclosures to investors on an as needed basis, and that he had informed a select group of investors as to the double lien issue and proposed workout. That would be in keeping with Mr. Chittick's prior approach to business. As far as Mr. Beauchamp knew, and as Mr. Chittick had previously told him, Mr. Chittick indeed had a select group of investors to whom he turned for advice and approval when confronted with important business decisions, such as, for example, diversifying his investments into different types of properties. Mr. Chittick told Mr. Beauchamp that he was seeking such advice from what Mr. Chittick described as an "advisory council." And again, while the letters Mr. Chittick appears to have authored prior to his passing contain hearsay and present questions regarding admissibility, they include various statements suggesting that Mr. Chittick may have previously told (and received approval from) a select group of investors that he was investing specifically with Menaged, that he was increasing his loan concentration with Menaged above the 10-15% concentration threshold suggested in his POMs, and that his lending process involved funding loans directly to borrowers, rather than a trustee or escrow account.

There was no reason for Mr. Beauchamp to question whether Mr. Chittick was in fact providing disclosures to limited investors. Moreover, over the more than decade long strong professional relationship Mr. Beauchamp had developed with Mr. Chittick, Mr. Chittick had proven himself to be a trustworthy client with a strong history of sharing information and making prudent decisions.

2. Mr. Beauchamp advises DenSco to enter into a forbearance agreement.

Beginning in early January, and over the course of several meetings and telephone conversations with Mr. Chittick, Mr. Beauchamp convinced Mr. Chittick that if he was going to keep doing business with Menaged (and Mr. Chittick never wavered from his insistence on working his way out of the double lien issue with Menaged), DenSco should at least document the issues and workout plan in a forbearance agreement. Entering into a forbearance agreement was sound, practical advice and consistent with the standard of care, particularly where Mr. Chittick and Menaged had already implemented their own workout plan. As Mr. Beauchamp repeatedly explained to Mr. Chittick, the forbearance agreement would, among other things, (a) clarify and set forth the facts that led to the double lien issue, (b) clarify and set forth the scope of the issue with the borrower, (c) acknowledge Mr. Menaged's defaults under his loan documents with DenSco, as well as the amount and validity of any debt owed to DenSco, (d) obtain additional written commitments from Menaged and his entities to fund the workout Mr. Chittick and Menaged had already agreed to; and (e) obtain additional security and other protections from Menaged and his entities to protect DenSco and its investors. Mr. Beauchamp was crystal clear with Mr. Chittick all of this would need to be disclosed to DenSco's investors. Other protections Mr. Beauchamp advocated for, including additional admissions of fault and fraud by Menaged to protect DenSco in the event of a bankruptcy filing by Menaged or his entities, were eventually stricken from the agreement at Menaged and Mr. Chittick's insistence, and over Mr. Beauchamp's objections.

Mr. Beauchamp had previously drafted and negotiated countless forbearance agreements. He reasonably anticipated that documenting DenSco's forbearance would take 2-3 weeks. Negotiating the forbearance agreement, however, turned out to be more difficult than Mr. Beauchamp could have reasonably imagined. For one, Menaged and his counsel repeatedly insisted on edits and revisions that served only to undermine DenSco's fiduciary

duty to its investors. Mr. Beauchamp repeatedly had to undo changes proffered by Menaged or Jeff Goulder, Menaged's attorney, and often by Mr. Chittick at Menaged's direction, in order to protect DenSco's investors. For example, Menaged (and Mr. Goulder) attempted to restrict the type of information that could be disclosed to investors, attempted to obtain releases for Menaged related to his defaults and conduct, and refused to provide additional security or information regarding that additional security. Mr. Beauchamp repeatedly pushed back on these efforts and advised DenSco and Mr. Chittick, both in writing and verbally, that they had fiduciary duties to DenSco's investors, which included disclosure obligations. *See e.g.*, February 4, 2014 email from Mr. Beauchamp to Mr. Chittick ("you cannot obligate DenSco to further help Scott, because that would breach your fiduciary duty to your investors"); February 14, 2014 email from Mr. Beauchamp to Mr. Chittick ("[Goulder] clearly thinks he can force you to agree to accept a watered down agreement and give up substantial rights that you should not have to give up. Unfortunately, it is not your money. It is your investors' money. So you have a fiduciary duty"); March 13, 2014 email from Mr. Beauchamp to Mr. Chittick ("we cannot give Scott and his attorney any time to cause further delay in getting this Forbearance Agreement finished and the necessary disclosure prepared and circulated").

In addition to Menaged and his counsel's constant revisions, the number of loans affected by the double lien issue also kept growing. The number of loans Mr. Chittick asserted were in issue grew from December 2013 to January 2014, and then grew again from January 2014 to February 2014. This resulted in constant changes to the revised workout documents, as well as to Menaged and Mr. Chittick's agreement regarding the manner in which to fund the workout. Mr. Chittick, however, maintained, despite multiple inquiries from Mr. Beauchamp, that he had run the calculations and projections and was confident his plan with Menaged would work. Mr. Chittick also told Mr. Beauchamp that he had gone over those projections with his "advisory council." As Mr. Chittick described it to Mr.

Beauchamp, it was a cash flow issue, not a payment issue, and that with Menaged's additional investments, the workout would succeed.

Nevertheless, Mr. Beauchamp at one point became concerned enough at Menaged's intransigence and the apparent influence he held over Mr. Chittick, that he reached out to third parties in late January 2014 to inquire about Menaged. Those third parties informed him that Menaged was generally someone to be distrusted and not someone to do business with. Mr. Beauchamp attempted to persuade Mr. Chittick of this during several heated conversations, but Mr. Chittick ignored these admonitions, explaining that while Menaged could be sharp and off-putting, Menaged had always performed on DenSco's loans in the past, and had stood by Mr. Chittick in tough times. Despite Mr. Beauchamp's efforts, Mr. Chittick could not be convinced to cut ties with Menaged.

F. Mr. Beauchamp terminates representation of DenSco and Mr. Chittick.

When Mr. Beauchamp agreed to represent DenSco with respect to Menaged, Mr. Beauchamp made clear that Mr. Chittick had to immediately update DenSco's POM and make full disclosure to its investors regarding the double lien issues, the workout with Menaged, and the potential implications thereof on DenSco's finances and the investors' investments. Mr. Chittick always acknowledged that responsibility and agreed to make the full disclosure once the forbearance agreement was properly documented. As the forbearance neared completion, Mr. Beauchamp and his associate, Daniel Schenk, began drafting the updated POM in April and May 2014. Specifically, the draft 2014 POM would have: provided a description of the forbearance agreement (including all the parties' funding obligations), the reason it was necessary, and its effect on DenSco's books; updated DenSco's goals for intended loan-to-value ratios; updated the descriptions regarding DenSco's loan funding and securitizations procedures; updated the number of loan defaults triggering foreclosures; and amended the descriptions regarding DenSco's borrower base, among other things. Further, Mr. Beauchamp explained that the updated POM would need

to be accompanied with a cover letter or other communication highlighting the major material changes, including the double lien issue and resulting workout agreement, to ensure that investors were fully informed. Mr. Chittick, however, refused to provide the necessary information to complete the POM and refused to approve the description of the workout or the double lien issue, despite his prior acknowledgement that he would need to make full disclosure to all of his investors about DenSco (as he had been doing through POMs and newsletters since 2003).

In May 2014, Mr. Beauchamp handed Mr. Chittick a physical copy of the draft POM and asked him what Mr. Chittick's specific issues were with the disclosure. Mr. Chittick responded that there was nothing wrong with the disclosure, he was simply not ready to make any kind of disclosures to his investors at this stage. Mr. Beauchamp again explained that Mr. Chittick had no choice in the matter and that he had a fiduciary duty to his investors to make these disclosures. Mr. Chittick would not budge. Faced with an intransigent client who was now acting contrary to the advice Mr. Beauchamp was providing, and with concerns that Mr. Chittick may not have been providing any disclosures to anyone since January 2014, Mr. Beauchamp informed Mr. Chittick that Beauchamp and Clark Hill could not and would not represent DenSco any longer. Mr. Beauchamp also told Chittick that he would need to retain new securities counsel, not only to provide the proper disclosure to DenSco's investors, but to protect DenSco's rights under the forbearance agreement. Mr. Chittick suggested that he had already started that process and was speaking with someone else.

Thereafter, Mr. Beauchamp and Clark Hill ceased providing DenSco with securities advice. Mr. Chittick accepted that, but asked that Mr. Beauchamp clean up some small issues with the forbearance agreement before ending the relationship entirely. Other than addressing those small forbearance agreement issues in June and July, Clark Hill stopped working with DenSco or Mr. Chittick in any capacity until 2016, when Mr. Chittick requested that Mr. Beauchamp assist with a very limited issue involving an audit by the

Arizona Department of Financial Institutions - work Mr. Beauchamp had previously performed for DenSco and that Mr. Chittick characteristically believed could be done most cost-effectively by Mr. Beauchamp rather than by a new lawyer with no background on the issue.

G. Menaged continues to perpetrate fraud on DenSco, which only grows in scale.

During the time that he represented it regarding securities matters, Mr. Beauchamp (a) repeatedly advised DenSco that it had to make full disclosure to its investors and then terminated his relationship as securities counsel for DenSco when DenSco refused, (b) explained that DenSco would need to retain new counsel after Mr. Beauchamp withdrew to provide proper disclosures and monitor the forbearance, and (c) repeatedly reminded Mr. Chittick that he needed to fund loans directly to a trustee or escrow company, rather than to the borrower. Mr. Chittick ignored Mr. Beauchamp's advice. It is unclear if DenSco ever engaged or even talked to new counsel. It appears Mr. Chittick never issued an updated POM, a fact which could not have gone unnoticed by DenSco's sophisticated investors, who had gotten used to regular updates from DenSco, not only through updated POMs, but through monthly newsletters and periodic investor meetings. It is quite clear that Mr. Chittick continued to loan funds directly to Menaged in direct contravention of Mr. Beauchamp's repeated advice.

Nevertheless, the brazen scope of Menaged's efforts to defraud DenSco was not foreseeable. After several years of bilking DenSco and others out of millions of dollars, Menaged was eventually arrested. The United States Department of Justice first charged Menaged with defrauding various banks through his purported furniture stores. Menaged used fabricated receipts of purchases made at the furniture store to obtain credit from banks using the names of, and personal identification information of, individuals who had recently died. He would then incur millions of dollars in fraudulent charges on those fake

accounts. Incredibly, Menaged acknowledged in his plea agreement that he had perpetrated the bank fraud in order to get cash to continue defrauding DenSco.

The Department of Justice then also charged Menaged with money laundering with respect to the DenSco fraud. In his plea agreement, Menaged admitted that from January 2014 through June 2016, he embezzled millions of dollars without purchasing properties with the loans obtained from Densco. He explained that Densco would wire money to purchase properties directly to Menaged who, in turn, would send Densco "an image of a bank cashier's check and a copy of a Trustee Certificate of Sale Receipt." No sales, however, actually took place. Menaged would simply redeposit the cashier's check into his account and create bogus receipts for the purchase of the property. Between January 2013 and June 2016, Menaged admitted he obtained 2,172 loans from DenSco totaling approximately $734,484,440.67. Yet, of the 2,712 loans made by DenSco, only 96 involved actual property transactions. Menaged supposedly used the remaining 2,616 loans for personal expenses, gambling trips, and transfers to his family members and associates. Menaged would also utilize new loans from DenSco to pay back outstanding DenSco loans to conceal the embezzlement. Menaged was sentenced to 17 years in jail. As First Assistant U.S. Attorney Elizabeth Strange stated, the "lengthy sentence is a fitting punishment for his egregious crimes."

Menaged shamelessly duped Mr. Chittick. Documents and recordings suggest that Menaged never invested any money into the workout plan. He never obtained any money from Israel despite purportedly making numerous trips to the country for that very purpose, blatantly lied that funds that could have been used to fund the workout were tied up in his divorce proceedings, and ultimately invented a non-existent investment scheme involving "auction.com" which Menaged falsely claimed was retaining most of DenSco's money (to go along with his fabrication of the fraudulent cousin and terminally ill wife). Sadly, Mr. Chittick bought into all of Menaged's lies until his last days.

Discovery is continuing. Defendants may supplement.

II. LEGAL THEORIES OF CLAIMS AND DEFENSES.

A. Plaintiff's claims

Legal Malpractice

Receiver asserts that Defendants, in their representation of DenSco, committed malpractice and breached fiduciary duties owed to DenSco. Legal malpractice requires proof of the existence of a duty, breach of duty, that defendant's breach was the actual and proximate cause of damages, and the "nature and extent" of those damages. *Glaze v. Larsen*, 207 Ariz. 26, 29 ¶ 12 83 P.3d 26, 29 (Ariz. 2004) (citations and quotations omitted).

Receiver cannot prove breach of duty, actual and proximate cause, or resulting damages. To prove breach of duty, Receiver will need to demonstrate that Defendants deviated from the professional standard of care. *Phillips v. Clancy,* 152 Ariz. 415, 418, 733 P.2d 300, 303 (App. 1986). Defendants' advice and conduct in representing DenSco and, in doing so, representing Mr. Chittick as president of DenSco, was consistent with Defendants' practice and experience, and consistent with the standard of care. Thus, Defendants did not breach their duties to DenSco. Receiver will also need to prove that if Defendants had not purportedly breached the standard of care, that DenSco would not have suffered injury. *Id.* Whatever harm befell DenSco was not an actual or foreseeable result of the advice provided by Defendants. Thus, Receiver's malpractice claim fails.

Aiding and Abetting Breach of Fiduciary Duties

Receiver asserts that Defendants aided and abetted Mr. Chittick in breaching his fiduciary duties to DenSco. Claims of aiding and abetting require proof that: (1) the primary tortfeasor must commit a tort that caused injury to the plaintiff; (2) the defendant must know that the primary tortfeasor's conduct constitutes a breach of duty; (3) the defendant must substantially assist or encourage the primary tortfeasor in the achievement of that breach and (4) there must be a causal relationship between the defendant's assistance or encouragement

and the primary tortfeasor's commission of the tort. *Wells Fargo Bank v. Az. Laborers, Teamsters and Cement Masons Local No. 395 Pension Trust Fund*, 201 Ariz. 474, 485 (Ariz. 2002); *Sec. Title Agency, Inc. v. Pope*, 219 Ariz. 480, 491 (App. 2008). Importantly, "[b]ecause aiding and abetting is a theory of secondary liability, the party charged with the tort must have knowledge of the primary violation." *Wells Fargo*, 201 Ariz. at 485.

It is unclear from the Complaint what actions the Receiver asserts constitute a breach of Mr. Chittick's fiduciary duties to DenSco. In any event, as set forth above, Defendants' advice and conduct in representing DenSco were consistent with the applicable standard of care. Defendants did not "substantially assist or encourage" Mr. Chittick in breaching his duties to DenSco, Defendants did not have knowledge of Mr. Chittick's purported "primary violation," nor is there a causal relationship between Defendants' representation of DenSco and Mr. Chittick's purported tortious conduct with respect to DenSco. Further, as set forth above, whatever harm befell DenSco was not an actual or foreseeable result of Defendants' actions or inactions.

B. Affirmative Defenses

Statute of Limitations

Both the legal malpractice claim and the aiding and abetting claim have a two-year statute of limitations. *See* A.R.S. §12-542(1) (An action "[f]or injuries done to the person of another" shall be commenced and prosecuted within two years after the cause of action accrues, and not afterward"). Receiver, who stands in the shoes of DenSco, did not file the Complaint in this action until October 16, 2017, which was well outside the statute of limitations. DenSco, and potentially the Investors, could have discovered at least as of Summer 2014, that DenSco's loans to Menaged (or his entities) and DenSco's lending practices with respect to Menaged, could give rise to potential causes of action against Mr. Chittick or his agents. Consequently, because the statute of limitations ran, at the latest, in the Summer of 2016, the Complaint is barred in its entirety.

In pari delicto and *unclean hands*

Arizona law recognizes the doctrine of in pari delicto. *Brand v. Elledge*, 89 Ariz. 200, 205, 360 P.2d 213, 217 (1961) (quoting *Furman v. Furman*, 34 N.Y.S.2d 699, 704 (N.Y. Sup. Ct. 1941), *aff'd*, 40 N.E.2d 643 (N.Y. 1942)). In pari delicto is an affirmative defense by which a party is barred from recovering damages if his losses are substantially caused by activities the law forbade him to engage in." *Stewart v. Wilmington Trust SP Servs., Inc.*, 112 A.3d 271, 301–02 (Del. Ch.), *aff'd*, 126 A.3d 1115 (Del. 2015) (quotation omitted). The defense may be raised against a receiver. *Id.* ("no cogent reason for sparing the innocent Receiver the effect of in pari delicto while equally innocent stockholders or policyholders would be barred from relief in the derivative context"); *Knauer v. Jonathon Roberts Fin. Grp., Inc.*, 348 F.3d 230, 236 (7th Cir. 2003) (affirming dismissal of the receiver's claims against the broker dealers, concluding that they were barred by the defense of in pari delicto).

Here, to the extent there are claims against the Defendants, DenSco, into whose shoes the Receivers steps, bears fault for damages about which it complains. Thus, the Receiver's claims are barred by doctrine of *in pari delicto* and, to the extent it specifically seeks equitable relief, by the related doctrine of unclean hands.

Laches

A claim is barred by laches when the delay in bringing the claim is "unreasonable under the circumstances" given "the party's knowledge of his or her right" and "any change in circumstances caused by the delay has resulted in prejudice to the other party sufficient to justify denial of relief." *Mathieu v. Mahoney*, 174 Ariz. 456, 459, 851 P.2d 81, 84 (1993). Receiver seeks to recover potentially millions of dollars in alleged damages resulting from loans Mr. Chittick made to Menaged. DenSco would have been aware of the harms that could befall DenSco and its investors as a result of DenSco's loans to, and lending practices with, Menaged, by Summer 2014 at the latest. DenSco's inaction for several years, up through the

death of Mr. Chittick, to seek relief against any potential third party for harms suffered by DenSco was unreasonable in light of DenSco's knowledge. Because the Receiver steps into DenSco's shoes, the claims are barred.

Setoff

Clark Hill filed a proof of claim in the DenSco Receivership for unpaid fees incurred by Clark Hill on behalf of DenSco after Mr. Chittick's death. The Receiver improperly denied the claim on the basis of an alleged conflict of interest. To the extent Defendants are found to owe Plaintiff anything, that debt must be reduced any sums Plaintiff owes Clark Hill.

Additional defenses:

- Third parties, including Mr. Chittick and Menaged, over whom Defendants have no authority or control, are at fault for any damages suffered.
- Densco, in to whose shoes the Receiver steps, is at fault for any damages suffered.
- Densco, in to whose shoes the Receiver steps, assumed the risk of any actions taken or not taken by DenSco or Mr. Chittick. *Hildebrand v. Minyard*, 16 Ariz. App. 583, 585, 494 P.2d 1328, 1330 (1972) ("A plaintiff who by contract or otherwise expressly agrees to accept a risk of harm arising from the defendant's negligent or reckless conduct cannot recover for such harm . . . .") (*quoting* Restatement (Second) of Torts § 496(B) (1965)).
- Receiver cannot demonstrate proximate cause or loss causation because Defendants are not the actual or proximate cause of any damages suffered.
- Any damages suffered were the result of intervening or superseding events or causes over which the Defendants had no control and were not legally responsible.
- Receiver's claims are barred by doctrines of waiver and estoppel.

Discovery is continuing. Defendants may supplement.

III. WITNESSES.

Because no discovery has taken place, Defendants have not yet identified all persons it may call as witnesses at trial, but reserves the right to call any of the following persons to testify as a witness at trial:

1. David Beauchamp
c/o Coppersmith Brockelman, PLC
2800N. Central Avenue, Suite 1900
Phoenix, Arizona 85004

Mr. Beauchamp is expected to testify regarding the allegations in the Complaint and his representation of DenSco and of Mr. Chittick in his capacity as president of DenSco.

2. Peter Davis, Receiver of DenSco Investment Corporation
c/o Osborn Maledon, P.A.
2929 N. Central Avenue, Suite 2100
Phoenix, Arizona 85012

Mr. Davis is expected to testify regarding the allegations in the Complaint; the Receiver's evaluations, analyses, and determinations regarding all aspects of DenSco's finances, including, but not limited to, DenSco's loans, lending practices, record keeping, financial transactions, and solvency; the Receiver's maintenance of any DenSco or Chittick records or property, including, but not limited to, electronic records, websites, and email communications; the Receiver's communications with third parties related to DenSco, including communications with financial institutions, investors, and accountants and other professionals; the Receiver's determinations regarding the Receiver's evaluation and analysis regarding the potential fault, liability, or culpability of any third party with respect to any losses suffered by DenSco, including, but not limited, to Chase Bank, U.S. Bank, Yomtov Menaged, Active Funding Group, LLC, and/or Gregg Seth Reichman.

3. Any witnesses disclosed by other parties.

4. Any witnesses that become known through discovery.

5. Custodian or other foundational witnesses necessary to admit exhibits.

Discovery is continuing. Defendants may supplement.

IV. ADDITIONAL PERSONS WHO MAY HAVE RELEVANT INFORMATION.

1. Yomtov "Scott" Menaged

Scott Menaged is expected to have knowledge regarding all aspects of any personal, financial, or business dealings he may have had with DenSco and Mr. Chittick; all aspects of the fraud(s) he perpetrated on DenSco and Mr. Chittick, either directly, or through one of his entities, including, but not limited to, Easy Investments, LLC, Arizona Home Foreclosures, LLC, Furniture King, LLC, and Scott's Fine Furniture; all aspects of actions or conduct related to his criminal indictment, plea bargain, or sentencing in the United States District Court for the District of Arizona; his communications with DenSco and Mr. Chittick; and his communications with Mr. Beauchamp.

2. PMK Easy Investments, LLC
10510 East Sunnyside Drive
Scottsdale, AZ 85259

See Description for Scott Menaged.

3. PMK Arizona Home Foreclosures, LLC
7320 West Bell Road
Glendale, AZ 85308

See Description for Scott Menaged.

4. PMK Furniture King, LLC
3200 North Central Avenue
Suite 2460
Phoenix, AZ 85012

See Description for Scott Menaged.

5. PMK Scott's Fine Furniture

See Description for Scott Menaged.

6. Veronica Castro aka Veronica Gutierrez Reyes
c/o Thomas W. Warshaw Attorney at Law
33147 North 71st Way
Scottsdale, AZ 85266

Ms. Castro is expected to have knowledge regarding Menaged's personal, financial, or business dealings with DenSco and Mr. Chittick; the fraud(s) Menaged perpetrated on DenSco and Mr. Chittick, either directly, or through one of Menaged's entities; Menaged's communications with DenSco and Mr. Chittick; Menaged's communications with Mr. Beauchamp; the actions or conduct related to Menaged's criminal indictment, plea bargain, or sentencing in the United States District Court for the District of Arizona; and Ms. Castro's communications with DenSco and Mr. Chittick.

7. Luigi Amoroso

Mr. Amoroso is expected to have knowledge regarding Menaged's personal, financial, or business dealings with DenSco and Mr. Chittick; the fraud(s) Menaged perpetrated on DenSco and Mr. Chittick, either directly, or through one of Menaged's entities; Menaged's communications with DenSco and Chittick; Menaged's communications with Mr. Beauchamp; the actions or conduct related to Menaged's criminal indictment, plea bargain, or sentencing in the United States District Court for the District of Arizona; and Mr. Amoroso's communications with DenSco and Mr. Chittick.

8. Alberto Pena
c/o Law Office of Cameron A. Morgan
4356 North Civic Center Plaza
Suite 101
Scottsdale, AZ 85251

Mr. Pena may have knowledge regarding Menaged's personal, financial, or business dealings with DenSco and Chittick; the fraud(s) Menaged perpetrated on DenSco and Chittick, either directly, or through one of Menaged's entities; Menaged's communications with DenSco and Mr. Chittick; and the actions or conduct related to Mr. Pena's and Menaged's criminal indictment, plea bargain, or sentencing in the United States District Court for the District of Arizona.

9. Troy Flippo
c/o Storrs Law Firm PLLC
1421 East Thomas Road
Phoenix, AZ 85014

Mr. Flippo may have knowledge regarding Menaged's personal, financial, or business dealings with DenSco and Mr. Chittick; the fraud(s) Menaged perpetrated on DenSco and Mr. Chittick, either directly, or through one of Menaged's entities; Menaged's communications with DenSco and Chittick; and the actions or conduct related to Flippo's and Menaged's criminal indictment, plea bargain, or sentencing in the United States District Court for the District of Arizona.

10. Menaged family members, including, Joseph Menaged, Michelle Menaged, Jennifer Bonfiglio, Joy Menaged, Jess Menaged

Menaged's family may have knowledge regarding Menaged's personal, financial, or business dealings with DenSco and Chittick; the fraud(s) Menaged perpetrated on DenSco and Chittick, either directly, or through one of Menaged's or his Family's entities; the use of funds obtained from DenSco; Menaged's communications with DenSco and Chittick; and the

actions or conduct related to Menaged's criminal indictment, plea bargain, or sentencing in the United States District Court for the District of Arizona.

11. Shawna Heuer
c/o Bonnett Fairbourn, PC
2325 E. Camelback Road
Phoenix, Arizona 85016

Ms. Heuer is expected to have knowledge regarding Mr. Beauchamp's work on behalf of DenSco after Mr. Chittick's death and her communications with Mr. Beauchamp. Ms. Heuer may also have knowledge regarding Mr. Chittick and DenSco's business, and Mr. Chittick's communications with Mr. Beauchamp, Menaged, or DenSco's investors.

12. Jeff Goulder
Stinson Leonard Street
1850 North Central Avenue, Suite 2100
Phoenix, Arizona 85004

Mr. Goulder is expected to have knowledge regarding the negotiations of the Forbearance Agreement. Mr. Goulder also may have knowledge regarding Menaged's businesses, business practices, and finances. Mr. Goulder also may have knowledge regarding Menaged's communications with Mr. Beauchamp.

13. David Preston
c/o Gammage & Burnham
2 N. Central Avenue, Suite 15
Phoenix, Arizona 85004

Mr. Preston is expected to have knowledge regarding DenSco and Mr. Chittick's finances and tax returns. Mr. Preston is also expected to have knowledge regarding Mr. Chittick's retirement plan.

14. DenSco Investors

The Investors are expected to have knowledge regarding Mr. Chittick's communications to the Investors and their knowledge of DenSco's business, the status of their investments, and the status of DenSco's loans at all relevant times.

15. PMK Chase Bank
3800 North Central Avenue
Suite 460
Phoenix, AZ 85012

Chase Bank is expected to have knowledge regarding Menaged's banking practices, including Menaged's use of Chase Bank to perpetrate his fraud on DenSco and Chittick.

16. PMK US Bank
3800 North Central Avenue
Suite 460
Phoenix, AZ 85012

US Bank is expected to have knowledge regarding Menaged's banking practices, including Menaged's use of Chase Bank to perpetrate his fraud on DenSco and Chittick.

17. Gregg Seth Reichman/Active Funding Group
Attention: Andrew Abraham
702 East Osborn Road
Suite 200
Phoenix, AZ 85014

Mr. Reichman may have knowledge regarding Menaged's businesses, business practices, and finances; the fraud(s) Menaged perpetrated on DenSco and Mr. Chittick, either directly, or through one of Menaged's entities; and Mr. Reichman or his entities' (including Active Funding Group) participation in any of those fraudulent schemes (as suggested by the Receiver's Petition No. 45).

18. Daniel Schenk
c/o Coppersmith Brockelman, PLC
2801N. Central Avenue, Suite 1900
Phoenix, Arizona 85004

Mr. Schenk is expected to have knowledge regarding any work he performed on behalf of DenSco and Mr. Chittick in his capacity as president of DenSco. Mr. Schenk may also have knowledge of Menaged's communications with Beauchamp, Menaged communications with Mr. Chittick, and Mr. Beauchamp's communications with Mr. Chittick.

19. Robert Anderson
c/o Coppersmith Brockelman, PLC
2802N. Central Avenue, Suite 1900
Phoenix, Arizona 85004

Mr. Anderson is expected to have knowledge regarding any work he performed on behalf of DenSco and Mr. Chittick in his capacity as president of DenSco.

V. PERSONS WHO HAVE GIVEN STATEMENTS.

None at this time. Discovery is continuing. Defendants may supplement.

VI. EXPERT WITNESSES.

Defendants will identify expert witnesses in accordance with the schedule ordered by the Court.

VII. COMPUTATION AND MEASURE OF DAMAGES.

Plaintiff is not entitled to recover damages against Defendants.

Discovery is continuing. Defendants may supplement.

VIII. EXHIBITS.

Defendants have not yet identified which of the documents listed in Section IX below will be used at trial, and therefore expressly reserve the right to introduce any of the listed documents as exhibits at trial. Defendants may also use any documents identified in any other

party's disclosure statement or otherwise disclosed in this matter. By reserving the right to introduce any of the listed documents as exhibits at trial, Defendants do not waive their right to object to the introduction of any of these documents at the time of trial. Defendants will supplement this initial disclosure statement in accordance with Arizona Rules of Civil Procedure 26.1(b)(2).

Discovery is continuing. Defendants may supplement.

IX. LIST OF RELEVANT DOCUMENTS.

Defendants have not yet identified any additional relevant documents. The following documents, or categories of documents, may be relevant or lead to discovery of admissible evidence in this action and have already been exchanged or are being produced herewith:

1. Documents previously produced by Clark Hill bates labeled CH_0000001-13330.
2. Additional documents produced herewith by Clark Hill bates labeled CH_0013331-13374.
3. Documents previously produced by Plaintiff including bates labeled DIC000001-25330, 28634-53950 and Quickbooks backup.
4. Documents previously produced by Plaintiff including bates labeled D126751-128731 and 130972-133111.
5. Documents previously produced by Bryan Cave in response to Subpoena Duces Tecum bates labeled BC000001-3188.
6. Documents produced herewith by Dave Preston in response to Subpoena Duces Tecum bates labeled DP000001-601.
7. Any and all documents in CR-17-00680, United States of America v. Yomtov Scott Menaged, et al.
8. All documents produced by any party or third party in this litigation.

9. All pleadings, filings, minute entries, orders and judgments.

10. All deposition or hearing transcripts in the above captioned litigation.

11. All transcripts from any Section 341 creditor meetings, Rule 2004 examinations, depositions, or hearings in Yomtov Menaged's bankruptcy pending in the United States Bankruptcy Court for the District of Arizona at 2:16-bk-04268.

Defendants reserves the right to supplement the list of documents that may be relevant as information becomes available.

X. INSURANCE AGREEMENTS.

Defendants produce the insurance policies in effect during the relevant time period and the November 10, 2017 correspondence from Mendes & Mount, LLP, all of which are stamped "Confidential Materials."

DATED this 20th day of March, 2018.

COPPERSMITH BROCKELMAN PLC

By: _____
John E. DeWulf
Marvin C. Ruth
Vidula U. Patki
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