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BEFORE THE FINANCIAL INDUSTRY
REGULATORY AUTHORITY

ORIGINAL

In the Matter of
MCGINN SMITH & COMPANY
20090179845

PART 1

VOLUME I
INVESTIGATIVE TESTIMONY OF
DAVID SMITH
WOODBIDGE, NEW JERSEY
FEBRUARY 1, 2010

ATKINSON-BAKER, INC.

COURT REPORTERS

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REPORTED BY: S. ARIELLE SANTOS, RPR, CSR, CLR

FILE NO.: A400C2F

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MCGINN SMITH & COMPANY
20090179845

Investigative testimony of DAVID SMITH, taken at
FINRA, 581 Main Street, 7th Floor, Woodbridge, New Jersey, on
February 1, 2010, commencing at 9:30 a.m.

1 APPEARANCES:

2
3 BY - CHRISTOPHER RATTINER

4 BY - STEVEN ROWEN

5 BY - MICHAEL NEWMAN

6 BY - GARY JAGGS

7 BY - MICHAEL PAULSEN

8 BY - REBECCA SMITH

9 BY - ROBERT MCCARTHY

10 FINRA

11 581 Main Street, 7th Floor

12 Woodbridge, New Jersey 07095

13 Representing FINRA.

14
15
16 BY - DAVID FRANCESKI, JR., ESQ.

17 STRADLEY, RONON, STEVENS & YOUNG LLP

18 2600 One Commerce Square

19 Philadelphia, Pennsylvania 19103

20 Tel: 215-564-8000

21 Representing Witness.

22
23 ALSO PRESENT:

24 JOSEPH CARR
25

DAVID SMITH

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A Brian Shea.

Q What personal bank accounts do you currently maintain?

A My bank accounts?

Q Yes, correct.

A I have a checking account at M&T Bank. That's it.

Q How about investment accounts?

A I have investments accounts in my own name. I don't think I have any.

Q Okay. How about trusts?

A I don't believe I have any trusts in my name.

Q Okay. And all your bills, your personal bills are paid through the M&T checking account?

A No. My wife has a checking account also.

Q Are you a signatory on that account?

A No.

Q And where is that account maintained?

A I believe it is at Bank of America.

Q Do you currently receive a salary?

A I have. It's quite spotty these

DAVID SMITH

days.

Q And where is that salary deposited?

A It's generally deposited in, I believe, my wife's account.

Q And have you filed your taxes for 2008?

A 2008, yes.

Q Correct. And obviously 2009, you have not done?

A No.

Q Have you received a 1099 in 2008?

A 2008, yes.

Q And who did you receive the 1099 from?

A Got one from NFS, may have gotten one from the bank. I don't know if I can get any interest on that checking account. If it is, it's not material. My wife gets a PIT from the New York State Teachers' Retirement, so she would have gotten a 1099. That's it.

Q Okay. And what are your current sources of income other than the broker-dealer?

A Basically income is -- define current for me, through all of 2009?

1 DAVID SMITH

2 Q 2009, let's say?

3 A Basically, the broker-dealer, for me
4 personally, I think that's it. I don't think there
5 are any investments in my name that produce income.
6 That's it.

7 Q Okay. Do you have income -- do you
8 have investments that are producing income in trusts,
9 not in your name?

10 MR. FRANCESKI: Wait a minute.

11 I am going to need an explanation as to
12 why that kind of personal financial
13 information is relevant. I have never
14 been in a deposition where my client,
15 that is not yet subject to any FINRA
16 sanction or fine, has been asked to give
17 personal financial information. So help
18 me out, guys.

19 MR. NEWMAN: Well, we are not
20 going to explain what the relevance to
21 our question is. We think it's relevant
22 to our inquiry, and we have had several
23 investigations where we asked for tax
24 records, personal financial information,
25 depending on what the case is about,

1 DAVID SMITH

2 and, you know, the questions we are
3 asking, I believe, are relevant to our
4 investigation.

5 MR. FRANCESKI: Okay. Without
6 further -- again, without further
7 explanation as to why that information
8 would be relevant, I am going to
9 instruct him not to answer for now. If
10 there is a foundation established that
11 is more connected to what is going on
12 here, you know, I will certainly
13 reconsider that for him, but at this
14 point I don't see any connection between
15 those questions and anything that I am
16 aware of adds to the subject of the
17 investigation.

18 MR. NEWMAN: Well, you might
19 want to consider that. There's plenty
20 of case law I can show you where, you
21 know, we don't have to establish
22 relevance to our questions for counsel,
23 and, you know, we have the prerogative
24 to ask questions we believe are relevant
25 to our investigation.

1 DAVID SMITH

2 If you want to advise him not
3 to answer, then we are going to have to
4 instruct him that his failure to answer
5 that question could result in
6 disciplinary action if he chooses not to
7 answer the question.

8 So if you want to discuss
9 that, we will hold off on that till the
10 next break, but -- and I can show you
11 some case law on that, too, if you like,
12 on that issue. Also, on the issue of
13 advice of counsel, too, in connection
14 with questions in OTRs, but the law is
15 pretty clear in that area.

16 MR. FRANCESKI: I would like
17 to see the cases, but for now I am
18 instructing him not to answer.

19 MR. NEWMAN: We will come back
20 to that. I do have a couple of
21 questions.

22 MR. RATTINER: Sure.

23 MR. NEWMAN: Piaker & Lyons,
24 that's the outside accounting firm that
25 McGinn Smith has utilized?

1 DAVID SMITH

2 work does he perform on behalf of McGinn
3 Smith?

4 THE WITNESS: He is the
5 auditor for the firm. He prepares tax
6 returns for a number of entities that
7 are associated with the firm, M&S
8 Partners, McGinn Smith Capital Holdings.
9 He's certainly been engaged in the past
10 to be the accountant for business
11 transactions that we have done through
12 the firm for 25 years. I couldn't give
13 you the list of them, but there's
14 certainly been a number of them.

15 MR. NEWMAN: Has Piaker &
16 Lyons ever audited the LLCs?

17 THE WITNESS: No.

18 MR. NEWMAN: Has any
19 accounting firm ever audited the LLCs?

20 THE WITNESS: No.

21 MR. NEWMAN: Now, you
22 testified before that you receive income
23 from McGinn Smith; is that correct?

24 THE WITNESS: (Nodding Head).

25 Yes.

1 DAVID SMITH

2 MR. NEWMAN: What other
3 entities have you received income from
4 over the last five years?

5 THE WITNESS: Well, I am sure
6 I have had investment income, interest,
7 dividends, but I don't think I have had
8 anything in my name for years. So when
9 you said five years, I don't recall any
10 material investment income. There are a
11 couple of old entities that we get cash
12 flow through, I think, TNA, which was a
13 20-year old thing. I get a 1099 from
14 Pine Street Capital. I think Chris
15 asked me that earlier, and I don't think
16 I listed that earlier. You were asking
17 for my 1099s.

18 MR. RATTINER: Hm-hm.

19 THE WITNESS: I think I get a
20 1099 from Pine Street Capital Partners.
21 I think that's to the best of my
22 recollection.

23 MR. NEWMAN: How long have you
24 been getting 1099s from Pine Street
25 Capital Partners?

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DAVID SMITH

THE WITNESS: Was the original partner, was formed in '04. I think maybe the first tax year was '05.

MR. NEWMAN: How about McGinn Smith Capital Holdings? Do you receive any income from McGinn Smith Capital Holdings?

THE WITNESS: No.

MR. NEWMAN: How about McGinn Smith Advisors?

THE WITNESS: No.

MR. NEWMAN: Does McGinn Smith Advisors file a tax return?

THE WITNESS: No. It's part of the holding company McGinn Smith Holdings.

MR. NEWMAN: Does McGinn Smith Holdings file tax returns?

THE WITNESS: Yes.

MR. NEWMAN: Was there a tax return filed for last year or was there a tax return filed in 2009?

THE WITNESS: Not in 2009, no.

MR. NEWMAN: When was the last

1 DAVID SMITH

2 THE WITNESS: It's an LLC.

3 MR. NEWMAN: What is your
4 position with the LLC?

5 THE WITNESS: I believe I am
6 president.

7 MR. NEWMAN: Who else is
8 involved in McGinn Smith Holdings?

9 THE WITNESS: Mr. McGinn.

10 MR. NEWMAN: What is his
11 position?

12 THE WITNESS: I believe he's
13 chairman.

14 MR. NEWMAN: Anybody else
15 besides the two of you?

16 THE WITNESS: Mr. Livingston.

17 MR. NEWMAN: What is his
18 title?

19 THE WITNESS: Senior
20 vice-president.

21 MR. NEWMAN: Anybody else?

22 THE WITNESS: No. I believe
23 that is it.

24 MR. NEWMAN: What is your
25 ownership interest?

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DAVID SMITH

THE WITNESS: 50 percent.

MR. NEWMAN: How about Mr.

McGinn?

THE WITNESS: 30 percent.

MR. NEWMAN: And Mr.

Livingston is 20?

THE WITNESS: 20, yes.

MR. NEWMAN: Have you ever

received income from McGinn Smith

Holdings?

THE WITNESS: No.

MR. NEWMAN: MS Advisors, when

was MS Advisors formed?

THE WITNESS: 2003, I believe.

MR. NEWMAN: Is that an LLC

also?

THE WITNESS: Yes.

MR. NEWMAN: What is the

ownership of the LLC?

THE WITNESS: It's 100 percent

owned by MS Holdings.

MR. NEWMAN: What is your

position with MS Advisors?

THE WITNESS: Managing member.

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DAVID SMITH

MR. NEWMAN: What do you do
for MS Advisors?

THE WITNESS: MS Advisors
primarily manages the four LLCs that
we've consistently referred to. I would
be the managing member of that.

MR. NEWMAN: Anybody else
affiliated with MS Advisors besides
yourself?

THE WITNESS: Well, Mr. McGinn
and Mr. Livingston, yes.

MR. NEWMAN: Same positions?

THE WITNESS: I think they are
-- I think, Mike, in terms of MS
Advisors, I think everybody is a
managing member, I think, is the
definition.

MR. NEWMAN: Have you ever
received any income from MS Advisors?

THE WITNESS: No.

MR. NEWMAN: Pardon me?

THE WITNESS: No.

MR. NEWMAN: Has MS Advisors
ever received any income?

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DAVID SMITH

Mr. Cranberry and everything.

MR. NEWMAN: What is 107
Associates?

MR. FRANCESKI: Simple
question. You can answer, but I am not
going to waste a whole lot of time.

THE WITNESS: It's an LLC
formed for investment purposes.

MR. NEWMAN: And that pertains
to the Coventry CMS offering?

THE WITNESS: The only
activity that I recall at 107 is done in
connection with the acquisition of USA.

MR. NEWMAN: Any other
entities besides the three you testified
to that are under the McGinn Smith
Holdings, LLC rubric?

THE WITNESS: There may be but
those are the three that come to mind.

MR. NEWMAN: And your
testimony is you never received any
income from McGinn Smith Holdings,
personal income?

THE WITNESS: I don't think

1 DAVID SMITH

2 so, no.

3 MR. NEWMAN: And would that
4 also apply to MS Advisors, MS Capital
5 Holdings and 107 Associates?

6 THE WITNESS: Well, it
7 certainly would with 107 Associates. I
8 am certain it applies for one for McGinn
9 Smith Advisors. McGinn Smith Capital
10 Holdings is a 28-year old entity and,
11 you know, a lot of ground covered over
12 28 years. I don't know. I can't recall
13 with certainty whether I received money
14 from Capital Holdings in those 28 years
15 or not.

16 BY MR. RATTINER:

17 Q What is the current status of First
18 Independent Income Notes?

19 A Continues to operate as an LLC, an
20 operating company in specialty finance. It has one
21 equity owner. It has multiple note holders in three
22 classes. The notes are presently in default. They
23 continue to collect income on investments that are
24 current in paying. They continue to address those
25 investments, or those loans, I guess is a better way

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DAVID SMITH

We chat with them, and from time to time, and they tell us that it's still in litigation, but I am not optimistic in these kind of enterprises.

Q And the connection there was this other broker-dealer?

A It was actually a gentleman that I had met -- that I had met through working with Palisades Pictures. And he was doing a \$25 million offering with Fox Pictures. They raised 17 million at the time. They were looking for some closing financing. We negotiated a special deal to conclude that financing and get paid, be the first ones out, and that never happened.

Q Okay. SPT4?

A SPT4 is, they are amortizing. Whatever is carried out in that balance sheet is, I believe, the amortized amount.

Q And the affiliation, if any?

A None, I mean -- well, at one point we made an offering of these Alarm Contracts back in -- quite a while ago, I think in the late '90s, maybe early 2000. But we have no ownership. So when you say affiliation, I have no ownership.

Q Did -- the offering was originally

1 DAVID SMITH

2 SPT1, that would have been four offerings in total?

3 A No. I think my recollection was that
4 there were four separate offerings of SPT -- the
5 acronym is Security Participation Trust, and it was
6 sort of innovative way to finance Alarm Contracts,
7 but I think we used that designation because that was
8 a specific pool of assets that were bought.

9 Q Okay. 74 State Street?

10 A 74 State Street has not been current
11 since March '09. So in '07 it was current. But it's
12 not current at the moment.

13 Q And the affiliation, if any?

14 A Again, McGinn Smith did a placement
15 for some preferred stock, but we have no ownership.

16 Q Okay. GSC?

17 A GSC, no ownership. The GS stands for
18 Goldman Sachs. It was a bunch of Goldman Sachs guys
19 that did an REIT to invest in RMBSS and CMBSS,
20 commercial mortgage-backed securities and residential
21 mortgage-backed securities. GSC in June of '09 has
22 filed for bankruptcy, and we will be writing that
23 entirely off.

24 MR. NEWMAN: And what was the
25 affiliation with GSC?

1 DAVID SMITH

2 THE WITNESS: Zero.

3 MR. NEWMAN: I want to go back
4 to SPT4. You said that was a series of
5 different Alarm Contract offerings?

6 THE WITNESS: Yeah. I think
7 Chris's question was how did four -- he
8 wanted to know if it was part of one,
9 and my recollection was that back in the
10 late '90s, we were very active in the
11 home security alarm business. That was
12 one of our offerings. Those assets
13 became available, and we purchased that
14 pool of assets, and I have to believe we
15 identified them as SPT4 to distinguish
16 that pool of assets.

17 MR. NEWMAN: Okay. Let's be
18 specific. Pool of assets, what exactly
19 did the LLC invest in? What type of
20 security was it?

21 THE WITNESS: Home security
22 Alarm Contracts. They are residential
23 Alarm Contracts that are under contract
24 by a home owner to make a specific
25 payment for a specific period of time.

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DAVID SMITH

MR. NEWMAN: Is that pooled
into some kind of security?

THE WITNESS: No.

MR. NEWMAN: So the LLC is
actually buying or investing in the
Alarm Contracts?

THE WITNESS: That is correct.

MR. NEWMAN: Now, does SPT4
raise money from investors?

THE WITNESS: Years ago they
did, yeah, but then those assets were
purchased by the LLC.

MR. NEWMAN: SPT4 raises --
SPT4, what is the entity, the
corporation, LLC? What is the
ownership?

THE WITNESS: They are
generally done under a grantor trust.
Most of our transactions were done in
that fashion.

MR. NEWMAN: Okay. So who was
the trustee on that trust?

THE WITNESS: I don't remember
specifically but more likely than not

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DAVID SMITH

McGinn Smith Capital Holdings.

MR. NEWMAN: All right. So McGinn Smith Capital Holdings owns a stake in that trust?

THE WITNESS: No. Just the trustee. They don't own any stake.

MR. NEWMAN: So who actually owns -- who are the beneficial owners of that?

THE WITNESS: Basically the note holders.

MR. NEWMAN: I am talking prior to the investment.

THE WITNESS: The note holders.

MR. NEWMAN: Okay. And the note holders were individuals who invested in the offering?

THE WITNESS: That is correct.

MR. NEWMAN: And does the investment of the LLC take out or pay off the note holder's investment?

THE WITNESS: If it was maturing and the assets were for sale,

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DAVID SMITH

yes.

MR. NEWMAN: Well, do you
know?

THE WITNESS: I just answered
yes.

MR. NEWMAN: Okay. You sort
of framed it like a hypothetical.

THE WITNESS: Well, I didn't
mean to. I mean, I was trying to
distinguish between if there was a
maturity date or if there was not a
maturity date. And if there is a
maturity date, then the answer to your
question would be affirmative. If there
is not a maturity date, it wouldn't be
affirmative. So I was wrestling with
that distinction.

MR. NEWMAN: Okay. That's
fine. SPT4, was there an offering,
memorandum or prospectus that was used
to sell that investment?

THE WITNESS: Sure.

MR. NEWMAN: And when was the
offering made, approximately?

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DAVID SMITH

THE WITNESS: I believe, as I testified, it was in late '90s, maybe 2000.

MR. NEWMAN: And how much money was raised?

THE WITNESS: I don't recall.

MR. NEWMAN: Approximately?

THE WITNESS: Approximately -- most of our offerings were in the 2 to \$3 million range. So I would suspect it was a similar amount.

MR. NEWMAN: And McGinn Smith is, as you said, a trustee for the trust that owns?

THE WITNESS: I believe, to the best of my knowledge, McGinn Smith Capital Holdings, that's generally who we used.

MR. NEWMAN: And McGinn Smith Capital Holdings receive an annual fee for acting as trustee?

THE WITNESS: No.

MR. NEWMAN: What fee does McGinn Smith Capital Holdings receive?

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DAVID SMITH

THE WITNESS: Zero.

MR. NEWMAN: So McGinn Smith
receives a placement fee for selling
the --

THE WITNESS: Yes.

MR. NEWMAN: -- units for
SPT4?

THE WITNESS: Yes.

MR. NEWMAN: And at the time
the LLC invested in SPT4, the money has
been raised, the Alarm Contracts have
been purchased, invested in. What is
the status of that investment at the
time the Alarm Contracts are purchased
by the LLC? Were they in default or
were the payments current?

THE WITNESS: No, there's not
a default with Alarm Contracts. When
you buy Alarm Contracts, you basically
buy a cash flow. The cash flow is
identified by recurring monthly revenue.
It's called RMR in the trade.

MR. NEWMAN: Okay.

THE WITNESS: There's a built

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DAVID SMITH

in attrition or assumption that one makes that there's going to be a certain number of contracts that are going to not renew, maybe they quit paying. There is a contract that is -- you lawyers have a term for it. I can't remember what it is. But it's basically if they default and they can prove you didn't have proper service, they don't have to pay. Help me out.

MR. FRANCESKI: I am not sure I can.

THE WITNESS: Anyway, the whole reason I am bringing that up is because there is a contract between the homeowner and the issuer of the Alarm Contract, but the ability to enforce is very -- is hard.

We have collection agencies, we have attorneys, but the real world is, you are not going to go in and pull the wires out of the guy's house. If he chooses not to pay, he basically says, well, the alarm didn't work. So, you

DAVID SMITH

1
2 know -- so when you do these kind of
3 investments, you know that there's going
4 to be a certain amount of people that
5 are not going to be there at the end of
6 the day.

7 So your question, Mike, was
8 are they in default, no. Have you lost
9 some of the contracts, yes. And so when
10 you make a new purchase, you always use
11 an evaluation of what the RMR is at
12 that -- any given time, and there's a
13 multiple of that RMR. I am telling you
14 more than you want to know, I can tell
15 by your look.

16 MR. NEWMAN: That's fine. I
17 understand the general concept. So
18 basically there's a cash flow analysis
19 is done based on certain number of Alarm
20 Contracts or security alarms, security
21 holders not paying their monthly
22 payment.

23 THE WITNESS: More
24 importantly, the ones that are paying.

25 MR. NEWMAN: So there's a

1 DAVID SMITH

2 set -- there's a minimum amount that's
3 needed to pay the promise return to the
4 Alarm Contract holders?

5 THE WITNESS: Right. And
6 it's -- those contracts are a function
7 of a number of things, not the least of
8 which is how mature they are. The more
9 mature they are, the better. If I go
10 out and sell you a new Alarm Contract,
11 and you are a new owner, maybe you think
12 it is a pretty neat idea, but after a
13 year you've never turned it on, or maybe
14 you've had six false alarms and you're
15 real tired of it so you decide you are
16 not going to do it. Most of these
17 contracts are for three years. After
18 the three year or the fifth year, if
19 that guy is still renewing and still
20 paying, you got him for life. He's
21 there for 20 years.

22 MR. NEWMAN: Okay. But the
23 investors in the note offering, they are
24 promised a certain return on their
25 investment?

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DAVID SMITH

THE WITNESS: Well, I wouldn't go so far as to use the word promise, but, yes, there is a coupon attached with the investment that feeds their return, yes.

MR. NEWMAN: And that return is a monthly return or a quarterly return?

THE WITNESS: Some were done monthly, some were done quarterly.

MR. NEWMAN: What were the majority of the investors in this SPT4? What were they receiving monthly?

THE WITNESS: Early on -- most of our deals we did on a monthly basis. At some point the administrator of that got really difficult, the administration of that got difficult. We switched to quarterly. I don't remember if SPT, whether it was monthly or quarterly.

MR. NEWMAN: All right. So at the time the LLCs invest in SPT4, were payments current on -- the monthly required payment, were they being made

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DAVID SMITH

as required or were there payments
reduced for some reason?

THE WITNESS: What we did was
determine whether the recurring monthly
revenue was equivalent to the purchase
price. We do an analysis. We do an
analysis of the description and the
maturity of the contracts because we
want to know should we make an
assumption going forward of 10 percent
or 12 percent or 20 percent, all of
which has a major impact of what you are
going to pay.

The RMR or the valuation in
this business ranges from 40 times to a
hundred times. Breaks just sold their
company last week for 60 times.

MR. NEWMAN: You are providing
more information.

MR. FRANCESKI: I think you
were at a different level, weren't you,
Mike?

MR. NEWMAN: I am trying to
find out.

1 DAVID SMITH

2 THE WITNESS: You are trying
3 to find out what we paid for them,
4 that's what I am trying to give you --

5 MR. FRANCESKI: No, he's
6 trying to find out --

7 MR. NEWMAN: We are talking
8 over each other. First of all, let me
9 finish my question or the court reporter
10 is going to hit both of us over the head
11 with a book. What I'm asking you is I
12 think a simple question. Maybe I am not
13 framing it in a way you can understand.

14 But when investors invest in
15 these Alarm Contracts, they are
16 expecting promise to receive a certain
17 return. Now, what I want to know is at
18 the time the LLCs invested or buy out
19 the interest in SPTC4 -- SPT4, had the
20 payments been made as promised in the
21 prospectus?

22 THE WITNESS: Yes.

23 MR. NEWMAN: The payments
24 weren't behind or there weren't lesser
25 payments being made?

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DAVID SMITH

THE WITNESS: No.

MR. NEWMAN: Or reduced amount
being paid?

THE WITNESS: No.

MR. NEWMAN: Why is this not
considered to be an affiliated
transaction given the fact that McGinn
Smith Capital Holdings is the trustee of
the alarm -- for the Alarm Contracts?
Why is that not considered to be an
affiliated transaction?

THE WITNESS: When you refer
to affiliated transaction --

MR. NEWMAN: Do you consider
this to be an affiliated transaction?

MR. FRANCESKI: You mean for
the collateral mortgage?

THE WITNESS: No. We don't
have any ownership, we have no
beneficial -- economic benefit from
owning it. So it's not considered -- I
guess as you're defining an affiliate,
whether we had an economic stake in the
company, in which case that was the

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DAVID SMITH

defining -- the 20 percent was sort of
the defining -- is that where we are,
talking about the collateral?

MR. NEWMAN: Right.

THE WITNESS: No, we had no
economic benefit in that whatsoever.

MR. NEWMAN: And who made the
determination or who was able to act on
behalf of SPT4 and sell that interest to
the LLC? Who represents the SPT4
contract?

THE WITNESS: The note
holders -- that basically either are
represented by the trustee or they are
represented by the fact that they had
reached maturity, in which case there's
really not a decision.

MR. NEWMAN: Well, in this
case who made the decision on behalf of
SPT4 Alarm Contract holders to sell
their interest to the LLC?

THE WITNESS: The trustee
represented them.

MR. NEWMAN: And that's McGinn

1 DAVID SMITH

2 Smith Capital Holdings?

3 THE WITNESS: SPT4, my
4 recollection, I am quite certain of
5 this, is that there was not a decision
6 to be made that the asset had matured.
7 The contracts would be sold to, in
8 effect, meet the maturity or meet the
9 obligation and therefore the trustee
10 acts on their behalf to sell those
11 contracts.

12 MR. NEWMAN: So the trustee
13 made the decision to sell the contracts
14 to the LLC?

15 THE WITNESS: Yeah, the
16 trustee for the notes.

17 MR. NEWMAN: And the trustee
18 is McGinn Smith Capital Holdings?

19 THE WITNESS: To the best of
20 my recollection.

21 MR. NEWMAN: And that was you?

22 THE WITNESS: McGinn Smith
23 Capital Holdings.

24 MR. NEWMAN: You, you're
25 McGinn Smith Capital Holdings?

1 DAVID SMITH

2 THE WITNESS: I am an officer
3 of McGinn Smith Capital Holdings.

4 MR. NEWMAN: Who made the
5 decision in this particular instance to
6 sell the Alarm Contracts to the LLC?

7 THE WITNESS: The decision was
8 made, but I guess I am not articulating
9 myself very well. The investment in
10 SPT4 had matured, so it's not a
11 decision. They have to be sold. They
12 have to basically -- to return the money
13 to the investors --

14 MR. NEWMAN: Right.

15 THE WITNESS: -- they have to
16 be sold. So you go out into the
17 marketplace and you sell them.

18 MR. NEWMAN: Right, and you
19 don't have to sell this to the LLC? It
20 can be sold to anybody?

21 THE WITNESS: That is correct.

22 MR. NEWMAN: You made the
23 decision on behalf of McGinn Smith
24 Capital Holdings to sell these contracts
25 to the LLC?

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DAVID SMITH

THE WITNESS: That is correct.

MR. NEWMAN: And you as the
advisor of the LLC made the
determination to invest in these
contracts?

THE WITNESS: That is correct.

MR. NEWMAN: Do you see any
conflict of interest in that?

THE WITNESS: No, no more than
happenings on Wall Street every day.

MR. NEWMAN: What does that
mean?

THE WITNESS: That means it's
the nature of the business. When
underwriters raise money, raise capital,
they get warrants, they get stock. It
is the way the business works.

MR. NEWMAN: Doesn't it have
to be disclosed? Aren't conflicts of
interest supposed to be disclosed?

THE WITNESS: We have all
sorts of disclosures in our PPM that we
will buy and sell securities that are
affiliated with McGinn Smith, as long as

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DAVID SMITH

the prices are fair market value, and
it's not being done at any price greater
than fair market value, it's totally
appropriate. It's right there in the
prospectus. So it was disclosed.

MR. NEWMAN: Did McGinn Smith
Capital Holdings receive any fees,
compensation in connection with the sale
of the Alarm Contracts to the LLC?

THE WITNESS: No.

MR. NEWMAN: At the time the
LLC invested in the Alarm Contracts,
were any of the Alarm Contract holders
or investors complaining to McGinn Smith
Capital Holdings about their investment
or inquiring about what was going to
happen with their investment or anything
like that?

THE WITNESS: No.

MR. NEWMAN: From what you
could determine, the investors were
satisfied?

THE WITNESS: Very satisfied.

MR. NEWMAN: Listen to my

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DAVID SMITH

Q And did you do any raises for JV
outside of the bridge loan?

A No.

Q And that's currently been not paid?

A That is correct.

Q Raging River?

A Raging River was an entity out of
North Carolina -- let me think a minute -- in the
basically wholesale clothing business, imported soft
goods, primarily sweat shirts, T-shirts. Went
through a dying process, then sold them to major
retailers.

Deal was brought to me by Mike Lash,
who I can't remember exact relationship, but he had a
relationship with the party. Mike used to work at
Fleet Bank of Boston, and I think maybe he dealt with
them through that. I don't remember. At any rate,
we advanced that money, had personal guarantees.
That will be written off -- was written off by
this -- I am not sure exactly when it was written
off, but if it hasn't been, it should be. I think it
was. I think it was written off, you know, virtually
about two years after we made the loan.

Q And what about RTC?

1 DAVID SMITH

2 A RTC is more Alarm Contracts, pool of
3 contracts that we bought.

4 Q And what's the -- so now, again, so
5 McGinn Smith Advisors or McGinn Smith Capital
6 Holdings is the managing member?

7 A Yeah, I guess -- no, I don't know who
8 is the managing member of that. I mean, we sort of
9 control it through -- we service the account. I
10 don't know if there is any direct ownership, but I
11 think we have taken -- that was -- that was a piece
12 of a spinoff of a group that went with a public
13 company, and I think, again, it was a grantor trust.
14 I don't know if we have any direct ownership. I
15 don't -- I just don't know.

16 Q How does this differ -- rather than
17 going through a whole host of questions, how does
18 this differ than the SPT4?

19 A Only that it was a partial piece, and
20 you're testing my memory really well, but I believe
21 that RTC was originally part of a much larger piece
22 that was sold to -- or not sold to, but was absorbed
23 by integrated alarm when it went public in 2003.

24 And I think there was a remaining
25 piece with a particular dealer, and I think that

DAVID SMITH

remained in the RTC Trust, didn't get sold. I think 85 percent of it got sold to IASG, and I think this represented 15 percent, and, you know, it's performed reasonably well, it's amortizing out. It is a group of contracts.

Q What is the current status?

A It's current.

Q Okay. On this document a few lines down we will see alarm, what looks to be contracts, but it was cut off, of 3 million 7.

Do you know what that is?

A It looks like it's probably part of the SPT groups that we bought and the amortized amount. That would be my guess.

Q And what is the current status of that?

A It's amortizing, paid.

MR. RATTINER: I think that's all we have with this. We are done with that exhibit at this point.

I am going to introduce Exhibit Number 3.

(Whereupon Exhibit 3 is Marked.)

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DAVID SMITH

interest to, or when the corporation is
in need of capital and calls for the
money back.

MR. NEWMAN: Has this been
reported as income on your tax return?

THE WITNESS: It is not
income. It is a loan.

MR. NEWMAN: Were you aware of
any IRS rules dealing with when loans
are considered to be income versus a
loan?

THE WITNESS: Yes, when they
are forgiven.

MR. NEWMAN: Is that your
understanding of when you have to report
a loan?

THE WITNESS: It's my
understanding, my accountant's
understanding, both, yes.

MR. NEWMAN: And you consult
with your accountant about that issue?

THE WITNESS: I have.

MR. NEWMAN: When did you
consult him?