

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF NEW YORK

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SECURITIES AND EXCHANGE COMMISSION

Plaintiff,

vs.

Case No. 1:10-CV-457
(GLS/CFH)

McGINN, SMITH & CO., INC.,
McGINN, SMITH ADVISORS, LLC
McGINN, SMITH CAPITAL HOLDINGS CORP.,
FIRST ADVISORY INCOME NOTES, LLC,
FIRST EXCELSIOR INCOME NOTES, LLC,
FIRST INDEPENDENT INCOME NOTES, LLC,
THIRD ALBANY INCOME NOTES, LLC,
TIMOTHY M. MCGINN, AND
DAVID L. SMITH, GEOFFREY R. SMITH,
Individually and as Trustee of the David L. and
Lynn A. Smith Irrevocable Trust U/A 8/04/04,
LAUREN T. SMITH, and NANCY MCGINN,

Defendants,

LYNN A. SMITH and
NANCY MCGINN,

Relief Defendants. and

GEOFFREY R. SMITH, Trustee of the
David L. and Lynn A. Smith Irrevocable
Trust U/A 8/04/04,

Intervenor.
-----X

**NOTICE OF FIFTH CLAIMS MOTION OF WILLIAM J. BROWN, AS
RECEIVER, FOR AN ORDER APPLYING PREFERENTIAL PAYMENT
OFFSET TO CERTAIN PREFERRED INVESTOR CLAIMS**

PLEASE TAKE NOTICE that upon the Fifth Claims Motion of William J. Brown, as Receiver, for an Order applying the Preferential Payment Offset to certain Preferred Investor Claims (“Motion”), Phillips Lytle LLP will move before the Hon. Christian F. Hummel, United States Magistrate Judge, United States District Court for the Northern District of New York, James T. Foley - U.S. Courthouse, 445 Broadway, Albany,

New York 12207-2924, on November 15, 2018 at 9:30 a.m., seeking an Order to be entered approving the Motion. No oral argument is requested.

PLEASE TAKE FURTHER NOTICE that objections, if any, to the relief requested in the Motion must be made in writing, and should be filed and served upon the undersigned at the address listed below in accordance with the Federal Rules of Civil Procedure and the Local Rules for the United States District Court for the Northern District of New York.

PLEASE TAKE FURTHER NOTICE that if no responses are timely filed and served with respect to the Motion or any claim listed in Exhibits A and B to the Motion, the Court may enter an Order granting the Motion and applying the Preferential Payment Offset without further notice or opportunity to be heard offered to any party.

Dated: October 15, 2018

PHILLIPS LYTTLE LLP

By /s/ Catherine N. Eisenhut
William J. Brown (Bar Roll #601330)
Catherine N. Eisenhut (Bar Roll #520849)

Attorneys for Receiver
Omni Plaza
30 South Pearl Street
Albany, New York 12207
Telephone No. (518) 472-1224

and

One Canalside
125 Main Street
Buffalo, New York 14203
Telephone No.: (716) 847-8400

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**FIFTH CLAIMS MOTION OF WILLIAM J. BROWN, AS RECEIVER, FOR
AN ORDER APPLYING PREFERENTIAL PAYMENT OFFSET TO
CERTAIN PREFERRED INVESTOR CLAIMS**

William J. Brown, as Receiver (“Receiver”), by his counsel, Phillips Lytle LLP,
moves (the “Motion”) for an order applying the Preferential Payment Offset to certain
Preferred Investor Claims, and respectfully represents as follows:

The Receiver files the Motion to request entry of an Order applying the Preferential Payment Offset to certain Preferred Investor Claims held by One City Center Associates (“OCC”) and Burton Fisher (“Fisher”)¹ as set forth on attached Exhibits A and B, and based on the accompanying Memorandum of Law and Declaration of William J. Brown, as Receiver (“Declaration”), each dated October 15, 2018.

RELIEF REQUESTED

The Receiver requests that the Court enter an Order substantially in the form attached as Exhibit C (“Order”) applying the Preferential Payment Offset to the Preferred Investor Claims as set forth on Exhibits A and B to the Motion, together with such other and further relief as the Court deems just and proper.

The Receiver reserves all rights to object on any other basis to the claims of all investors or claimants, including OCC and Fisher.

Dated: October 15, 2018

PHILLIPS LYTTLE LLP

By /s/ Catherine N. Eisenhut
William J. Brown (Bar Roll #601330)
Catherine N. Eisenhut (Bar Roll #520849)
Attorneys for Receiver
Omni Plaza
30 South Pearl Street
Albany, New York 12207
Telephone No. (518) 472-1224

and

One Canalside
125 Main Street
Buffalo, New York 14203
Telephone No.: (716) 847-8400

¹ It is the Receiver’s practice consistent with prior Court direction to avoid referring to individual investors by name in publicly filed documents and to instead rely on claim numbers to identify investors. Since counsel to OCC and to Fisher previously named OCC and Fisher in the Memorandum of Law in Opposition to Fourth Claims Motion of William J. Brown, as Receiver, for an Order (A) Disallowing Preferred Investor Paper Claims and (B) Applying Preferential Payment Offset (Docket No. 1019), the Receiver will also refer to OCC and Fisher by name.
Doc #01-3153906.2

Exhibit A

Exhibit A
Preferential Payments

Claim No.	Investor	Description	Claim Amount	Proposed First Distribution (10%)	Proposed First Distribution After Fourth Claims Motion Offset	Total Preferential Payment Amount	Further Adjusted Distribution
5946-5948	One City Center Associates, LLC	FEIN SECURED SENIOR SUBORDINATED NOTES DUE 12/15/2009	\$700,000.00	\$70,000.00	\$40,992.50	\$33,468.75	\$7,523.75
4809, 4813	Burton Fisher	TAIN SECURED JUNIOR NOTES DUE 12/15/2010	\$111,000.00	\$11,100.00	\$4,050.01	\$866.25	\$3,183.76

Exhibit B

Exhibit B
Unspecified Preferential Payments

Claim No.	Investor	Description	Claim Amount	Proposed First Distribution (10%)	Proposed First Distribution After Fourth Claims Motion Offset	Preferential Payment Offset from Exhibit A	Total Unspecified Preferential Payment Amount	Further Adjusted Distribution
5946-5948	One City Center Associates, LLC	FEIN SECURED SENIOR SUBORDINATED NOTES DUE 12/15/2009	\$700,000.00	\$70,000.00	\$40,992.50	\$33,468.75	\$172,097.50	(\$164,573.75)

Exhibit C

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF NEW YORK

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Individually and as Trustee of the David L. and
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LAUREN T. SMITH, and NANCY McGINN,

Defendants,

LYNN A. SMITH and
NANCY McGINN,

Relief Defendants. and

GEOFFREY R. SMITH, Trustee of the
David L. and Lynn A. Smith Irrevocable
Trust U/A 8/04/04,

Intervenor.
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**ORDER APPROVING FIFTH CLAIMS MOTION OF WILLIAM J. BROWN,
AS RECEIVER, FOR AN ORDER APPLYING PREFERENTIAL PAYMENT
OFFSET TO CERTAIN PREFERRED INVESTOR CLAIMS**

Upon the Fifth Motion of William J. Brown, as Receiver, for an Order Applying Preferential Payment Offset to Certain Preferred Investor Claims; and notice of the Motion having been given to the Securities and Exchange Commission, each of One City Center Associates (“OCC”) and Burton Fisher (“Fisher”) by first class mail, and all parties who have filed a Notice of Appearance in this action by ECF, and all creditors of the McGinn, Smith entities and other parties in interest via the Receiver’s website, which notice

is deemed good and sufficient notice; and the Court having deemed that sufficient cause exists; it is therefore

ORDERED, that the Motion is approved, and it is further

ORDERED, that the application of the Preferential Payment Offset to reduce the distributions to OCC and Fisher is approved as set forth on Exhibits A and B to the Motion, and the rights of the Receiver to object on any other basis to the claims of all investors or claimants, including OCC and Fisher, are expressly preserved.

Dated: _____, 2018

HON. CHRISTIAN F. HUMMEL

Doc #01-3154012.1

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF NEW YORK

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TIMOTHY M. MCGINN, AND :
DAVID L. SMITH, GEOFFREY R. SMITH, :
Individually and as Trustee of the David L. and :
Lynn A. Smith Irrevocable Trust U/A 8/04/04, :
LAUREN T. SMITH, and NANCY MCGINN, :

Defendants, :

LYNN A. SMITH and :
NANCY MCGINN, :

Relief Defendants, :

- and - :

GEOFFREY R. SMITH, Trustee of the :
David L. and Lynn A. Smith Irrevocable :
Trust U/A 8/04/04, :

Intervenor. :

-----X

**DECLARATION OF WILLIAM J. BROWN, AS RECEIVER, IN SUPPORT OF
FIFTH CLAIMS MOTION FOR AN ORDER APPLYING PREFERENTIAL
PAYMENT OFFSET TO CERTAIN PREFERRED INVESTOR CLAIMS**

William J. Brown, as Receiver, declares, under the penalty of perjury, pursuant to 28

U.S.C. § 1746, as follows:

1. I am the Receiver of McGinn, Smith & Co. Inc., et al. (“MS & Co.”) appointed by the Court in this action pursuant to the Preliminary Injunction Order dated July 26, 2010 (Docket No. 96).

2. I make this Declaration in support of the Receiver’s Fifth Claims Motion (“Motion”) for an Order applying the Preferential Payment Offset to certain claims held by One City Center Associates (“OCC”) and Burton Fisher (“Fisher”).

PROCEDURAL BACKGROUND

3. MS & Co. was a broker-dealer registered with the Securities and Exchange Commission (“SEC”) with its headquarters in Albany, New York from 1981 to 2009. From 2003 through 2010, the broker-dealer was owned by David L. Smith (“Smith”), Timothy M. McGinn (“McGinn”), and Thomas E. Livingston.

4. On April 20, 2010, the Securities and Exchange Commission (“SEC”) filed a Complaint initiating the above-captioned action (Docket No. 1). Also, on April 20, 2010, this Court granted a Temporary Restraining Order (Docket No. 5), which, among other things, froze certain assets of the above-captioned Defendants and Relief Defendants, and appointed the Receiver as temporary receiver with respect to numerous entities controlled or owned by Defendants Timothy M. McGinn and David L. Smith including those listed on Exhibit A to the Preliminary Injunction Order entered in this action (Docket No. 96) (collectively, the “MS Entities”).

5. On July 26, 2010, following a hearing, the Court entered an order granting the SEC’s Motion for a Preliminary Injunction and appointing the Receiver as receiver, pending a final disposition of the action (“Preliminary Injunction Order”) (Docket No. 96).

6. On August 3, 2010, the SEC filed an Amended Complaint (Docket No. 100). On June 8, 2011, the SEC filed a Second Amended Complaint (the “Complaint”) (Docket No. 334). On February 17, 2015, the Court issued its Memorandum-Decision and Order (Docket No. 807) (“MDO”) granting the SEC’s motion for summary judgment. The Court entered judgments in favor of the SEC in 2016 (Docket Nos. 835, 836, 837).

7. Generally, McGinn and Smith “orchestrated an elaborate Ponzi scheme, which spanned over several years, involved dozens of debt offerings, and bamboozled hundreds of investors out of millions of dollars.” MDO at 7. McGinn and Smith raised over \$136 million between 2003 and 2010 in over twenty unregistered debt offerings, including the Four Funds -- FAIN, FEIN, FIIN, and TAIN -- and various Trust Offerings, by representing that investor money would be “invested,” when instead it was “funneled” into various entities owned or controlled by McGinn and Smith. That money was then used to fund unauthorized investments and unsecured loans, make interest payments to investors in other entities and offerings, support McGinn’s and Smith’s “lifestyles,” and cover the payroll at MS & Co. MDO at 7.

THE FOUR FUNDS

8. The Four Funds—FAIN, TAIN, FIIN, and FEIN— were single-purpose, New York limited liability companies formed between September 2003 and October 2005. The private placement memoranda (“PPMs”) for each of the Four Funds were substantively identical, and each offered \$20 million worth of Notes, with the exception of TAIN, which offered \$30 million. The offerings had three tranches of Notes, which paid quarterly interest of 5% to 10.25%, and promised a return of principal at maturity in one, three or five years. MDO at 10.

9. McGinn and Smith engaged in a course of conduct and dealings that were contrary to the PPMs issued for the Four Funds. First, investor proceeds from the Four Funds were used to purchase contracts from pre-2003 trusts for the purpose of redeeming or making interest payments to investors. Second, the Four Funds used investor money to directly invest in, rather than purchase investments from, affiliates. Many of the affiliated investments provided no cash flow to the Four Funds and were ultimately considered worthless. Finally, proceeds from the Four Funds were funneled through McGinn Smith Transaction Funding Corporation (“MSTF”) and then used to pay MS & Co.’s payroll. MDO at 11-12.

10. In late 2007, David Smith received an e-mail from David Rees, MS & Co.’s comptroller, which showed a \$48.8 million deficit in the Four Funds. Notwithstanding that deficit, Smith continued to solicit new investments in the Four Funds. MDO at 12. On January 15, 2008, Smith sent a letter to investors in the Four Funds notifying investors that interest payments on the junior tranches of Notes were being reduced from 10.25% to 5%. *See* Letter attached hereto as **Exhibit A**. By April 2008, interest payments on the junior tranches of Notes were eliminated entirely. *See* Letter attached hereto as **Exhibit B**. The reduction, and subsequent elimination, of interest payments were attributed by McGinn and Smith to the collapse of various debt and credit markets and the “sub prime mess.” In October 2008, David Smith sent a letter to all Note holders in the Four Funds, outlining a restructuring plan which extended the maturity dates of the Notes, reduced interest payments for all tranches, and forfeited all future fees due to MS & Co. *See* Letter attached as **Exhibit C**; MDO at 12-13.

PREFERENTIAL PAYMENTS

11. Most investors in the junior tranches of the Four Funds Notes received reduced interest payments starting in January 2008 and stopped receiving interest payments altogether by April 2008. OCC, however, continued to receive interest payments on its junior Four Funds Notes (“Preferential Payments”) in excess of what other investors were receiving. In February, 2008, OCC received the same reduced 5% interest payment that other investors received, and, in addition, Preferential Payments making up the difference between the 5% interest payment and the full 10.25% interest payments that all investors were supposed to receive.

12. I have recovered wire transfer confirmations dated February 4, 2008, showing Preferential Payments made to OCC in the aggregate amount of \$34,355.00 on account of OCC’s investments at the time in FIIN, FEIN, and TAIN Notes, representing the “gap” 5.25% interest that other investors did not receive in February 2008. *See Exhibits D(1) - D(3)*. These Preferential Payments came from MSF funds, and were not proceeds of the Four Funds.

13. Certain of OCC’s Four Funds investments were transferred to Fisher after OCC received the Preferential Payments. An excerpt from the original investment register for the TAIN 10.25% Secured Junior Notes (“Investment Register”) is attached as **Exhibit E**. The Investment Register was an excel spreadsheet maintained internally at MS & Co. to track investments. The Investment Register has been edited to remove certain extraneous information. The Investment Register shows that on January 8, 2009, the TAIN investment held by OCC was transferred to Burton Fisher.

14. In addition to the Preferential Payments that OCC received in February 2008, OCC also received a series of supplemental payments through 2008 that other investors did not receive (“Unspecified Preferential Payments”). From April 2008 through to October 2008, OCC received five Unspecified Preferential Payments aggregating \$172,097.50. I have recovered copies of cashier’s checks issued by Mercantile Bank from an account held by McGinn Smith Funding to OCC evidencing the Unspecified Preferential Payments. *See* Exhibits D(4) - D(8).

15. All of OCC’s and Fisher’s claims (collectively, “Preferred Investor Claims”), have been adjusted for pre-Receivership distributions of principal and interest like all other investor claims, as shown on the Receiver’s Claims Website (defined below). The Preferred Investor Claims, however, have not been adjusted to account for the Preferential Payments or the Unspecified Preferential Payments.

16. All of the Preferential Payments and Unspecified Preferential Payments received by OCC are listed in the attached **Exhibit D**. For each Preferential Payment or Unspecified Preferential Payment, Exhibit D describes the payment amount, the payment date, and the evidence supporting such payment. Exhibit D identifies the exhibit number for each piece of evidence supporting the Preferential Payments and the Unspecified Preferential Payments. The evidence described in Exhibit D is attached in the exhibits following Exhibit D.

CLAIMS PROCEDURE

17. On March 9, 2012, in my capacity as Receiver, I filed a Motion (“Claims Procedure Motion”) (Docket No. 466) for entry of an Order approving, among

other things, the Receiver's proposed procedure for the administration of claims against the MS Entities.

18. On March 27, 2012, the Court entered an Order granting the Claims Procedure Motion (Docket No. 475), which was subsequently amended by an Order dated April 17, 2012 ("Claims Procedure Order") (Docket No. 481). Each investor and known creditor of the MS Entities was mailed on May 1, 2012 an Access Notice describing the claims process and enclosing (i) Notice of the Claims Bar Date and Claims Procedure and (ii) a Claim Form. A confidential password providing access to the Receiver's Claims Website at www.mcginnsmithreceiver.com ("Claims Website") was also provided. If an investor or creditor agreed with the description and amount of their claim(s) as listed on the Claims Website and the claim(s) were not listed as disputed, contingent or unliquidated, the investor or creditor did not need to take any further action. All other investors and creditors needed to timely file a paper claim before the bar date of June 19, 2012, as further described in detail on the Claim's Website.

19. The Claims Procedure Order established June 19, 2012 ("Bar Date") as deadline for creditors and investors to file claims against the MS Entities.

20. In accordance with the Claims Procedure Order, nearly six hundred creditors and investors timely filed paper claims prior to the Bar Date. In addition, more than 3,127 claims of investors and creditors were included on the schedules posted by the Receiver on the Claims Website in accordance with the Claims Procedure Order.

21. The Receiver conducted an initial review of the paper claims timely filed by creditors and investors in accordance with the Claims Procedure Order and determined it was necessary to establish a reserve as to investor claims totaling

approximately \$23,617,190 since those claims have been listed by the Receiver as disputed, contingent or unliquidated.

PLAN OF DISTRIBUTION PROCESS

22. On December 30, 2015, the Receiver filed a Motion (Docket No. 847) (“Plan Distribution Motion”) to seek approval of (i) a plan of distribution of assets of the MS Entities to investors (“Plan of Distribution”); and (ii) interim distributions to investors with allowed claims scheduled or timely filed in accordance with the Claim Procedure Order.

23. On October 31, 2016, the Court entered a Memorandum-Decision and Order (Docket No. 904) (“Plan Distribution Order”) granting the Plan Distribution Motion, overruling objections, approving the Plan of Distribution, and allowing the Receiver to make interim distributions as set forth in the Plan Distribution Motion.

24. Among other things, the Plan of Distribution provides for a reserve for disputed claims to allow the Receiver to make initial distributions, but to also provide for funds to be reserved until any objections to disputed claims can be heard and decided by final order of the Court. As of July 6, 2018, \$6,308,887 has been distributed to investors with allowed claims as a First Distribution.

25. The Plan of Distribution provides that all investor claims would be calculated by using the “Net Investment” methodology, i.e., the claim amount is equal to the amount of the initial investment made less any distributions received prior to the appointment of the Receiver, including any distributions of principal or interest. Plan of Distribution, Art. IV. The Plan of Distribution further provides for a collateral recovery offset (“Collateral Recovery Offset”), where distributions made on account of investor

claims will be reduced on a dollar-for-dollar basis to the extent the investor has received a recovery from a source other than the Receivership in connection with their claimed loss.

Id. Art. II.

CLAIMS MOTIONS

26. On September 21, 2017, in my capacity as Receiver, I filed a Motion (Docket No. 937) (“First Claims Motion”) to seek disallowance of certain filed paper claims that were duplicative of the corresponding claims granted by the Receiver. On November 9, 2017, I filed a Statement (Docket No. 957) in furtherance of the First Claims Motion, adjourning the First Claims Motion with respect to those duplicative investor paper claims filed by investors whose Receiver-granted claims have been disputed by the Receiver. On December 28, 2017, the Court entered an Order granting the First Claims Motion and disallowing the duplicative paper claims other than with respect to those filed by investors with disputed claims (Docket No. 966).

27. On February 15, 2018, in my capacity as Receiver, I filed a Motion (Docket No. 974) (“Second Claims Motion”) to seek disallowance of certain filed paper claims for which there is no basis for payment in the books and records of MS & Co. On April 13, 2018, the Court entered an Order granting the Second Claims Motion and disallowing the paper claims.

28. On March 19, 2018, in my capacity as Receiver, I filed a Motion (Docket No. 984) (“Third Claims Motion”) to seek disallowance of certain claims of former MS & Co. brokers. On May 4, 2018, I filed a Reply (Docket No. 1002) to the Response of Frank Chiappone (Docket No. 995) to the Third Claims Motion. That Motion remains pending.

29. On July 6, 2018, in my capacity as Receiver, I filed a Motion (Docket No. 1009) (“Fourth Claims Motion”) to seek disallowance of certain paper claims filed by Preferred Investors and to apply a Preferential Payment Offset to the distributions to be made to Preferred Investors. On August 27, 2018, I filed a Reply (Docket No. 1020) (“Reply”) to the Opposition filed by certain Preferred Investors (Docket No. 1019) to the Fourth Claims Motion. The Reply contained brokerage statements, wire transfer confirmations, and copies of cashier’s checks supporting the Receiver’s claims as to all of the Preferential Payments alleged in the Fourth Claims Motion. OCC and Fisher were among the Preferred Investors described in the Fourth Claims Motion, but the payments made to OCC described above were not addressed in the Fourth Claims Motion

APPLICATION OF THE PREFERENTIAL PAYMENT OFFSET

30. To apply the Preferential Payment Offset, I have used the books and records of MS & Co., including records of wire transfers and bank checks, to determine when the Preferential Payments and the Unspecified Preferential Payments were made to OCC and, if discernable, on account of which specific investment the Preferential Payment was made. Presently, OCC only has claims for investments made in FEIN. Accordingly, I have applied the Preferential Payment Offset to OCC’s distribution on account of its FEIN claims.

31. The evidence I recovered shows that in February 2008, OCC received a Preferential Payment in the amount of \$866.25 on account of the TAIN investment it held at the time. The Investment Register shows that on January 8, 2009, that TAIN investment

was transferred to Fisher. Accordingly, the Receiver has applied the Preferential Payment Offset for this Preferential Payment to Fisher's TAIN Claims.¹

NOTICE

32. In connection with service of the Motion and all accompanying papers, including this Declaration, I will cause to be mailed to each of OCC and Fisher's legal representative a copy of the Motion and related pleadings.

Dated: October 15, 2018

/s/ William J. Brown

William J. Brown

Doc #01-3153462.3

¹ I have recovered evidence in the books and records of MS & Co. that a portion of OCC's FIIN investment was also transferred to Fisher in January 2009. It is unclear, however, exactly what portion of the investment was transferred to Fisher and so I have elected to apply the Preferential Payment received by OCC in February 2008 in connection with its FIIN investment to OCC's distribution on account of its remaining Four Funds Claims.

Exhibit A

January 15, 2008

Re: \$ _____ Third Albany Income Notes, LLC – Internal Investment # _____
Registration: _____

Dear: _____

As an investor in one of the following mezzanine debt funds (FUNDS) managed by McGinn, Smith Advisors (MSA), we thought that it was important to communicate with you the general status of the funds, our view on the current credit markets and their impact on your fund, how MSA views the markets going forward, and steps that we are considering to address the present credit conditions.

The FUNDS include:

- First Independent Income Notes, LLC
- First Excelsior Income Notes, LLC
- Third Albany Income Notes, LLC
- First Advisory Income Notes, LLC

Each of the LLC's has three series of notes that have been issued: Senior Notes, Senior Subordinated Notes, and Junior Notes, all with varying interest rate coupons and maturities. In each of the LLC's, the notes starting with the Senior down through the Junior have a primary call on the assets and cash flow of the various investments in each of the LLC's. Thus, the Senior Notes receive all of the income and asset value of the entire LLC until satisfied, followed by the Senior Subordinate Notes, and finally the Junior Notes are entitled to asset coverage and cash flow only after the Senior and Senior Subordinate Notes are satisfied. You are an investor in the Junior Notes.

MSA is the sole equity member of all the FUNDS, and therefore as the managing member is responsible for all the decisions impacting the business of the FUNDS. MSA has a fiduciary responsibility to manage the FUNDS in a manner consistent with the investment goals and to best preserve the assets of the FUNDS.

Over the last several months, a number of investors have inquired as to the impact on the FUNDS due to the turmoil, and in some cases collapse, of the various debt and credit markets, as a result of the sub-prime mortgage debt crises that started to boil over in July of 2007. As the impact has grown, and in our judgment the crisis shows less and less probability of being resolved quickly and easily, MSA has begun an effort to get

ahead of events and formulate strategies that will protect the value of the LLC's and your investment in them.

While the media, including newspapers and financial publications, have provided a daily accounting of the credit market crisis and the subsequent financial impact, I realize some of you may not be in a position or have the interest to follow what has been taking place, so I have provided a brief summary. First, it should be understood that the credit crisis is primarily a result of the major Wall Street investment banks and the largest commercial banks in the country developing and marketing a variety of investment instruments built on a shaky foundation of sub prime mortgages. Sub prime mortgages can be defined as those mortgages offered to borrowers with spotty credit, mortgages that required too little equity, mortgages on properties in less desirable areas or where the supply of housing was growing beyond the demand, and where the terms of the mortgage often emphasized "teaser rates" or interest only requirements early in the amortization schedule. While these types of mortgages carry a high risk of default, the early years of the recent housing boom produced unusually low rates of default and created a false sense of security for the mortgage lenders.

In pure destructive power, the sub prime mess has become Wall Street's version of Hurricane Katrina. It has reeked havoc on the nation's largest brokerage firm, Merrill Lynch, and biggest bank, Citigroup, which have announced billions of dollars in losses and have fired their celebrated CEOs. Dozens of similar companies in the mortgage business have folded completely. As stunning as today's losses are, more carnage lies ahead. Wall Street banks are holding tens of billions in risky securities on their books, and no one seems to have any idea what they are worth. The follow on crisis is that confidence in the value of all securities, but mostly the smaller and more illiquid securities, is destroyed. Investors are reluctant to pay any price because they are not sure what the real value is, and if they are forced to sell them in the future they may do so only by slashing prices. Thus, investors go on strike and refuse to bid any price. In addition, many of these securities were purchased with debt. As prices go down, lenders require more security through increased equity. To get equity and raise cash, investors have to sell the illiquid securities. With no real markets, prices are driven forever lower, and a vicious cycle is started. In a high number of cases, there is simply no price that investors are willing to pay, and the value of the securities must be further marked down, generally based on some theoretical model put together by the investment bankers. That is why Merrill Lynch predicted a \$4.5 billion sub prime loss for the third quarter, then jolted investors and analysts three weeks later by announcing that its real default was \$7.9 billion, or 76% more than the initial estimate. And just last week, Merrill Lynch again announced an increase in their losses to over \$15 billion dollars, approximately 3 ½ times their original estimate. And Merrill is not alone. Losses on CDO's, asset backed securities, and other structured products include announced losses by Citigroup (\$9.8 billion, followed by an additional \$24 billion dollars as of January 14th). UBS (\$4.4 billion), and Morgan Stanley (\$3.7 billion). These conditions, aside from producing real and enormous losses for the holders of these debt instruments are creating a far more difficult problem for the capital markets in general. The aforementioned lack of liquidity, or the inability to sell ones investments, causes enormous difficulty throughout the investment cycle. For example, companies who are looking to raise equity either in the private or public markets often borrow capital in the form of short term debt in order to

"bridge" the time between the present and when they can complete their equity offering, a time that can easily take up to one year. This type of credit has become increasingly scarce as lenders are withdrawing from the markets until they have a better level of comfort regarding risk and their own financial condition. Merger and acquisition activity that is often financed with debt has dramatically decreased. The last six months has seen daily announcements of the withdrawal of financings for these types of transactions. Meanwhile, the funds at the heart of the situation known as structured investment vehicles or SIV's – need to find investors for billions of dollars coming due in the next six to twelve months. However, as ratings firms come out with reports that lower the ratings of these type of securities, this causes a further depression in the value of those investments and a large number of buyers are now precluded from investing because their corporate indenture prevents them from investing in lower rated securities. Holders of the SIV notes are bearing the brunt of this fallout because they face two options: they risk losing money if the SIV sells assets at a loss in order to meet their capital needs, including the payment of maturing notes, or try to provide liquidity for the SIV's by buying more of its debt. The FUNDS in which you are invested have some of those similar problems.

The impact on the FUNDS from the aforementioned credit crisis has primarily been on liquidity and the upcoming need to sell assets in the next year to pay off maturing notes. While there have been losses in the FUND's investments, we have a limited and manageable exposure to the real estate markets, including the mortgage market. Our real concern is the present and future ability to sell our present investments at a value that is needed to meet the FUND's obligations. When managing the FUND's assets, MSA always had to be mindful of meeting the future liquidity needs. It was always anticipated that those needs would be able to be met through a combination of having some of the assets mature at approximately the same time as its liabilities, that some of the assets would be invested in public securities with a ready market, that the FUNDS would have the ability to raise new capital from either present or new investors, and that some of the assets would be able to be sold to other investors. The credit crisis has impacted all of those strategies, and unless the markets dramatically improve over the next year, we will face the same challenges that we do today.

As mentioned previously, there presently is no market at fair prices that exist for non-public debt securities. Investors are now looking for the safest most liquid securities until the crisis is better understood or is resolved. In addition, many of the investments in these companies are dependent on new financings to have the capital to pay off their existing debt to the FUNDS. Several of our investments fall into this category. For example, we have an investment in several of the FUNDS in a company that provides print and advertising financing for the independent film industry. For the last nine months they have had a commitment from an investment bank to raise approximately \$10 mm in equity, contingent on the company's ability to secure a credit line of \$10-15 mm. That capital is to be used to retire their obligation to the FUNDS. To date, the company has been unable to procure the credit line, and thus the equity raise has been put on hold. They have no source of funds to repay us until that capital raise is completed. Thus, we have no choice but to extend their debt, probably past the time when our obligations to our debt holders are due. Another example is a company that we have financed that is in the business of evaluating and providing capital to companies based on the worth of the

company's intellectual property. A major investment bank has given the company a term sheet that will provide \$750 million of financing over the next five years. However, the original structure called for a substantial portion of that capital to be provided up front and that would be used to repay our debt. The investment bank is now only willing to provide the capital on a staggered basis over the next five years, with the result that while we are confident of being repaid in full, it is not likely that we will be paid out until the fourth and fifth year of their commitment. Again, a decision that will impact our liquidity for next year.

MSA has determined that we need to be very proactive over the next year to be in a position to overcome these credit market conditions and the lack of liquidity now present. If we have learned anything in being in the business for over 30 years, it is that a financial crisis is never solved in a short time or without substantial pain to investors. We don't believe that this one will be any different. We believe that the credit markets are likely to continue to be under very severe pressure and that a two to three year time horizon is the minimum for a return to normality.

MSA has spent the last several months reviewing a variety of strategies that will address the present problems and give our investors liquidity within a reasonable time frame from what they had originally expected.

First, any strategic approach has to recognize the capital structure of the FUNDS that calls for assets and cash flow to be pledged in their entirety to the most senior class of securities. Thus, as notes mature next year we need to be in a position to first retire the senior one year notes. We are confident that we will be in a position to maintain the current level of interest, and as long as conditions do not materially worsen; we will be able to retire the debt on a timely basis. The second class of securities issued by the LLCs is the Senior Subordinated Notes. Here too, as long as present conditions remain relatively stable, we believe that the current rate of interest will be maintained. However, the ability to retire the entire issue at the same time as the Senior notes is most unlikely. Our present thinking is that these notes will have to be extended for two-three years in order to establish the capital resources to pay off the debt. The third class of securities, the junior notes, present the biggest challenge because they are subordinate to the claims on assets and cash flow of the senior securities. In order to meet the obligations of the Senior securities, the FUNDS have to pledge all of their cash flow to them, thus at the present time the rate of interest is being reduced to 5% on the Junior notes until such time as some of our investments return to a timely cash flow or we can refinance our debt or raise additional capital. MSA is presently working on plans to provide the needed liquidity and help some of our investments restructure their debt in order to meet their obligations.

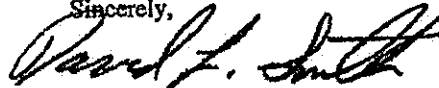
MSA is making a significant contribution to increasing the cash flow for all of the Funds by suspending the commissions due to McGinn, Smith & Co., the advisory fee due to MSA, and the administrative fee due to McGinn, Smith Capital Holdings. These fees for the combined Funds amount to \$2,827,500, annually.

Over the next year we will hopefully be able to get a better handle on how to evaluate our investments. This difficulty to evaluate remains the number one problem for credit markets today. During this summer's credit crunch, more than 80% of investors in bonds tied to the mortgage market said they had trouble obtaining price quotes from their bond dealers. "Michael Vranos, recently told investors in his large hedge-fund company, Ellington Management Group, that he was suspending investor redemptions because he couldn't figure out values for some of the fund's investments". "There is no way to determine values that would be simultaneously fair both to investors redeeming from the funds and to investors remaining in the funds", he wrote in a September 30th letter. Recently the Federal Reserve, in a move to make credit markets more liquid, announced a plan that is designed to enable banks to borrow money directly from the Fed at below-market rates. However, there can be no assurances that this plan will ease the current credit and liquidity crisis.

In conclusion, MSA believes that by trying to get out in front of the problem of having sufficient liquidity by next year when the FUNDS notes become due, they are both doing the right thing and will lesson the anticipated challenges a year from now. **The Senior and Senior Subordinated note holders will maintain current interest payments, while Junior note holders will have their interest reduced to 5%.** Over the course of the year we will communicate with you regarding the progress and plans that we are making to address the liquidity needs for next December. Our obvious goal is first preservation of your investment and second to maximize cash flow to the FUNDS in order to have sufficient cash to meet the interest payments.

If there are any questions concerning this communication, please contact your McGinn, Smith & Co. representative.

Sincerely,



David L. Smith
Managing Member
McGinn, Smith Advisors

Exhibit B

*McGinn Smith
& Company, Inc.*

Investment Bankers • Investment Brokers

6 Executive Park Dr.
Clifton Park, NY 12065
518-348-0060
Fax 518-348-0107
www.mcginnsmith.com

April 11, 2008



Re: \$25000 First Independent Income Notes, LLC – Internal Investment # 1800
Registration:

Dear

In our communication of January 15, 2008 we outlined for you the negative impact that the present credit crisis resulting from the sub-prime mortgage collapse was having on First Independent Income Notes (FIIN), LLC. We provided the background leading to the crisis and reasons why we felt it was likely to worsen before the markets were able to stabilize. We cited the tremendous losses that the major commercial and investment banks were being forced to take and that these losses were spreading to institutions worldwide and to credit markets far beyond the mortgage business. We mentioned that the major impact was on market liquidity and that debt holders were being forced to sell securities and investments at prices below fair market value in an effort to deleverage their balance sheets and to meet forced margin calls. Unfortunately, all the problems that we cited have become more acute, and by now the daily news brings repeated announcements of the adverse effects the crisis is having on the general economy and of major financial institutional failures such as the collapse of Bear Stearns, Inc.

The central theme for all fixed income investments and managed funds of such investments has been the inability to refinance their investments and thus be forced to cease or eliminate interest payments and distributions. Leading the way in this category has been the area of Auction Rate Securities (ARS) which are long term municipal bonds, corporate bonds, and preferred stocks that are traded at auctions that set the instrument's interest rate and ultimately the price of the security. The market in total is somewhere around \$320 billion and it is estimated that \$80 billion or 25% of the market has recently failed. These investments were often marketed as substitutes for money market accounts with a higher yield. Many businesses invested their excess cash in these instruments and now find themselves not only not receiving interest, but with no access to their cash as well. The good news is that the majority of the underlying investments are still paying interest, but the funds just are not able to refinance them at rates that allow them to pay investors their principal.

Since our last communication with you, two of our investments have been forced to eliminate their dividend or cease distributions. One was a result of their loss of refinancing from a bank that was a major lender to Countrywide Credit, the country's largest sub-prime mortgage lender and who suffered major losses from that relationship and had to withdraw their commitment. The other was a holder of only AAA mortgages and who in November assured us that they were at limited risk and the dividend was safe. In February, they were forced to sell most of their portfolio to meet margin calls and suffered losses that have wiped out their earnings

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EXHIBIT

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and their ability to pay their dividend. This in turn has put increased pressure on our cash flow and our ability to meet our obligations. Consequently, we are being forced to eliminate the interest payment to the Junior Subordinated debt holders for this quarter.

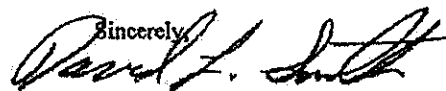
In keeping with our goal to solve the longer term problem of capital preservation we have been working on two fronts. First, we are working with individual companies within our portfolio to help them gain access to capital that would allow them to operate during this crisis. I am pleased to report, that in two of our investments we have been successful and that I am confident that later in the year both of these companies will be successful in obtaining permanent financing that will bring liquidity back to our investment.

The second area is to restructure the Funds, or at least the Junior Subordinated debt, in order to have a plan that will provide investors with an eventual exit. The issues here are complex because of the need to preserve the rights of the Senior and Senior Subordinated Noteholders. We have engaged securities counsel to assist us with the restructuring, but they have not yet been willing to provide a legal opinion as to a particular course of action. One of the ideas that we are pursuing is that instead of a total restructuring that will carry the risk that the Senior Noteholders might find objectionable we will keep the structure intact, but offer Junior Subordinated Noteholders an opportunity to receive equity in other investments that will provide them an additional source of return for their investment in the FUNDS.

In addition to having the cash flow in the FUNDS recently reduced and therefore causing us to suspend the quarterly interest for the Junior Subordinated Noteholders, we have also been advised by counsel that distributions at this time quite probably reflect a return of capital and not interest, and therefore distributions might be considered an invasion of the principal due to the Senior and Senior Subordinated Noteholders. This is a result of not knowing how and where to price our investments in these very illiquid markets. We have also heard from several Junior Subordinated Noteholders that until market conditions become clearer, they would rather suspend their distributions which are taxable interest in order to preserve future distributions of return of capital which of course are not taxable.

We do expect to have a better picture by next quarter as to a specific plan of action available to us going forward and of course the hope that markets will at least stabilize and stop retreating. However, we repeat, we do not view this crisis to be easily settled or to exhaust itself anytime soon. There has been severe and long lasting damage to the U.S. and world financial markets that will require patience to work through.

As always, if there are any questions regarding your account or this memorandum, please contact your McGinn, Smith & Company representative.

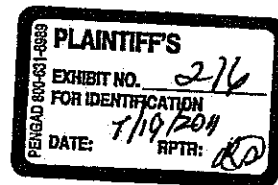
Sincerely,


David L. Smith
Managing Member
MS Advisors, LLC

DLS/gbg

MGS0011555

Exhibit C



First Independent Income Notes, LLC

99 Pine Street
Albany, NY 12207
Phone 518-449-5131
Fax 518-449-4894

October 13, 2008

RE [Redacted]

Re: \$5,000 First Independent Income Notes 7% due 12/15/08
Internal Investment # [Redacted]
Registration: [Redacted]

Dear Mr. & Mrs. [Redacted]

copy

This communication is being sent to investors of First Independent Income Notes, LLC (the FUND) in each of the three classes of Notes, Senior, Senior Subordinated, and Junior maturing on December 15, 2008. The purpose of the communication is to apprise you of the status of your investment and also inform you of the restructuring plan that has been presented to the FUND's Trustee, McGinn, Smith Capital Holdings Corp. by the FUND's managing member, McGinn, Smith Advisors, LLC.

McGinn, Smith Advisors, LLC (MSA) has determined that as a result of losses incurred in the FUND's investments and the total illiquidity for the vast majority of the FUND's investments it is not possible to redeem the Notes on the due date of December 15, 2008 and will require a restructuring of all classes of Notes. In restructuring the notes, MSA has taken into account the responsibility of the Trustee to address both the principal and interest payments due to the Senior noteholders and therefore must reschedule future interest and principal payments for all three classes of noteholders, giving priority to the Senior noteholders. Based on best estimates of current cash flow and present liquidity, MSA has developed a plan that alters scheduled interest and principal payments for all three classes. All three classes are having their maturities extended and their interest payments reduced. MSA has the responsibility to manage the FUND consistent with the provisions of the note's indenture and in a manner that best protects the assets of the FUND. Accordingly, MSA will be presenting a plan outlined later in this communication that in its sole judgment provides for an orderly liquidation of assets, payment of reasonably expected cash flows, and gives priority to the Senior Noteholders over the Senior Subordinated Noteholders and the Junior Noteholders. The plan takes into account that current conditions in financial credit markets presently offer

no liquidity for almost any financial instrument other than U.S. Treasury Notes and Bonds. The investments in the FUND are primarily non public securities that presently have no secondary market for resale and in fact do not have the ability to even establish a fair market value. The plan makes assumptions that cannot be relied upon with any certainty. Events in the US and world financial markets have been changing with a degree of volatility never before experienced at any time in history. The Credit market crisis that started approximately 18 months ago with the troubles in the sub prime mortgage market has accelerated to the point that threatens to impair the entire world's financial foundations and has spread from Wall Street to Main Street. Under these conditions, any planning has to be subject to changing events. We have assumed that markets will continue to be unstable and primarily illiquid for at least two years. The damage to the world's banking system and investment markets is very severe and in our judgment will dramatically change the nature of markets for years to come. While governments, worldwide are rushing to shore up the system with liquidity and taking steps to restore confidence the fact is that no one knows what the ultimate impact of their actions and the reaction of markets will be. What was initially a financial crisis is now a full blown worldwide economic crisis with unknown consequences. MSA is fully confident that financial markets will eventually stabilize and that investor confidence and liquidity will be restored. Anything less is just not acceptable, and therefore the allocation of resources, new efforts of governmental oversight and regulation, and cooperation on a global scale of financial markets is expected to ultimately resolve the present crisis. But the aforementioned intervention in markets will certainly change the way markets work and with any change comes the need for patience and time for investors to first understand and then accept those changes.

As I write this memo the US Stock Market has just finished the day with the Dow Jones Industrial average down over 500 points and down almost 900 points for the last two days. This of course is subsequent to the "rescue bill" or formally the "Emergency Economic Stabilization Act of 2008" signed into law last Friday after several weeks of Congressional wrangling. While in my opinion this was a necessary first step, the idea in some circles that its ultimate passage would bring instant cure to what was ailing the credit markets was ill founded. The stock market's decline is just a symptom of the credit crisis, and while I am in total sympathy for all of us suffering market losses, the real issue is the total lack of liquidity in the credit markets. This is the major issue that impacts your investment in the FUND. Lack of liquidity simply means that there are no efficient markets to buy and sell investments because investors have lost confidence that they can fairly judge what those investments are worth. As the events of the mortgage markets and eventually all fixed income markets played out over the last 18 months, investors repeatedly got burned on making a decision to invest. A sophisticated hedge fund investor made a \$1.8 billion investment last April in Washington Mutual, the country's largest saving bank, only to see it reduced to zero after being taken over by the FDIC last month. National political leaders assured us this summer that Fannie Mae and Freddie Mac, our two leading GSE (Government Sponsored Enterprises) mortgage lenders, were financially sound only to be declared bankrupt and taken over by the FDIC in mid September. Three of the five largest investment banks, Bear Stearns, Merrill Lynch, and Lehman Brothers no longer exist. AIG, the world's largest insurance

company required an \$85 billion cash infusion and equity investors were wiped out. Hundreds of banks and mortgage companies have been closed including the forced sales of Wachovia to Wells Fargo and Citi Corp. Virtually all financial institutions have had to either cut or eliminate dividends in order to strengthen their balance sheets. Other evidence of the cessation of liquidity in the credit markets include:

- 1.) billion dollar hedge funds such as D.B. Zwirn and Pardus Capital Management refused to allow investors to redeem because they were unable to sell assets to raise cash
- 2.) last week \$120 billion of commercial paper not marketable, causing companies to lose liquidity for normal operating functions like payroll
- 3.) despite a lowering of interest rates, banks refusing to lend overnight to other banks from fear of not knowing the financial soundness of the borrower
- 4.) Reserve Money Market Fund assets fall below the one dollar redemption price and overnight withdrawal of \$40 billion of the \$60 billion in assets forces the fund to cease redemptions
- 5.) The College Fund, who manages assets for 1500 college endowments and their operating funds restrict access to their money market fund to 38% of their deposits and state that 100% of your capital won't be available until 2010

There are hundreds of other examples that have occurred and demonstrate the liquidity crisis. Most of you are aware of this because the media has been giving this story full attention for months. The reason that it is important for you to be aware of the freezing of the credit markets is because it impacts the investments in the FUND in a variety of ways. First, if the most liquid and strongest investment assets such as money market funds, commercial paper, and mortgages are having difficulty in finding buyers, than the ability for almost all other assets to have liquidity is impossible. Second, if forced to sell these assets in order to redeem the notes, the market price would be far below fair market value. As an example, Merrill Lynch in July, in an effort to get some of these assets off their balance sheet and receive cash, sold \$30 billion worth for just 22 cents on the dollar. And even then, the buyer forced Merrill Lynch to finance 75% of the purchase with a non-recourse loan which meant the true cost of the purchase was just 6 cents on the dollar. Third, many of the assets, including loans of the companies in our portfolio, were dependent on subsequent financing in order to repay us. Often, our loans were bridge loans to companies until they could get permanent financing through stock or bond offerings. The initial public offerings (IPO's) hit a 5 year low in July and included only some of the most visible companies in the world such as Visa International. Of the 25 billion dollars in offerings through July, Visa accounted for 18 billion dollars, leaving just 6 billion dollars for the other 23 companies taken public. Thus, the companies in our portfolio have been totally shut out, and in several instances the capital raises included money to satisfy their debts to us or to provide us with liquidity for our investments. When these offerings will once again be available is not determinable, but it is not likely to be anytime soon.

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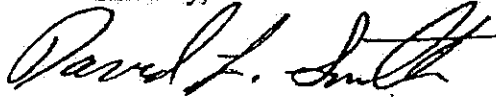
So what is next for what former Chairman of the Federal Reserve, Alan Greenspan, has identified as the once in a century financial crisis? First, the Federal Government continues to be active through all of its agencies. As mentioned earlier, Congress recently passed a bill that is to provide \$700 billion dollars to help purchase some of these distressed assets and restore liquidity to the banks so that they can begin to make the loans and provide the credit that allows our economy to begin to function normally. The SEC has decreed that short selling in financial stocks is no longer permitted until further notice. The FDIC has instituted an insurance program for money market funds. They have raised FDIC insurance on bank deposits from \$100,000 per account to \$250,000. This week they have opened the discount window, normally reserved only for banks, to allow for the purchase of commercial paper. Those actions are designed to both restore a semblance of confidence and provide sufficient liquidity for the most critical markets of our economy. However, time is what ultimately is required for banks and financial institutions to deleverage their balance sheets and restore sufficient liquidity that will allow them to once again start lending to businesses and consumers. J.P. Morgan, one of our leading financial institutions, believes that credit losses will eventually exceed 4 trillion dollars and that the housing price decline will bottom out down 30% from 2006 levels and last until 2010.

MSA has tried to evaluate and model the impact of the current crisis on its own investments and put forth a plan that provides for all classes of note holders to first get their principal back and second provide them with some return on their investment in the interim. We have communicated with some of you earlier in the year indicating that MS was working on a plan to meet those objectives, mindful of the Senior notes and the subordination issues of the other two classes. Anything that we would have proposed earlier this year certainly would have already proven to be too optimistic. Thus, our current plan we believe to be very achievable, and we are hopeful that as markets and liquidity are restored to a more normal operational mode, we in fact may be able to accelerate the repayment. However, we must emphasize that we are in uncharted waters and what we have learned from the last 18 months is to expect the unexpected.

The plan calls for immediate implementation on the next interest payment due date. We have taken great care, and with consultation with our attorneys, to present a plan that we believe to be fair, protect all classes, and still give priority to the rule of seniority. We understand that many of you have personal liquidity issues due to retirement or other financial needs and this plan may put a personal hardship on you. MSA and its affiliate McGinn, Smith & Co. will be making its own sacrifice. Management fees, commissions, and administrative fees aggregate approximately \$2,750,000 per year for all of our FUNDS that are part of this reorganization. In an effort to improve liquidity we have agreed to forfeit all such future fees while this reorganization plan is in effect. Legal fees attributed to defense of our actions and fees incurred in the pursuit of recovering any of our investments will be the responsibility of the FUNDS. The plan will be implemented for the benefit of all investors. Obviously, to be fair and acceptable to all investors, we cannot entertain a different approach for individual investors. If circumstances change in the future, hopefully for the better, we reserve the right to restructure and implement a new plan.

In conclusion, we thank you in advance for your patience and understanding of the very difficult position that we are in. If there are any questions regarding your accounts or this memorandum, please contact your McGinn, Smith & Company representative.

Sincerely,



David L. Smith
Managing Partner
McGinn, Smith Advisors

DLS/gg

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The attached is the restructuring plan for First Independent Income Notes, LLC (FIIN) for the Senior, Senior Subordinated, and Junior Noteholders. This Schedule makes no attempt to configure the benefit of asset sales beyond approximately 8% per year of the capital base for the first 6 years due to the manager's inability to predict the timing and price received for asset sales. While we believe that the market environment will remain difficult for the first 2-3 years for asset sales, we remain optimistic that the market should improve subsequent to that period. Fifty percent of the proceeds of those sales will be a return of principal to the Senior noteholders until they are paid in full. Subsequently, the same 50% of asset sales will be returned as principal to the Senior Subordinated noteholders. When both Senior and Senior Subordinated noteholders are paid out in full, distribution of future sales to the Junior noteholders will be at the discretion of MSA, deemed to be consistent with successfully being able to return full principal to those Junior noteholders.

COPY

The attached is the restructuring plan for First Independent Income Notes, LLC (FIIN) for the Senior, Senior Subordinated, and Junior Noteholders. This Schedule makes no attempt to configure the benefit of asset sales beyond approximately 8% per year of the capital base for the first 6 years due to the manager's inability to predict the timing and price received for asset sales. While we believe that the market environment will remain difficult for the first 2-3 years for asset sales, we remain optimistic that the market should improve subsequent to that period. Fifty percent of the proceeds of those sales will be a return of principal to the Senior noteholders until they are paid in full. Subsequently, the same 50% of asset sales will be returned as principal to the Senior Subordinated noteholders. When both Senior and Senior Subordinated noteholders are paid out in full, distribution of future sales to the Junior noteholders will be at the discretion of MSA, deemed to be consistent with successfully being able to return full principal to those Junior noteholders.

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**First Independent Income Notes, LLC
Restructuring Plan of October 2008**

I. Senior Notes 7%, due December 15, 2008

Payments: October 15th
January 15th
April 15th
July 15th

1. Starting October 15, 2008 through July 15, 2009
Annual rate of 5%, interest only
2. Starting October 15, 2009 through October 15, 2014
Annual rate of 5%
10 year amortization
3. Maturity – October 15, 2014

Example of \$100,000 note:

1st year: 5% interest
4 quarterly payments of \$1,250

2nd – 6th year - 5% interest, 10 year amortization
20 quarterly payments of \$3,192.14

Maturity payment - \$56,179.51

Note: 50% of all liquidated investment proceeds will be applied immediately to principal.

II. Senior Subordinated Notes 7.5%, due December 15, 2008

Payments: October 15th
January 15th
April 15th
July 15th

COA

1. 1st payment October 15, 2010 through July 15, 2013
Annual rate of 3%,
10 year amortization
2. Starting October 15, 2013 through July 15, 2020
Annual rate of 6%
7 year amortization

Final payment July 15, 2020

Example of \$100,000 note:

Year 1-2	no payments
Year 3-5	3% interest, 10 year amortization 12 quarterly payments of \$2,903.02
Year 6-12	6% interest, 7 years amortization 28 quarterly payments of \$3,215.20

Note: Starting in year 7, 50% of all liquidated investment proceeds will be applied immediately to principal.

III. Junior Subordinated Notes 10.25%, due December 15, 2008

Payments: October 15th
January 15th
April 15th
July 15th

1. 1st payment October 15, 2010 through July 15, 2014
5% principal only
2. Starting October 15, 2014 through July 15, 2023
Annual rate of 5%,
15 year amortization
3. Maturity July 15, 2003

Example of \$100,000 note:

Year 1-2	no payments
Year 3-6	5% principal only 16 quarterly payments of \$1,250
Year 7-15	5% cpn, 15 year amortization 36 payments of \$1,903.19

Maturity payment - \$39,251.93

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Exhibit D

Exhibit D
Supporting Evidence

Payment Date	Payment Amount	Supporting Evidence	Exhibit No.
2/4/2008	\$24,281.25	Wire Transfer Confirmation Reference 08020414422639DB for wire transfer from Mercantile Bank to Once City Center Associates	D(1)
2/4/2008	\$9,187.50	Wire Transfer Confirmation Reference 08020414475639DB for wire transfer from Mercantile Bank to Once City Center Associates	D(2)
2/4/2008	\$866.25	Wire Transfer Confirmation Reference 08020414452639DB for wire transfer from Mercantile Bank to Once City Center Associates	D(3)
4/18/2008	\$69,187.50	Cashier's Check No. 602896 issued by Mercantile Bank to One City Center Associates	D(4)
5/1/2008	\$17,937.50	Cashier's Check No. 602980 issued by Mercantile Bank to One City Center Associates	D(5)
7/31/2008	\$17,937.50	Cashier's Check No. 617268 issued by Mercantile Bank to One City Center Associates	D(6)
10/21/2008	\$49,097.50	Cashier's Check No. 635544 issued by Mercantile Bank to One City Center Associates	D(7)
10/30/2008	\$17,937.50	Cashier's Check No. 635577 issued by Mercantile Bank to One City Center Associates	D(8)
TOTAL	\$206,432.50		

Exhibit D-1

WireHouse - Message Details

MID: 08020414422639DB

Beneficiary: ONE CITY CENTER ASSOCIATES LLC
Originator: MCGINN SMITH FUNDING LLC

Message Text:

User ID:: DCB81139
Message St: COMPLETE
Value Date: 02/04/2008
Date:: 02/04/2008
Time:: 14:51:38
URC::
Test Key::
Branch Cod: 06880
Fee:: 20.00
Pin::
ExtRef::
Skpclbck: N
Tkprf::
Trancode::
SkipHost: N
AUTO FX: N
REU ID:: 06880

Sender ABA: 063113772
Sender Nam: MERCANTILE BANK
Receiver A: 011200608
Receiver N: KEY BANK MAINE
Message Ty: 10
Message Su: 00
Product Co: CTR
Amount:: 24281.25
Reference:: 08020414422639DB
ORG Idcode: AC
ORG Id: 7600601635
ORG: MCGINN SMITH FUNDING LLC
ORG Adres: 99 PINE ST
ORG Adres: ALBANY,NY 12207-
ORG Adres:
OGB Idcode:
OGB Id:
OGB: MERCANTILE BANK
OGB Adres:
OGB Adres:
OGB Adres:
INS Idcode:
INS Id:
INS:
INS Adres:
INS Adres:
INS_Adr2:
IBK Idcode:
IBK Id:
IBK:
IBK Adres:
IBK Adres:
IBK Adres:

Printed By: RHONDA BOATWRIGH THE SOUTH FINANCIAL GROUP

Date: March 9, 2010 10:57:24 AM

893239

MERC 001657

WireHouse - Message Details

MID: 08020414422639DB

BBK Idcode:
BBK Id:
BBK:
BBK Address:
BBK Address:
BBK Address:
BNF Idcode: AC
BNF Id: 700810211
BNF: ONE CITY CENTER ASSOCIATES LLC
BNF Address: 99 PINE ST
BNF Address: ALBANY NY 12207
BNF Address:
RFB:
OBI:
BBI: {6500}FIRST INDEPENDENT INCOME NOTES*
As of reas:
As of date:
Reference:
IMAD: 20080204F3B7491C000098
OMAD: 20080204D1B74P1C00015802041451FT01
Charges:
Free text1:
Free text2:
Corcode:
Corid:
Cor:
CorAddr:
CorAddr:
CorAddr:

Printed By: RHONDA BOATWRIGH THE SOUTH FINANCIAL GROUP

Date: March 9, 2010 10:57:24 AM

893240

MERC 001658

Exhibit D-2

WireHouse - Message Details

MID: 08020414475639DB

Beneficiary: ONE CITY CENTER ASSOCIATES LLC
Originator: MCGINN SMITH FUNDING LLC

Message Text:

User ID:: DCB81139
Message St: COMPLETE
Value Date: 02/04/2008
Date:: 02/04/2008
Time:: 14:59:48
URC::
Test Key::
Branch Cod: 06880
Fee:: 20.00
Pin::
ExtRef::
Skpcllbck:: N
Tkprf::
Trancode::
SkipHost: N
AUTO FX:: N
REU ID:: 06880

Sender ABA: 063113772
Sender Nam: MERCANTILE BANK
Receiver A: 011200608
Receiver N: KEY BANK MAINE
Message Ty: 10
Message Su: 00
Product Co: CTR
Amount:: 9187.50
Reference:: 08020414475639DB
ORG Idcode: AC
ORG Id:: 7600601635
ORG:: MCGINN SMITH FUNDING LLC
ORG Adres: 99 PINE ST
ORG Adres: ALBANY,NY 12207-
ORG Adres:
OGB Idcode:
OGB Id:
OGB:: MERCANTILE BANK
OGB Adres:
OGB Adres:
OGB Adres:
INS Idcode:
INS Id:
INS:
INS Adres:
INS Adres:
INS_Adr2:
IBK Idcode:
IBK Id:
IBK:
IBK Adres:
IBK Adres:
IBK Adres:

Printed By: RHONDA BOATWRIGHT THE SOUTH FINANCIAL GROUP

Date: March 9, 2010 10:57:09 AM

893235

MERC 001653

WireHouse - Message Details

MID: 08020414475639DB

BBK Idcode:
BBK Id::
BBK::
BBK Address:
BBK Address:
BBK Address:
BNF Idcode: AC
BNF Id:: 700810211
BNF:: ONE CITY CENTER ASSOCIATES LLC
BNF Address: 99 PINE ST
BNF Address: ALBANY NY 12207
BNF Address:
RFB::
OBI::
BBI:: {6500}FIRST EXCELSIOR INCOME NOTES*
As of reas:
As of date:
Reference:
IMAD:: 20080204F3B7491C000104
OMAD:: 20080204D1B74P1C00016902041502FT01
Charges::
Free text1:
Free text2:
Corcode::
Corid:
Cor::
CorAddr::
CorAddr::
CorAddr::

Printed By: RHONDA BOATWRIGHT THE SOUTH FINANCIAL GROUP Date: March 9, 2010 10:57:09 AM

893236

MERC 001654

Exhibit D-3

WireHouse - Message Details

MID: 08020414452639DB

Beneficiary: ONE CITY CENTER ASSOCIATES LLC
Originator: MCGINN SMITH FUNDING LLC

Message Text:

User ID:: DCB81139
Message St: COMPLETE
Value Date: 02/04/2008
Date:: 02/04/2008
Time:: 14:53:07
URC::
Test Key::
Branch Cod: 06880
Fee:: 20.00
Pin::
ExtRef::
Skpcllback:: N
Tkprf::
Trancode::
SkipHost:: N
AUTO FX:: N
REU ID:: 06880

Sender ABA: 063113772
Sender Nam: MERCANTILE BANK
Receiver A: 011200608
Receiver N: KEY BANK MAINE
Message Ty: 10
Message Su: 00
Product Co: CTR
Amount:: 866.25
Reference:: 08020414452639DB
ORG Idcode: AC
ORG Id: 7600601635
ORG:: MCGINN SMITH FUNDING LLC
ORG Address: 99 PINE ST
ORG Address: ALBANY,NY 12207-
ORG Address:
OGB Idcode:
OGB Id:
OGB:: MERCANTILE BANK
OGB Address:
OGB Address:
OGB Address:
INS Idcode:
INS Id:
INS:
INS Address:
INS Address:
INS_Addr2:
IBK Idcode:
IBK Id:
IBK:
IBK Address:
IBK Address:
IBK Address:

Printed By: RHONDA BOATWRIGHT THE SOUTH FINANCIAL GROUP

Date: March 9, 2010 10:56:39 AM

893229

MERC 001647

WireHouse - Message Details

MID: 08020414452639DB

BBK Idcode:
BBK Id::
BBK::
BBK Address:
BBK Address:
BBK Address:
BNF Idcode: AC
BNF Id:: 700810211
BNF:: ONE CITY CENTER ASSOCIATES LLC
BNF Address: 99 PINE ST
BNF Address: ALBANY NY 12207
BNF Address:
RFB::
OBI::
BBI:: {6500}THIRD ALBANY INCOME NOTES*
As of reas:
As of date:
Reference:
IMAD:: 20080204F3B7491C000100
OMAD:: 20080204D1B74P1C00016102041453FT01
Charges::
Free text1:
Free text2:
Corcode::
Corid:
Cor::
CorAddr::
CorAddr::
CorAddr::

Printed By: RHONDA BOATWRIGH THE SOUTH FINANCIAL GROUP

Date: March 9, 2010 10:56:39 AM

893230

Exhibit D-4

MISCELLANEOUS DEBIT

ACCOUNT NAME: *M.C. Smith* DATE: *4/18/08*

RECEIPT NUMBER: *4111*

ACCOUNT NUMBER: *7600601635* TRAN CODE: *74* AMOUNT: *\$ 121308.75*

DESCRIPTION: *Per Check Request*

ca 12125 & 12126

19-12-50 to Div City Center Assoc

00634137724 74

Date 04-18-2008 Account 7600601635 Serial 0 Amount 121308.75
 TR 6311377 Sequence 40171890 BankNum 6 TranCode 74
 DbCr D

MERCANTILE BANK OF INDIA 602895

REMITTER: *MCCAN SMITH FUNDING*

PAY TO THE ORDER OF: *NATIONAL FINANCIAL SERVICES* APR 17 20 08

AMOUNT: *\$ 52,121.25*

Fifty Two Thousand One Hundred Twenty One Dollars and Twenty Five Cents

CASHIER'S CHECK

⑆602895⑆ 00631137724 05000017⑆ 10

Date 04-18-2008 Account 5000017 Serial 602895
 Amount 52121.25 TR 6311377 Sequence 40171870 BankNum 6
 TranCode 10 DbCr C

MERCANTILE BANK OF INDIA 602896

REMITTER: *MCCAN SMITH FUNDING*

PAY TO THE ORDER OF: *THE CITY CENTER ASSOCIATION* APR 17 20 08

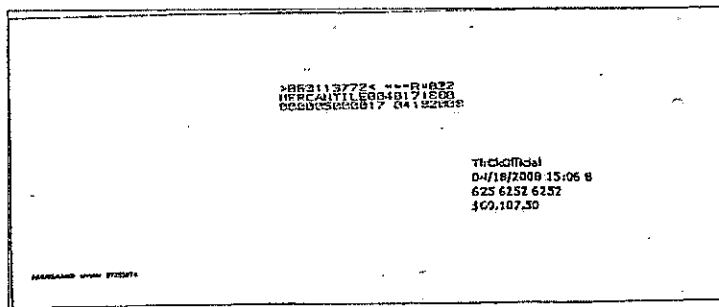
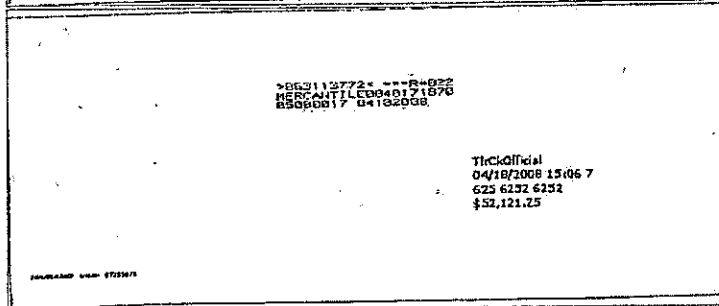
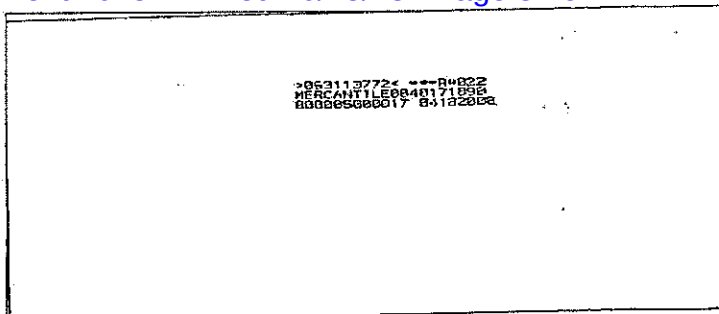
AMOUNT: *\$ 69,187.50*

Sixty Nine Thousand One Hundred Eighty Seven Dollars and Fifty Cents

CASHIER'S CHECK

⑆602895⑆ 00631137724 05000017⑆ 10

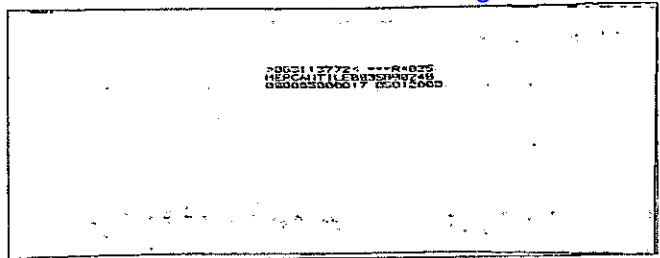
Date 04-18-2008 Account 5000017 Serial 602896
 Amount 69187.50 TR 6311377 Sequence 40171880 BankNum 6
 TranCode 10 DbCr C



893316

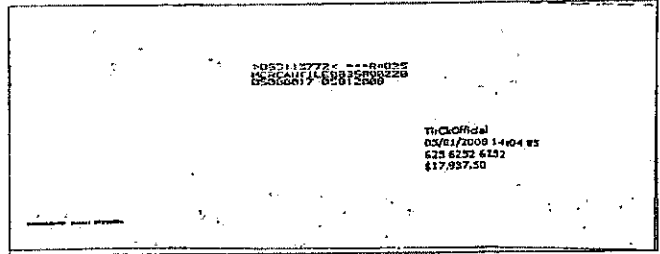
Exhibit D-5

MISCELLANEOUS DEBIT
 MERCANTILE BANK INITIALS Q10 DATE 5/1/08
 ACCOUNT NAME McGinn Smith Funding Llc APP BY _____
 DESCRIPTION / REMARKS _____ AMOUNT _____
 ACCOUNT NUMBER 2600601635 74 3190313
 ⑆053113772⑆



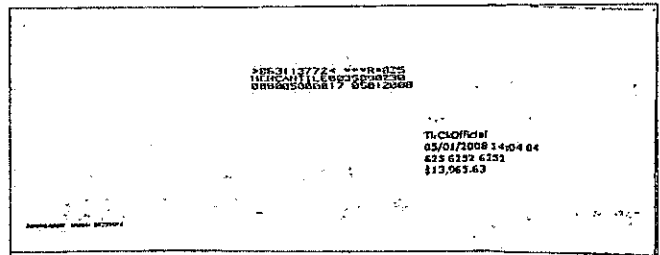
Date 05-01-2008 Account 7600601635 Serial 0 Amount 31903.13
 TR 6311377 Sequence 35890240 BankNum 6 TranCode 74

MERCANTILE BANK 602980
 REMITTER McGINN SMITH FUNDING LLC
 BOCA RATON FL 33433
 May 1 20 08
 PAY TO THE ORDER OF "ONE CITY EMIER ASSOCIATES" \$ 17,937.50
 Seventeen Thousand Nine Hundred Thirty Seven Dollars and Fifty Cents
 DOLLARS
 CASHIER'S CHECK
 ⑆602980⑆ ⑆053113772⑆ ⑆05000017⑆ 10



Date 05-01-2008 Account 5000017 Serial 602980
 Amount 17937.50 TR 6311377 Sequence 35890220 BankNum 6

MERCANTILE BANK 602979
 REMITTER McGINN SMITH FUNDING LLC
 BOCA RATON FL 33433
 May 1 20 08
 PAY TO THE ORDER OF "NATIONAL FINANCIAL SERVICES" \$ 13,965.63
 Thirteen Thousand Nine Hundred Fifty Five Dollars and Sixty Three Cents
 DOLLARS
 CASHIER'S CHECK
 ⑆602979⑆ ⑆053113772⑆ ⑆05000017⑆ 10



Date 05-01-2008 Account 5000017 Serial 602979
 Amount 13965.63 TR 6311377 Sequence 35890230 BankNum 6
 TranCode 10 DbCr C

893350

Exhibit D-6

MISCELLANEOUS DEBIT

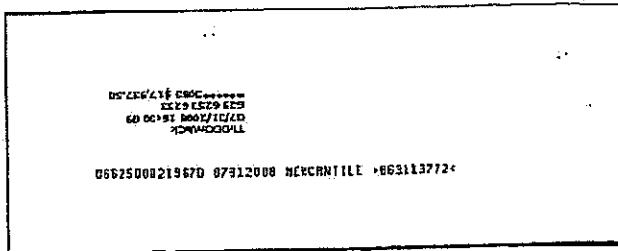
MERCANTILE BANK OF INDIANA DATE 7/31/08

ACCOUNT NAME Nelson Smith Transac Funding APP# 10

DESCRIPTION / REMARKS	AMOUNT
<u>Bank check payable to Home City Center Associates</u>	<u>17,937.50</u>

ACCOUNT NUMBER 7600643083 74 17937.50

00631137724 74



Date 07-31-2008 Account 7600643083 Serial 0 Amount 17937.50
 TR 6311377 Sequence 311391530 BankNum 6 TranCode 74

MERCANTILE BANK OF INDIANA 617268

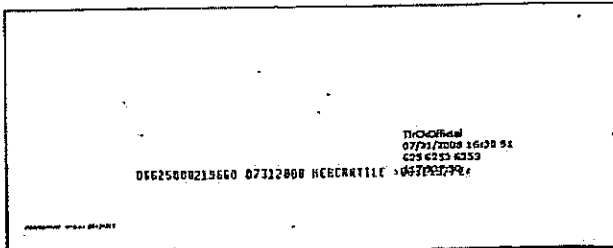
REMITTER: NELSON SMITH TRANSACTION FUNDING
804 BRIDGE TOWER CO

PAY TO THE ORDER OF: HOME CITY CENTER ASSOCIATES July 31, 2008 \$ 17,937.50

Amount in Words: Seventeen Thousand Nine Hundred Thirty Seven Dollars and Fifty Cents DOLLARS

CASHIER'S CHECK

617268 00631137724 05000017* 10



Date 07-31-2008 Account 5000017 Serial 617268
 Amount 17937.50 TR 6311377 Sequence 311391520 BankNum 6
 TranCode 10 DbCr C

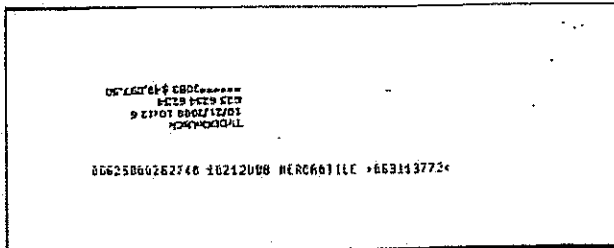
893569

MERC 001989

Exhibit D-7

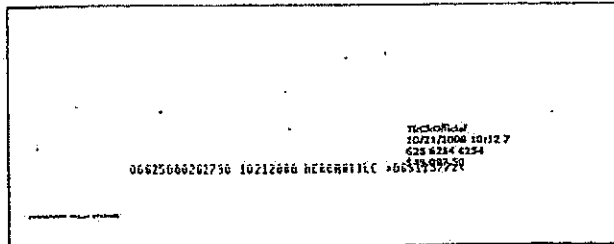
MISCELLANEOUS DEBIT
 MERCANTILE BANK OF INDIA
 DATE 10/21/08
 ACCOUNT NAME McGinn Smith Trans APP BY _____
 DESCRIPTION / REMARKS AMOUNT
ck for One City
Center Assoc.
 ACCOUNT NUMBER
7600643083 74 4909750
 6031137720 74

Date 10-21-2008 Account 7600643083 Serial 0 Amount 49097.50
 TR 6311377 Sequence 314522090 BankNum 6 TranCode 74



MERCANTILE BANK OF INDIA 635544
 REMITTER McGINN SMITH & COMPANY SOCIAL MANAGERS
 PAY TO THE ORDER OF "ONE CITY CENTER ASSOCIATES" October 21 20 08
\$ 49,097.50
 Dollars
 Forty Nine Thousand Ninety Seven Dollars and Fifty Cents
 CASHIER'S CHECK
 635544 6031137720 05000017 10

Date 10-21-2008 Account 5000017 Serial 635544
 Amount 49097.50 TR 6311377 Sequence 314522080 BankNum 6
 TranCode 10 DbCr C



893670

MERC 002090

Exhibit D-8

MERCANTILE BANK 635577

REMITTER: MCDONN SMITH TRANK
DOCA MARINE/JO

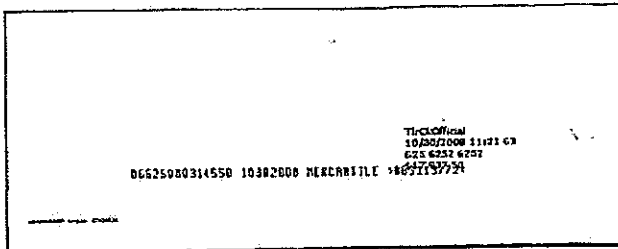
PAY TO: "ONE CITY CENTER ASSOC."
THE ORDER OF: 17,937.50

October 30 2008

See amount. Thousand Nine Hundred and Thirty Seven Dollars and Fifty Cents

CASHIER'S CHECK

*635577# RDE3113772# 05080819# 10



Date 10-30-2008 Account 5000017 Serial 635577
Amount 17937.50 TR 6311377 Sequence 314887780 BankNum 6

MISCELLANEOUS DEBIT

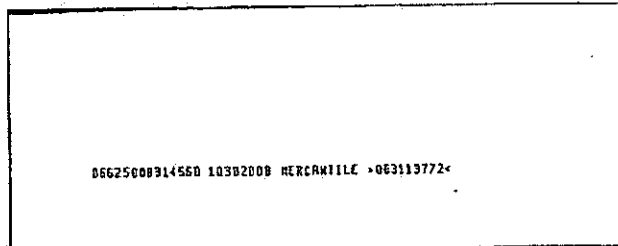
INITIALS go DATE 10/30/08

ACCOUNT NAME McKin Smith Assoc. EFF DATE _____ APP BY _____

DESCRIPTION / REMARKS
One City Center Assoc.

ACCOUNT NUMBER	TRAN CODE	AMOUNT
<u>7600643083</u>	<u>74</u>	<u>\$ 17937.50</u>

06625080314550 10382008 MERCANTILE *063113772#



Date 10-30-2008 Account 7600643083 Serial 0 Amount 17937.50
TR 6311377 Sequence 314887790 BankNum 6 TranCode 74
DbCr D

893677

Exhibit E

Exhibit E

INVEST REGISTRATION	INVEST PRD ID	PRD DESC	PRD DESC2	TOTPAID	TICKETED AMOUNT	FIRST PAYMENT	LAST PAYMENT	INVEST STATUS	ACCOUNT#	INVEST_ORIG	INVEST_CIT ID FROM
ONE CITY CENTER ASSOCIATES	TAIN 10.25%	THIRD ALBANY INCOME NOTES	SECURED JUNIOR NOTES DUE 12/15/2009	384000	450000	06-Dec-04	08-Jan-09	TRANSFERRED	ONECITY	NEWL	
BURTON FISHER	TAIN 10.25%	THIRD ALBANY INCOME NOTES	SECURED JUNIOR NOTES DUE 12/15/2009	66000	66000	08-Jan-09	08-Jan-09	OPEN	MSA015580	TRANSFER	ONECITY

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF NEW YORK

-----X
SECURITIES AND EXCHANGE COMMISSION

Plaintiff,

vs.

Case No. 1:10-CV-457
(GLS/CFH)

McGINN, SMITH & CO., INC.,
McGINN, SMITH ADVISORS, LLC
McGINN, SMITH CAPITAL HOLDINGS CORP.,
FIRST ADVISORY INCOME NOTES, LLC,
FIRST EXCELSIOR INCOME NOTES, LLC,
FIRST INDEPENDENT INCOME NOTES, LLC,
THIRD ALBANY INCOME NOTES, LLC,
TIMOTHY M. MCGINN, AND
DAVID L. SMITH, GEOFFREY R. SMITH,
Individually and as Trustee of the David L. and
Lynn A. Smith Irrevocable Trust U/A 8/04/04,
LAUREN T. SMITH, and NANCY MCGINN,

Defendants,

LYNN A. SMITH and
NANCY MCGINN,

Relief Defendants. and

GEOFFREY R. SMITH, Trustee of the
David L. and Lynn A. Smith Irrevocable
Trust U/A 8/04/04,

Intervenor.

-----X

**MEMORANDUM OF LAW IN SUPPORT OF
FIFTH CLAIMS MOTION OF WILLIAM J. BROWN, AS RECEIVER, FOR
AN ORDER APPLYING PREFERENTIAL PAYMENT OFFSET TO
CERTAIN PREFERRED INVESTOR CLAIMS**

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<i>U.S. Commodity Futures Trading Comm’n v. Lake Shore Asset Mgmt. Ltd.</i> , No. 07 C 3598, 2010 WL 960362 (N.D. Ill. Mar. 15, 2010)	11
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William J. Brown, as Receiver (“Receiver”) of McGinn, Smith & Co., Inc., et al. (“MS & Co.”), respectfully submits this Memorandum of Law in support of his Fifth Claims Motion (“Motion”) for an Order applying the Preferential Payment Offset to certain Preferred Investor Claims (as defined below) held by One City Center Associates (“OCC”) and Burton Fisher (“Fisher”) as set forth on Exhibits A and B to the Motion.

PRELIMINARY STATEMENT

From 2003 to 2010, David L. Smith and Timothy M. McGinn orchestrated an elaborate Ponzi scheme through which more than 900 investors were defrauded. In late 2007, when the Four Funds were revealed to have a massive deficit, Smith and McGinn decided to first reduce, and then eliminate entirely, the interest payments owed to investors in the Four Funds Notes. Notwithstanding that most investors ceased receiving the interest payments that they were entitled to, the Receiver’s due diligence discovered that a certain subset of preferred investors continued to receive full payments of interest on their Four Funds investments. Specifically, investor OCC received supplemental payments commencing in February 2008 which it was not entitled to receive. For no legitimate reason, McGinn and Smith elevated OCC to a “preferred” status and provided it with supplemental, “lulling” payments. It would be inequitable to permit OCC to retain these Preferential Payments. Accordingly, the Receiver proposes to reduce the distributions on account of OCC’s Four Funds investments by the amount of Preferential Payments received on a dollar-for-dollar basis. Such a reduction would return OCC to the position it would have otherwise occupied had it been treated like the majority of investors that McGinn and Smith defrauded.

STATEMENT OF FACTS

MS & Co. was a broker-dealer registered with the Securities and Exchange Commission (“SEC”) with its headquarters in Albany, New York from 1981 to 2009. From 2003 through 2010, the broker-dealer was owned by David L. Smith (“Smith”), Timothy M. McGinn (“McGinn”), and Thomas E. Livingston. Brown Dec’1 ¶ 3.¹

On April 20, 2010, the SEC filed a Complaint initiating the above-captioned action (Docket No. 1). Also, on April 20, 2010, this Court granted a Temporary Restraining Order (Docket No. 5), which, among other things, froze certain assets of the above-captioned Defendants and Relief Defendants, and appointed the Receiver as temporary receiver with respect to numerous entities controlled or owned by Defendants McGinn and Smith, including those listed on Exhibit A to the Preliminary Injunction Order entered in this action (Docket No. 96) (collectively, the “MS Entities”). Brown Dec’1. ¶4.

On July 26, 2010, following a hearing, the Court entered an order granting the SEC’s Motion for a Preliminary Injunction and appointing the Receiver as receiver, pending a final disposition of the action (“Preliminary Injunction Order”) (Docket No. 96).

On August 3, 2010, the SEC filed an Amended Complaint (Docket No. 100). On June 8, 2011, the SEC filed a Second Amended Complaint (the “Complaint”) (Docket No. 334). On February 17, 2015, the Court issued its Memorandum-Decision and Order (Docket No. 807) (“MDO”) granting the SEC’s motion for summary judgment. The Court entered judgments in favor of the SEC in 2016 (Docket Nos. 835, 836, 837).

Generally, McGinn and Smith “orchestrated an elaborate Ponzi scheme, which spanned over several years, involved dozens of debt offerings, and bamboozled

¹ “Brown Dec’1. ¶ __” refers to the Declaration of William J. Brown dated October 15, 2018 filed in support of the Motion.

hundreds of investors out of millions of dollars.” MDO at 7. McGinn and Smith raised over \$136 million between 2003 and 2010 in over twenty unregistered debt offerings, including the Four Funds -- FAIN, FEIN, FIIN, and TAIN -- and various Trust Offerings, by representing that investor money would be “invested,” when instead it was “funneled” into various entities owned or controlled by McGinn and Smith. That money was then used to fund unauthorized investments and unsecured loans, make interest payments to investors in other entities and offerings, support McGinn’s and Smith’s “lifestyles,” and cover the payroll at MS & Co. MDO at 7.

A. The Four Funds

The Four Funds—FAIN, TAIN, FIIN, and FEIN— were single-purpose, New York limited liability companies formed between September 2003 and October 2005. The private placement memoranda (“PPMs”) for each of the Four Funds were substantively identical, and each offered \$20 million worth of Notes, with the exception of TAIN, which offered \$30 million. The offerings had three tranches of Notes, which paid quarterly interest of 5% to 10.25%, and promised a return of principal at maturity in one, three or five years. MDO at 10.

McGinn and Smith engaged in a course of conduct and dealings that were contrary to the PPMs issued for the Four Funds. First, investor proceeds from the Four Funds were used to purchase contracts from pre-2003 trusts for the purpose of redeeming or making interest payments to investors. Second, the Four Funds used investor money to directly invest in, rather than purchase investments from, affiliates. Many of the affiliated investments provided no cash flow to the Four Funds and were ultimately considered worthless. Finally, proceeds from the Four Funds were funneled through McGinn Smith

Transaction Funding Corporation (“MSTF”) and then used to pay MS & Co.’s payroll. MDO at 11-12.

In late 2007, David Smith received an e-mail from David Rees, MS & Co.’s comptroller, which showed a \$48.8 million deficit in the Four Funds. Notwithstanding that deficit, Smith continued to solicit new investments in the Four Funds. MDO at 12. In January 2008, Smith sent a letter to investors in the Four Funds notifying investors that interest payments on the junior tranches of Notes were being reduced to from 10.25% to 5%. *See Exhibit A to Brown Dec’1; see also MDO at 12.* By April 2008, interest payments on the junior tranches of Notes were eliminated entirely. *See Exhibit B to Brown Dec’1; see also MDO at 12.* The reduction, and subsequent elimination, of interest payments were attributed by McGinn and Smith to the collapse of various debt and credit markets and the “sub prime mess.” In October 2008, David Smith sent a letter to all Note holders in the Four Funds outlining a restructuring plan which extended the maturity dates of the Notes, reduced interest payments for all tranches, and forfeited all future fees due to MS & Co. *See Exhibit C to Brown Dec’1; see also MDO at 12-13.*

B. Preferential Payments to OCC

Most investors in the junior tranches of the Four Funds Notes received reduced interest payments starting in January 2008 and stopped receiving interest payments altogether by April 2008. OCC, however, continued to receive interest payments on its junior Four Funds Notes (“Preferential Payments”) in excess of what other investors were receiving. In February, 2008, OCC received the same reduced 5% interest payment that other investors received, and, in addition, Preferential Payments making up the difference

between the 5% interest payment and the full 10.25% interest payments that all investors were supposed to receive. Brown Dec'1 ¶ 11.

The Receiver has recovered wire transfer confirmations dated February 4, 2008, showing Preferential Payments made to OCC in the aggregate amount of \$34,355.00 on account of OCC's investments at the time in FIIN, FEIN, and TAIN Notes, representing the "gap" 5.25% interest that other investors did not receive in February 2008. *See* Brown Dec'1, Exhibits D(1) - D(3). These Preferential Payments came from MSF funds, and were not proceeds of the Four Funds. Brown Dec'1 ¶ 12.

Certain of OCC's Four Funds investments were transferred to Fisher after OCC has received the Preferential Payments. An excerpt from the original investment register for the TAIN 10.25% Secured Junior Notes ("Investment Register") is attached to the Brown Declaration as Exhibit E. The Investment Register was an excel spreadsheet maintained internally at MS & Co. to track investments. The Investment Register has been edited to remove certain extraneous information. The Investment Register shows that on January 8, 2009, the TAIN investment held by OCC was transferred to Burton Fisher. Brown Dec'1 ¶ 13.

In addition to the Preferential Payments that OCC received in February 2008, OCC also received a series of supplemental payments through 2008 that other investors did not receive ("Unspecified Preferential Payments"). From April 2008 through to October 2008, OCC received five Unspecified Preferential Payments aggregating \$172,097.50. Brown Dec'1 ¶ 14. The Receiver has recovered copies of cashier's checks issued by Mercantile Bank from an account held by McGinn Smith Funding to OCC evidencing the Unspecified Preferential Payments. *See* Brown Dec'1, Exhibits D(4) - D(8).

All of OCC's and Fisher's claims (collectively, "Preferred Investor Claims") have been adjusted for pre-Receivership distributions of principal and interest like all other investor claims, as shown on the Receiver's Claims Website (defined below). The Preferred Investor Claims, however, have not been adjusted to account for the Preferential Payments or the Unspecified Preferential Payments. Brown Dec'l. ¶ 15.

C. Claims Procedure

On March 9, 2012, the Receiver filed a Motion ("Claims Procedure Motion") (Docket No. 466) for entry of an Order approving, among other things, the Receiver's proposed procedure for the administration of claims against the MS Entities.

On March 27, 2012, the Court entered an Order granting the Claims Procedure Motion (Docket No. 475), which was subsequently amended by an Order dated April 17, 2012 ("Claims Procedure Order") (Docket No. 481). Each investor and known creditor of the MS Entities was mailed on May 1, 2012 an Access Notice describing the claims process and enclosing (i) Notice of the Claims Bar Date and Claims Procedure and (ii) a Claim Form. Brown Dec'l. ¶18. A confidential password providing access to the Receiver's Claims Website at www.mcginnsmithreceiver.com ("Claims Website") was also provided. *Id.* If an investor or creditor agreed with the description and amount of their claim(s) as listed on the Claims Website and the claim(s) were not listed as disputed, contingent or unliquidated, the investor or creditor did not need to take any further action. *Id.* All other investors and creditors needed to timely file a paper claim before the bar date of June 19, 2012, as further described in detail on the Claim's Website. *Id.*

The Claims Procedure Order established June 19, 2012 ("Bar Date") as deadline for creditors and investors to file claims against the MS Entities. Brown Dec'l. ¶19.

In accordance with the Claims Procedure Order, nearly six hundred creditors and investors timely filed paper claims prior to the Bar Date. Brown Dec'l. ¶20. In addition, more than 3,127 claims of investors and creditors were included on the schedules posted by the Receiver on the Claims Website in accordance with the Claims Procedure Order. *Id.*

The Receiver conducted an initial review of the paper claims timely filed by creditors and investors in accordance with the Claims Procedure Order and determined it was necessary to establish a reserve as to investor claims totaling approximately \$23,617,190 since those claims have been listed by the Receiver as disputed, contingent or unliquidated. Brown Dec'l. ¶21.

D. Plan of Distribution Process

On December 30, 2015, the Receiver filed a Motion (Docket No. 847) (“Plan Distribution Motion”) to seek approval of (i) a plan of distribution of assets of the MS Entities to investors (“Plan of Distribution”); and (ii) interim distributions to investors with allowed claims scheduled or timely filed in accordance with the Claim Procedure Order. On October 31, 2016, the Court entered a Memorandum-Decision and Order (Docket No. 904) (“Plan Distribution Order”) granting the Plan Distribution Motion, overruling objections, approving the Plan of Distribution, and allowing the Receiver to make interim distributions as set forth in the Plan Distribution Motion.

Among other things, the Plan of Distribution provides for a reserve for disputed claims to allow the Receiver to make initial distributions, but to also provide for funds to be reserved until any objections to disputed claims can be heard and decided by

final order of the Court. As of July 6, 2018, \$6,308,887 has been distributed to investors with allowed claims as a First Distribution. Brown Dec'1. ¶24.

The Plan of Distribution provides that all investor claims would be calculated by using the “Net Investment” methodology, i.e., the claim amount is equal to the amount of the initial investment made less any distributions received prior to the appointment of the Receiver, including any distributions of principal or interest. Plan of Distribution, Art. IV. The Plan of Distribution further provides for a collateral recovery offset (“Collateral Recovery Offset”), where distributions made on account of investor claims will be reduced on a dollar-for-dollar basis to the extent the investor has received a recovery from a source other than the Receivership in connection with their claimed loss. *Id.* Art. II.

E. Claims Motions

On September 21, 2017, the Receiver filed a Motion (Docket No. 937) (“First Claims Motion”) to seek disallowance of certain filed paper claims that were duplicative of the corresponding claims granted by the Receiver. On November 9, 2017, the Receiver filed a Statement (Docket No. 957) in furtherance of the First Claims Motion, adjourning the First Claims Motion with respect to those duplicative investor paper claims filed by investors whose Receiver-granted claims have been disputed by the Receiver. On December 28, 2017, the Court entered an Order granting the First Claims Motion and disallowing the duplicative paper claims other than with respect to those filed by investors with disputed claims (Docket No. 966).

On February 15, 2018, the Receiver filed a Motion (Docket No. 974) (“Second Claims Motion”) to seek disallowance of certain filed paper claims for which there

is no basis for payment in the books and records of MS & Co. On April 13, 2018, the Court entered an Order granting the Second Claims Motion and disallowing the paper claims.

On March 19, 2018, the Receiver filed a Motion (Docket No. 984) (“Third Claims Motion”) to seek disallowance of certain claims of former MS & Co. brokers. On May 4, 2018, the Receiver filed a Reply (Docket No. 1002) to the Response of Frank Chiappone (Docket No. 995) to the Third Claims Motion. That Motion remains pending.

On July 6, 2018, the Receiver filed a Motion (Docket No. 1009) (“Fourth Claims Motion”) to seek disallowance of certain paper claims filed by Preferred Investors (as defined therein) and to apply a Preferential Payment Offset to the distributions to be made to Preferred Investors. On August 27, 2018, the Receiver filed a Reply (Docket No. 1020) (“Reply”) to the Opposition filed by certain Preferred Investors (Docket No. 1019) to the Fourth Claims Motion. The Receiver’s Reply contained brokerage statements, wire transfer confirmations, and copies of cashier’s checks supporting the Receiver’s claims as to all of the Preferential Payments alleged in the Fourth Claims Motion. OCC and Fisher were among the Preferred Investors described in the Fourth Claims Motion, but the payments made to OCC, as described herein, were not addressed in the Fourth Claims Motion.

ARGUMENT

A. Rising Tide Accounting Methodology Should be Applied to Promote Equality Among Investors

The district court has broad power and discretion to determine relief in an equity receivership. *See S.E.C. v. Elliott*, 953 F.2d 1560, 1566 (11th Cir. 1992); *S.E.C. v. Basic Energy & Affiliated Res., Inc.*, 273 F.3d 657, 668 (6th Cir. 2001). “In equity receiverships resulting from SEC enforcement actions, district courts have very broad powers and wide

discretion to fashion remedies and determine to whom and how the assets of the Receivership Estate will be distributed.” *S.E.C. v. Detroit Mem’l Partners, LLC*, No. 1:13-cv-1817-WSD, 2016 WL 6595942 at *5 (N.D. Ga. Nov. 8, 2016) (internal quotation omitted). A receiver’s choice among allocation schemes in the course of administering a receivership is within the discretion of the district court to approve or disapprove. *S.E.C. v. Huber*, 702 F.3d 903, 908 (7th Cir. 2012).

Of the methodologies available for the distribution of receivership, two common methodologies are the Net Investment method and the Rising Tide method. “Courts regularly employ these methodologies in distributing receivership assets.” *S.E.C. v. Forte*, Nos. 09-63, 09-64, 2012 WL 1719145 at *3 (E.D. Pa. May 16, 2012). When applying the Net Investment method, pre-receivership payments received by an investor are subtracted from the investor’s total principal amount before determining that investor’s pro rata distribution. *In re S.E.C. v. Coadum Advisors, Inc.*, No. 1:08-CV-11-ODE, 2009 WL 10664889 at *6 (N.D. Ga. Sept. 24, 2009). The Court already approved the Net Investment method for the calculation of investor claim amounts pursuant to the Receiver’s Plan of Distribution. *See* Plan Distribution Order at 15. The Court also approved the use of the Rising Tide methodology in the calculation of the Collateral Recovery Offset. *See* Plan Distribution Order at 12-13.

The Rising Tide method is also commonly approved for the apportionment of assets in an equity receivership. *See S.E.C. v. Huber*, 702 F.3d at 906 (“Rising tide appears to be the method most commonly used (and judicially approved) for apportioning receivership assets.”). The Rising Tide method subtracts pre-receivership payments received by an investor from the investor’s pro rata distribution, reducing that investor’s pro rata

distribution on a dollar-for-dollar basis. *U.S. Commodity Futures Trading Comm’n v. Lake Shore Asset Mgmt. Ltd.*, No. 07 C 3598, 2010 WL 960362 at *7 (N.D. Ill. Mar. 15, 2010).

The Rising Tide methodology “brings the recovery of claimants who received no payments during the course of the Ponzi Scheme equal to those claimants who did receive payments during the course of the Ponzi Scheme.” *In re Receiver*, No. 3:10-3141-MBS, 2011 WL 2601849 at *2 (D.S.C. July 1, 2011). Otherwise, a straight pro rata distribution of funds, irrespective of pre-receivership payments, “would be inequitable because it would unfairly elevate investors who received those pre-receivership payments.” *Lake Shore Asset Mgmt. Ltd.*, No. 07 C 3598, 2010 WL 960362 at *9.

Courts have not approved the use of the Rising Tide methodology where a significant amount of investors would not recover any distribution as a result of applying that methodology. *S.E.C. v. Huber*, 702 F.3d 903, 907 (7th Cir. 2012) (approving Rising Tide where only 18% of investors would receive no recovery); *U.S. Commodity Futures Trading Comm’n v. Barki, LLC*, No. 3:09 CV 106-MU, 2009 WL 3839389 (W.D.N.C. Nov. 12, 2009) (refusing to approve Rising Tide where 55% of investors would receive no recovery); *see also S.E.C. v. Byers*, 637 F. Supp. 2d 166, 182 (S.D.N.Y. 2009) (approving the Net Investment methodology after receiver did not recommend using Rising Tide because 45% of investors would not receive a recovery). In this Receivership, the Receiver is making distributions to all investors with allowed claims. *See* Third Written Status Report of the Receiver, at 6 (Docket No. 925).

B. OCC’s Distributions Should be Adjusted Using the Rising Tide Methodology

Distributions made on account of the Preferred Investor Claims should be adjusted to account for OCC’s receipt of Preferential Payments and Unspecified Preferential

Payments using the Rising Tide methodology (“Preferential Payment Offset”). After January 2008, when interest payments on the junior tranches of Four Funds Notes were reduced and ultimately eliminated for all other investors, OCC continued to receive Preferential Payments and Unspecified Preferential Payments. OCC was elevated to a preferred position by MS & Co. over all other investors in the Four Funds.

The Net Investment method was applied to all investor claims, including the Preferred Investor Claims, to account for pre-receivership payments of principal and/or interest made to all investors, as approved by the Plan Distribution Order. *See* Plan Distribution Order at 15. Unlike the rest of the investors in the Four Funds, however, OCC recovered the Preferential Payments and the Unspecified Preferential Payments while ordinary investors ceased receiving anything on account of their Four Funds investments. The Preferential Payments and the Unspecified Preferential Payments received by OCC thus reduced amounts available for distribution to all investors defrauded by McGinn and Smith and unfairly increased total recoveries of OCC.

Although courts have not approved the use of the Rising Tide methodology where a large percentage of investors would not receive a recovery as a result of the application of Rising Tide, this is not the case here. After application of the Preferential Payment Offset, OCC will not receive an interim first distribution and will have a credit against future distributions in the amount of the excess of the Preferential Payments and the Unspecified Preferential Payments over the amount of the interim first distribution.² OCC, however, represents less than 1% of all MS & Co. investors. Further, the credit against

² After application of the Preferential Payment Offset proposed in the Fourth Claims Motion, and application of the Preferential Payment Offset proposed here, Fisher will still receive an interim first distribution on account of his TAIN Claims. *See* Motion, Exhibit A.

future distributions would not prevent OCC from receiving further distributions if the credit were to be consumed by the amount of the distribution.

To permit OCC to retain the Preferential Payments and the Unspecified Preferential Payments, without a corresponding dollar-for-dollar reduction in the amount of its pro rata distribution, would result in the OCC retaining excess amounts for no reason other than that it was arbitrarily selected by MS & Co. to receive supplemental payments while other investors received nothing. The Preferential Payment Offset promotes equality among all investors by accounting for the arbitrary treatment of OCC.

To apply the Preferential Payment Offset, the Receiver has used the books and records of MS & Co., including records of wire transfers and bank checks, to determine when the Preferential Payments and the Unspecified Preferential Payments were made to OCC and, if discernable, on account of which specific investment the Preferential Payment was made. Presently, OCC only has claims for investments made in FEIN. Accordingly, the Receiver has applied the Preferential Payment Offset to OCC's distribution on account of its FEIN claims. Brown Dec'1 ¶ 30.

The evidence recovered by the Receiver shows that in February 2008, OCC received a Preferential Payment in the amount of \$866.25 on account of the TAIN investment it held at the time. The Investment Register shows that on January 8, 2009, that TAIN investment was transferred to Fisher. Accordingly, the Receiver has applied the Preferential Payment Offset for this Preferential Payment to Fisher's TAIN Claims.³ Brown Dec'1 ¶ 31.

³ The Receiver has recovered evidence in the books and records of MS & Co. that a portion of OCC's FIIN investment was also transferred to Fisher in January 2009. It is unclear, however, exactly what portion of the investment was transferred to Fisher and so the Receiver has elected to apply the Preferential Payment

C. Summary Proceedings are Appropriate

The Receiver has sought to provide OCC and Burton Fisher with appropriate notice and sufficient time to respond to the Motion. Accordingly, the Receiver has complied with the claim objection and notice procedures set forth in the Federal Rules of Bankruptcy Procedure (“Bankruptcy Rules”) as a form of best expression of law. Bankruptcy Rule 3007 requires that a claim objection must be filed and served at least thirty days before any scheduled hearing and that the objection must be served on the claimant by first class mail. Fed. R. Bankr. P. 3007(a)(1), (2).

In accordance with Rule 7.1 of the Local Rules of Practice for the United States District Court for the Northern District of New York, the Receiver has filed and will serve the Motion on each of OCC and Fisher’s legal representative, as well as their counsel, at least thirty-one days in advance of the scheduled return date of November 15, 2018. The Receiver will give notice of the Motion to the Securities and Exchange Commission, all parties who have filed a Notice of Appearance in this action by ECF, and all creditors and parties in interest via the Receiver’s website (www.mcginnsmithreceiver.com), as well as posting at the top of the Receiver’s website an explanation of the Motion. Additionally, notice by first class mail will be given to each of OCC and Fisher. Brown Dec’1 ¶32.

The Receiver requests that the Court enter an order granting the relief requested in this Motion without a hearing with respect to those claims for which an objection is not timely interposed. Disallowance or adjustment of a claim without a hearing where there is no factual dispute is an appropriate and preferred procedure in federal receivership cases. *See S.E.C. v. Elliott*, 953 F.2d 1560, 1566 (11th Cir. 1992) (holding that

received by OCC in February 2008 in connection with its FIIN investment to OCC’s distribution on account of its remaining Four Funds Claims. Brown Dec’1 ¶ 31, n.2.

summary proceedings are favored in federal receivership cases because a summary proceeding “reduces the time necessary to settle disputes, decreases litigation costs, and prevents further dissipation of receivership assets”); *United States v. Fairway Capital Corp.*, 433 F. Supp. 2d 226, 241 (D. R.I. 2006) (“Receivership courts can employ summary procedures in allowing, disallowing and subordinating claims of creditors”).

CONCLUSION

The Receiver requests that the Court enter an Order substantially in the form attached to the Motion as Exhibit C applying the Preferential Payment Offset to the Preferred Investor Claims, together with such other and further relief as the Court deems just and proper.

Dated: October 15, 2018

PHILLIPS LYTTLE LLP

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UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF NEW YORK

-----X
SECURITIES AND EXCHANGE COMMISSION :

Plaintiff, :

vs. :

Case No. 1:10-CV-457
(GLS/CFH)

McGINN, SMITH & CO., INC., :
McGINN, SMITH ADVISORS, LLC :
McGINN, SMITH CAPITAL HOLDINGS CORP., :
FIRST ADVISORY INCOME NOTES, LLC, :
FIRST EXCELSIOR INCOME NOTES, LLC, :
FIRST INDEPENDENT INCOME NOTES, LLC, :
THIRD ALBANY INCOME NOTES, LLC, :
TIMOTHY M. MCGINN, AND :
DAVID L. SMITH, GEOFFREY R. SMITH, :
Individually and as Trustee of the David L. and :
Lynn A. Smith Irrevocable Trust U/A 8/04/04, :
LAUREN T. SMITH, and NANCY MCGINN, :

Defendants, :

LYNN A. SMITH and :
NANCY MCGINN, :

Relief Defendants. and :

GEOFFREY R. SMITH, Trustee of the :
David L. and Lynn A. Smith Irrevocable :
Trust U/A 8/04/04, :

Intervenor. :

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CERTIFICATE OF SERVICE

I, Dawn M. Spires, being at all times over 18 years of age, hereby certify that on October 15, 2018, 2018, a true and correct copy of the (i) Notice of Motion and Fifth Claims Motion of William J. Brown, as Receiver, for an Order Applying Preferential Payment Offset to Certain Preferred Investor Claims (“Fifth Claims Motion”), Declaration of William J. Brown, as Receiver, in Support of the Fifth Claims Motion, and (iii) Memorandum of Law in Support of the Fifth Claims Motion was caused to be served by e-mail upon all parties who receive electronic notice in this case pursuant to the Court’s ECF filing system, and by First Class Mail to the parties indicated below:

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And, I hereby certify that on October 15, 2018, I mailed, via first class mail using the United States Postal Service, a copy of i) Notice of Motion and Fifth Claims Motion of William J. Brown, as Receiver, for an Order Applying Preferential Payment Offset to Certain Preferred Investor Claims (“Fifth Claims Motion”), Declaration of William J. Brown, as Receiver, in Support of the Fifth Claims Motion, and (iii) Memorandum of Law in Support of the Fifth Claims Motion to the individuals listed below:

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Dated: October 15, 2018

/s/ Dawn M. Spires
Dawn M. Spires