

Dear Tim,

Enclosed please find 26 pages of thoughts, rambblings if you will. I apologize for the length and the handwriting.

The material is sensitive so I could not ask Norma to type. If I tried to type it, you would be on your 3rd day at Beaver Creek when I finished. You will have difficulty reading it, but please take the time.

After reading it (maybe a couple of times), please feel free to comment and criticize. It is meant to be thought provoking, not the final solution to anything. I would like you to give it substantial thought before we get together. I believe that will be enormously helpful towards a productive end to our meeting. I would like to get together with you to discuss the enclosed before our Wednesday meeting with Brian and Mary Ann. I believe we need to do that away from the office - maybe a meeting room at the FOC.

We have a lot of hard work ahead of us, and we need to be rowing the boat together in order to successfully complete the tasks before us. My hope is that you recognize my comments for what they are - well intended, without malice, necessary to get us working together again in an agreed upon direction.

I will be in around 10:00, as I have to stop by CSTDS. I know we have a meeting with Bill Spoyer at 10:00. After meeting with Bill we can get together to determine the best time for our meeting.

Thanking you in advance for your patient patience and understanding.

Sincerely -
MS

Dear Tim,

I have chosen to put my thoughts on paper rather than express them in our planned meeting with Brian and Mary Ann on Wednesday evening for several reasons. First and foremost, the present crisis we are facing is really our crisis, and our discussions should remain confidential. We are the ones responsible for a plan, and any comments or ideas from Brian and Mary Ann will probably be more supplementary than structural. Secondly, I am sensitive to the fact that there may come a time when they may be asked to recount these discussions, and I would not want either of them to be in a position that forces them to choose between testimony harmful to us or perjury.

I am hopeful that you are reading this prior to our meeting on Tuesday. I wanted to get together with just you, to express some things that should be addressed solely between partners; and, after our more personal discussions I am looking forward to

developing a course of action that will stave off our immediate financial crisis and then lead to an ultimate resolution.

The idea that I am communicating to you by this means is awkward at best and probably seen as somewhat ridiculous. However, my present state of mind is such that this exercise will hopefully have a therapeutic effect as well as communicative.

We have worked together for over 20 years in a generally benign, ~~prop~~ prosperous, and endearing relationship. We have been through so much together to get where we are. Building and holding together a business for over 20 years is no small feat. There are very, very few who can point to this kind of accomplishment. From very early on it has been very apparent to me that the vast majority of the credit for the success of this business is a result of your efforts. It has been your intellect, your vision, and your good business instincts that have been responsible for us not

only surviving, but succeeding. Every business or enterprise needs a leader, and you have filled that role extremely well. Over the years I have assumed the mantle of caretaker, one that is also necessary, but one that without leadership is merely an appendage. Our functions have worked well, and for twenty some years I have been the beneficiary of an extremely well balanced and satisfied life. I have enjoyed monetary rewards, but not at the expense of family or leisure. In short, it has been a great life.

However, for the last year, and in particular the last few months, I find myself overwhelmed and in a state recently that is probably bordering on depression. My work, my life at home, and I am sure my personality have all become negatively impacted. It is a result of one thing, and one thing only - the thought that the present situation with C⁺ is about to implode, and with it everything I have ever cherished.

I am sure that you will agree, that if our trusts go into default, everything else will come apart. The business has become addicted to the cash flow from the trust business, and without ~~it~~ ~~we~~ them will have a difficult time surviving. Although, I believe that we are on the verge of being able to develop other investment banking businesses, just as the importance of the brokerage revenues are diminishing. But we need time, and I am not convinced we will be able to acquire that time. The default of the trusts will drastically reduce revenues, cause us to lose brokers and at least their confidence in us, bring on crushing litigation and devastating publicity, and I am convinced prosecution by regulators or worse. The impact on our employees, customers, friends, and family will be devastating. I am just overwhelmed by the thought of the financial losses, the humiliation, the perceived betrayal of trust. I am trying to be strong in face of all

of this, but I can't sleep, I am convinced I have developed an ulcer, and I am being driven to moods of depression. I am sure that you are feeling some of these things as well. I know Mary Ann is. I have not shared any of this with Ryan, I assume because I have determined that it won't be helpful.

Aside from the above, I, unlike you, feel that we are vulnerable to criminal prosecution. Aside from the probable violation of Reg D as it relates to accredited investors, I am not aware of any action that would be remotely considered illegal. However, I would never underestimate the zeal of local or state or even SEC prosecutors to make a story out of our failure. Convictions of pit cat financiers is a great stepping stone up the career ladder.

I believe that we are at risk for the continued raising of investment dollars that are ~~not~~ now clearly unlikely to be repaid in full. As we do each

transaction we distribute every excess dollar back to C⁴ or McGinn, Smith & Associates partners. More recently, those dollars for the most part are used to fulfill the investment promise to earlier investors. While you have previously rejected my characterization of these acts as similar to a "ponzi scheme" because new dollars being raised are in fact buying new product, and only "profit dollars" are being used to cover shortfalls, I believe that our actions could be defined otherwise. The reason for my belief is that we are now in possession of indisputable empirical evidence that the new investments have no chance of being repaid in full. Whether less than 100% collections (66%) is due to normal attrition, fraud, billing errors, or poor credit judgment, it really does not matter. The facts are that we will never collect 100% or close to it. Therefore, our "profits" which we use are not profits at all, but rather monies that should be held in reserve to allow for the default collections for the protection of the new investors.

For us not to allow for these defects by setting up adequate reserves is, in my judgment, bordering on fraud. Certainly, by not disclosing in the prospectus our poor history of collections, we are not providing the prospective investor an accurate picture of his risk. We both know why we don't make that disclosure - because such disclosure would cause our salesman to cease selling and investors to cease buying. Thus, we are misleading both our own employees and customers.

I fully understand, as well as you, our need to continue raising money, and that a number of the collection defects were isolated incidents of fraud or gross incompetence by some of our dealers. However, those incidents have not impacted the majority of collections. Most of the defects are from poor credit risks. We now know that, and we continue to accept their contracts without adequate reserves, and treat the excess discounted cash flow as certain profit to be distributed as we see fit.

This is wrong. I strongly believe that in civil or criminal litigation we would lose badly on this point. "We knew the poor collection history, and yet continued to raise money as if we were ignorant of our own collection experience."

I am not an Eagle Scout, but I believe that both you and I are violating the high standards of integrity and ethics that have been the historical standard for us. That bothers me very, very much. But what terrifies me is the possibility of being indicted for such conduct, and worse, the prospect of conviction. I cannot emphasize enough how strongly I feel about this point.

I believe, and insist upon, that any plan we initiate to solve our problem must demonstrate our intentions to no longer proceed with "business as usual". We must be able to point to corrective action that was intended to prevent the recurrence of poor credit collections.

I am nearing the end of this personal confession, so I hope that I still have your attention. I apologize for the length.

Before we can realistically hope to overcome this crisis, we need to address how we are going to work together. One of the really great joys of building McGinn, Smith was the close personal style and relationship that we developed together. We became best friends, our families socialized together, and we worked very closely together. Yes, we assumed different responsibilities over the years, but we always did things together. We discussed business plans prior to implementation, consulted on problems and possible solutions, and always shared equally in profits and losses. Partners from beginning to end. While I would always give you the lion's share of the credit for those successes, I do believe there was and is a great benefit from having a partner to draw upon. I feel the last couple of years has seen us move away from that approach.

Your interests in WYFA and Poente have stolen some of the time that you would naturally be devoting to McGinn, Smith. This is a result of the excessive travel that both interests demand. I am not remotely suggesting that these interests have negatively impacted your effort or contribution. Far from it. You accomplish more in two days than most of us do in one. Where it has had an effect is that those times away have left less hours for us to get together and share our thoughts on business developments and personal feelings. When you are in the office, the door is generally closed, I assume to avoid the many interruptions from brokers and staff. While that is understandable, again it has an effect on the time we have to communicate with each other. I don't think we need to start making appointments to see each other or to draw up daily agendas, but I do think that it is critical for us to start meeting more regularly to discuss the implementation of whatever plan we agree upon.

These kind of personal crises that we are going through needs a lot of support. Due to the highly confidential nature of the cases, we are kind of stuck with each other. Besides, you have a great way of always giving me some glimmer of hope that all will end well. It usually does. I love you like a brother, and I am in awe of your many talents and abilities. ~~It is~~ I am hopeful that you see this epistle for what it is - a call to arms for both of us. A realization that we have to do things radically different and that we must start immediately. We must work closely together, but that we can expect help and support from both Mary Ann and Brian. With a lot of effort and a little luck, a year from now we can look back upon this time as our finest effort together. We really have no choice but to make that effort, the consequences of failure are absolutely intolerable.

Your everlasting friend
and partner
Dave

Facts to think about

1. C⁴ trusts

Year	Approximate funding
1994	2,500,000
95	8,575,000
96	10,200,000
97	22,846,000
98	26,000,000
99	35,601,000

Substantial growth in year 97-99
~~and~~ a result of business with
 Phase I and Safebank - dealers
 with poor collection history.
 Attrition in future years likely
 to accelerate. Deals have
 seen lengthened maturities in
 these years, adding to probable
 increased attrition.

Older deals are better deals,
 so as they are paid down, the
 ongoing requirements and deficits
 grow

2. Total debt outstanding at the
 end of 1999 is 70,000,000. This
 is a huge number in any body's
 world.

Prior to BC, CPD, MTP
 total debt was 61,000,000.

Collected monthly cash flow: 1,100,000
 At 38 x RMR = Portfolio Value = 41,800,000

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Debt :	61,000,000	
Portfolio value :	<u>41,800,000</u>	
	19,200,000	Deficit
Albany MS Credit :	2,000,000	
Line	<hr/>	
	\$ 21,200,000	Present value Deficit and liability

3. Structural monthly deficit of 600,000 and growing. Under present plan and approaches, the need is for new spending of 4,000,000 line. Assumes no future deficits. Thus, we need to raise 48,000,000 in 2000, 12,400,000 more than 1999 - a 35% increase. This is not realistic. Brokers are running out of sources. At sales meeting last week, the consensus was they would probably be able to match 1999. Slowness in closing recent deals would confirm this.

4. 1999 game plan called for structural monthly deficit to decrease from \$315,000 to \$243,000. Instead, it has grown to \$600,000. Plan called for a surplus of \$2,414,000 - does not exist.

2000 Plan - Same approach, same business mix, same assumptions

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5. even if we assumed that we were able to generate \$800,000/mo, the deficit will soon reach that if we continue to fund the same credits, leaving nothing for other uses. Once we exceed it - game, set, match. If we stay on this course, I see us with no more than 6 mo. life
6. We are also paying monthly monitoring costs of \$110,000, including 75,000 for ITing. This too, will probably continue to grow
7. All bank credit line no longer secured with separate contracts. Now is unsecured for Tim & Dave. Balance around \$2,000,000 ouch!
8. Present morale of Brian and Mary Ann is very low. Both are fearful - Brian for the future of McBurn, Smith, Mary Ann for personal legal liability and loss of license to practice. Plan needs to instill confidence in them.

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9. Sephora - all of staff is extremely uncomfortable with them. They are ~~our~~ line people - we should listen to them. This kind of business is no different than Phase F. Result will be the same. We must continue to demand higher standards, give no exceptions to those standards, and ~~ask~~ to move away from this kind of dealer and this type of business ASAP

10. Distributions to Tim & Dave going forward should be eliminated. Not only should those monies be set up as reserves for investor protection, but in future litigation, those distributions would be extremely detrimental to us. Hard to justify investors being 1/2 their money, while we continue to ~~prop~~ prosper at compensation levels that would seem obscene to the average citizen sitting in judgement. This is a very personal issue for us, but I feel strongly about it. You have larger financial commitments than F, and loss of

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distributions would be more of an impact. I am in a position to help. Let's talk!

11. Is it time to ask ourselves a fundamental question as to this whole business? Are the business concepts flawed? With industry leaders now giving away the product, it is not surprising that sales are being made to anyone and everyone, as long as a dealer has access to a supplier, such as ourselves, his risk is negligible. The entire approach evokes poor credit policy at best and fraud at the worst. Our problems are hardly unique - Protection One, Montronics, DeMark - all have the same problems. If we are going to remain in business - we must upgrade the credit quality and find new ways to help ensure payments will be made for the life of the contract.

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Plan ideas / ramblings

1. First and foremost - we must stop funding deficit creating business. We can't fix the past problems if we are creating future problems at an equal or faster rate.
2. Obviously, we must reduce the present deficit:
 - a. dramatically increase collections
 - and/or
 - b. restructure debt
3. Increase collections:

here we have made a start. We should hire mgt. and staff from Key Bank. All 3 that we interviewed last week are interested. They believe they can bring staff collectors with them. None can start until April 1st - this is a problem, but we can use them to consult prior to that date.

We need to determine who, how many, where, budgets, and equipment/resource needs

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4. We also need to review our legal remedies and approaches. One of the key people we interviewed holds that responsibility at Home.
5. While collections are a priority, we need to continue to find ways to improve due diligence and install better credit reviews. Again, let's seek experienced people.
6. The collapse of WFC (Clifton Park) in December might hold some resources and opportunities. This was a fast growing sub-prime lender of mortgages. Bear Stearns was financing. 500 employees. National presence. A number of local financial institutions have already been buying. Let's talk to the principals. See what we can learn. Get possible leads on key people.

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Next Page - finally something new to think about. I hope that I haven't already lost you.

Heart & Soul of some ideas
to restructure debt and
reduce present financing costs.

1. First, I believe it is
in our interest to bring the
overall debt level down.
If we are forced to deal
with defaults in the future,
it will be easier to restructure
a smaller debt load. Plus,
it is obviously easier to
reduce debt before any defaults
occur.

I had previously suggested
repackaging existing RMR,
selling it, and paying down
Trust debt. Probably this
can only be done where
we have only Junior tranche
remaining, otherwise we will
violate Senior tranche cover
ratio. You were calling
Monotronics, etc. Can people
like Roy be of help here?
I understand that he is
doing some selling away from
us. If we can get an
acceptable price, this seems
like an idea worth pursuing.
I haven't even tried to
do numbers - that I leave
up to you.

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2. Absence the ability to package and sell existing RMR, we should consider reselling those trusts ^{as senior debt} where the Senior is paid down.

This amounts to approximately \$9,000,000. These include

LAI, INES, WSO, RTD, KT, STP, FMD, MBM, EB.

This would accomplish saving some interest costs, shifting liability from retail to institutional, putting cash in the hands of retail customers for future reinvestment.

One stumbling block may be the additional coverage required by banks. However, our more accommodative lenders (BSB etc) might be willing to be buyers.

We might get some queasy from customers and brokers because of loss of higher yield (most are 13 1/2%), but we can probably counter by saying most of the contracts are due to expire and we don't want to take the risk of homeowners ^{not} renewing.

3. Another idea might be to start to establish ourselves as a broker. Buy and sell RMR for fees and the spread.

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Obviously, we would try to do as riskless transactions. Maybe get brokers who are not only to bring us product but to sell product as well. On the other eye, make the purchases and sales within, in order to avoid paying brokerage costs and thus adding to our returns.

*** 4.

All of the aforementioned might be helpful, but they certainly do not present the opportunity for a final solution. However, there is a more daring and challenging path we can take that I believe can be a tremendous opportunity and eventually resolve a lot of our problems. The plan I speak of is to dramatically grow C⁴ into a major financial company. The business plan would be centered around C⁴ being a financial company that buys credit that is presently in arrears. Bob Wade the head of Key Bank's Collection and Loan Recovery mentioned this during our interview.

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Evidently, there is a huge market in purchasing credit that has been deemed uncollectible and has been forced by regulators to be written off. This credit is purchased at 6-12¢/1.00. It can then be packaged and resold or the debt can be turned over to collection people for another attempt at recovery. The concept is that a lot of this debt has never been properly handled by the existing collection departments. Experienced and highly competent recovery groups can do very well. Obviously, what debt is ~~also~~ selected for purchase and at what price is critical to success. I believe that we have the opportunity to acquire Key Bank's unit by hiring individuals and not have to pay for acquiring a complete business.

The attractiveness of this idea is not only that we might be able to develop a business with substantial cash flows to help reduce our present deficits, but it could be an outlet for ~~too~~ the trusts to sell ~~some~~ some of its accounts that are

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in arrears and then provide cash to help pay down the Trust debt. Those transactions would have to be a part of the overall business otherwise they would be accurately perceived as a bailout to the trusts. But if they were part of an overall business strategy of buying loans and credit in default, and returns were commensurate with other the returns on other asset purchases, I believe it could be done.

We would need to capitalize the company with substantial equity and ~~and~~ ~~then~~ acquire bank lines of credit to help finance the asset purchases. Potential equity partners might be:

1. Key Capital
2. GE Capital
3. Banks looking for a strategic partner and who understand the business

4. Venture Capital

I was thinking that your friend John Meriwether might have an interest or that he could be helpful in referring some investment sources.

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John could certainly be helpful ~~in helping~~ with the structure - he certainly understands leverage. Pointe Financial might have an interest. They would certainly understand the business concept.

The key to getting these people involved would be making them comfortable with who was running the business. If they saw the experienced hands of Key Bank personnel, they might be more inclined to become investors. Just as we see the possibility of recovering dollars for the trusts, banks might see the possibility of recovering some of their own assets that had been charged off. Thus, we would play the strategic partner angle and get a source of business.

The major benefit to us would be the transfer of assets from the various trusts. We would not have to sell only paper in arrears. We could also sell paper that is presently current. At what multiple I do not know, but every asset transferred out of the trusts into a commercial enterprise would

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be helpful to us in managing over deficits and thus keeping McGraw, Smith and its customers out of harms way.

Management structure for C⁴ would be critical. We would need a President, one experienced in these affairs. Collection and credit departments would have to be set up or reorganized. Documents would have to be acquired, laws governing credit companies researched, procedure manuals put together, training of employees, etc. A major commitment of our available resources - time, personnel, money ~~too~~ would have to be pledged. Your attention and commitment would be critical. Your ability in loan restructuring and deal making would be invaluable.

One of the reasons I like ~~about~~ this approach is that it gives a major deal to focus on. You are at your best when you are out elephant hunting. I don't know how much equity capital would be needed, but I am thinking in the \$50,000,000

range. I am trying to arrange a lunch with Bob Wade this week to get a better understanding of the business - its costs and its opportunities. I want you to join us.

This needs to be done in a big way if it is going to work. Now is the time for us to do this. Money is available. I believe people are at least starting to look for alternatives to a very pricey stockmarket. The challenge can get our motors working again, and we can do it together.

I have obviously not covered all possible approaches or solutions to our problems. Nor has there been an in-depth due diligence ~~done~~ done on the ideas that I did present. However, I think that they present a good starting point. Hopefully, you and I will have an opportunity to examine these in depth and outline the steps to get started. We need to get the ground running. I am available Tuesday afternoon and night and Wednesday morning. Thanks for your attention.

PTJ