

1 DAVID SMITH  
 2 tranches at each of those given times,  
 3 and what you will see, is you start in  
 4 '03, when the offering is first being  
 5 done, obviously it would be something  
 6 considerably less than 20 million.  
 7 It will eventually reach, I  
 8 believe, 20 million and stop, and then  
 9 subsequent to that, there will --  
 10 whether it was resales or not, you know,  
 11 I don't know the answer. I mean, I  
 12 don't have that data available.  
 13 Certainly one of the possibilities.  
 14 And the other possibility, you  
 15 know, is that maybe -- maybe they were  
 16 putting deposits from investments  
 17 instead of having an -- maybe they  
 18 didn't open an operating account yet. I  
 19 just don't know. That's seven years  
 20 ago. But, you know, you cannot take the  
 21 cumulative deposits after the offering  
 22 has been completed and add them to the  
 23 total subscription amount. That's what  
 24 Mike was doing. It's not correct.  
 25 MR. JAGGS: I have one quick

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1 DAVID SMITH  
 2 question before we break for lunch.  
 3 BY MR. JAGGS:  
 4 **Q If a shareholder wanted to retitle --**  
 5 **I want to shift interest in one of the LLCs, were**  
 6 **they required to fill out a new subscription**  
 7 **agreement and a new purchaser questionnaire?**  
 8 A When you say retitle, you mean  
 9 transfer within family or something?  
 10 **Q Yes.**  
 11 A I don't know the answer to that.  
 12 That is a good question. I mean, if it was -- it  
 13 probably should have if it -- you mean, like it went  
 14 from John Jones to John Jones IRA for the benefit of;  
 15 is that what you are thinking of?  
 16 **Q Yeah, or also say there was an**  
 17 **elderly couple that had owned a LLC jointly, one**  
 18 **passed away?**  
 19 A One passed away, no, I don't think in  
 20 that -- that is a good example. I don't think in  
 21 that case we got a new subscription document. I  
 22 think what Patty did was indicated exactly what  
 23 happened because I know there's plenty of instances  
 24 where that has happened, not plenty but a few.  
 25 And it would be then re-registered.

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1 DAVID SMITH  
 2 She would actually re-register the certificate from  
 3 John and Mary Jones to -- we always know it's going  
 4 to be Mary that survives, so it would be Mary Jones.  
 5 **Q So then on Miss Sicluna's investor**  
 6 **list, would it then go from the joint ownership to**  
 7 **the individual ownerships so they would only be**  
 8 **reflected once?**  
 9 A That is correct. That is correct.  
 10 And her final register, that's right, there should  
 11 be -- she would have a record -- maybe I  
 12 misunderstood your question. She would have a record  
 13 of the original investment as joint, but then she  
 14 would show it as re-registered, and in terms of the  
 15 amount, assuming that there was no change in the  
 16 subscription amount, the dollars would stay the same.  
 17 MR. NEWMAN: The only thing I  
 18 have is information request. Staff  
 19 would like to request, again, pursuant  
 20 to Rule 8210, that the firm provide the  
 21 Access Database that we have been  
 22 referring to in the last day and a half.  
 23 THE WITNESS: The entire  
 24 Access?  
 25 MR. NEWMAN: Yeah, actually,

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1 DAVID SMITH  
 2 in a readable CD format so we can look  
 3 at it.  
 4 MR. FRANCESKI: Put it in  
 5 writing, and we will certainly consider  
 6 it.  
 7 MR. RATTINER: Similar to what  
 8 you did with the Quicken file.  
 9 MR. FRANCESKI: Put it in  
 10 writing, we will consider.  
 11 MR. NEWMAN: Okay. Let's take  
 12 a break.  
 13 (Whereupon a Recess is Taken.)  
 14 BY MR. JAGGS:  
 15 **Q We are back on the record. At this**  
 16 **point Staff would like to go back to a few**  
 17 **subscription agreements and just try and clear up a**  
 18 **few things.**  
 19 A Sure.  
 20 MR. JAGGS: So at this point  
 21 Staff is going to introduce Exhibit 15.  
 22 It is a subscription agreement for  
 23 Werner Paul and his purchase of a  
 24 \$50,000 First Excelsior Junior Note on  
 25 July 7, 2008, and it's Bates stamps are

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1 DAVID SMITH  
2 MGS 0004426 to MGS 0004410.  
3 (Whereupon Exhibit 15 is  
4 Marked.)

5 MR. FRANCESKI: And who else  
6 is in the room that wasn't here before,  
7 a gentleman new to us?

8 MR. JAGGS: We have a special  
9 guest, Robert McCarthy.

10 THE WITNESS: (Reviewing).  
11 BY MR. JAGGS:

12 **Q Mr. Smith, do you recognize this**  
13 **document?**

14 A I recognize the document, yes.

15 **Q And can you please explain why you**  
16 **recognize the document?**

17 A It is a subscription agreement for  
18 the purchase of First Excelsior notes which we had  
19 used many times.

20 **Q Okay. The customer is [REDACTED]**  
21 **Do you know Mr. [REDACTED]?**

22 A I do not.

23 **Q If you look at -- when you look**  
24 **through the document, it appears that Mr. [REDACTED]**  
25 **invested \$50,000 in a First Excelsior Junior Note in**

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1 DAVID SMITH  
2 thought it was post-January of '08,  
3 maybe it wasn't until October '08, but  
4 we basically would not take new  
5 subscriptions as a result of the  
6 restructuring or as a result of the  
7 reduction of interest.

8 So what Gary is referring to,  
9 I believe, in terms of re-titling,  
10 certainly the way I interpreted it, I'd  
11 mentioned earlier in my testimony, that  
12 there were times when people  
13 intra-family or IRA to regular account,  
14 or something that they had a basically  
15 no diminution in their interest or no  
16 diminution in value for what they  
17 already owned was deemed to be an  
18 acceptable trade. So I don't know if  
19 that's the case, but if it wasn't the  
20 case, I would suggest it was --  
21 shouldn't have been done.

22 MR. NEWMAN: So were there any  
23 situations where a customer was allowed  
24 to invest after the restructuring was  
25 initially presented?

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1 DAVID SMITH  
2 **July 2008; is that correct?**

3 A That's what it would suggest here,  
4 yes.

5 **Q Do you know whether this is being**  
6 **retitled or is an actual new purchase?**

7 A I don't. I am hoping it's being  
8 retitled, but I don't know.

9 **Q If it was a new purchase and Mr. [REDACTED]**  
10 **paid \$50,000, do you think that's fair to Mr. [REDACTED]?**

11 A I do not.

12 MR. NEWMAN: Why is that?

13 THE WITNESS: Because at that  
14 time that's post the reduction and  
15 interest being paid on the juniors, and  
16 so it would be difficult to argue that  
17 it was worth full value.

18 MR. NEWMAN: Well, even -- we  
19 are talking about re-titling. To make  
20 sure I understand, that scenario that  
21 would be a situation where somebody was  
22 buying interest and somebody had  
23 redeemed prior to maturity?

24 THE WITNESS: No. At some  
25 point, and I don't know if it was -- I

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1 DAVID SMITH  
2 THE WITNESS: Other than the  
3 -- other than the intra-trades, unless  
4 somebody did it at something less than  
5 50,000 -- we are using this example,  
6 unless they did it something less than  
7 par amongst, again, client base, and  
8 even then we highly discouraged it, for  
9 obvious reasons.

10 We had both taken the position  
11 publicly and certainly with our brokers,  
12 it was very difficult to value these,  
13 and that when you traded them at a  
14 discount, the only thing we knew for  
15 sure is that somebody was paying the  
16 wrong price.

17 I don't know the buyer or  
18 seller, but when you weren't able to get  
19 a good value on those in that time  
20 frame, we -- we not only discouraged it,  
21 it was a prohibitive practice. So I  
22 don't -- I am hoping this was a retitle  
23 because I don't -- it shouldn't have  
24 been approved.

25 MR. NEWMAN: Were there

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1 DAVID SMITH  
2 resales in 2006?  
3 THE WITNESS: In '06, I am  
4 sure there were, yeah.  
5 MR. NEWMAN: And those  
6 customers or investors were given a  
7 prospectus?  
8 THE WITNESS: Yes.  
9 MR. NEWMAN: Was the  
10 prospectus amended to reflect any change  
11 in the operations of the LLCs or the  
12 status of their investments?  
13 THE WITNESS: No.  
14 MR. NEWMAN: Why is that?  
15 THE WITNESS: Because it was a  
16 secondary market sale. We gave them a  
17 prospectus to basically make sure that  
18 they understood the risk and understood  
19 the general makeup of the LLC, but it  
20 was not a new subscription, therefore it  
21 didn't require a new prospectus.  
22 MR. NEWMAN: Just so we  
23 discussed the actual mechanics of those  
24 resales, the customer X said they were  
25 in the First Albany LLC and a \$20,000

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1 DAVID SMITH  
2 investment, and they were selling or  
3 redeeming prior to maturity, customer X  
4 would sell their note to First Albany?  
5 THE WITNESS: I don't mean to  
6 be corrective. You are thinking First  
7 Advisory, I guess, right?  
8 MR. NEWMAN: First Advisory.  
9 THE WITNESS: The only reason  
10 I draw that distinction is First Albany  
11 was a brokerage firm of some reputation.  
12 MR. NEWMAN: Just trying to  
13 get to the mechanics.  
14 THE WITNESS: The mechanics  
15 would be, and, again, depending on the  
16 circumstances, which tranche, but  
17 generally it would be sold into the  
18 operating account of the LLC, and the  
19 operating account, using its liquidity,  
20 would buy it, and then if it was being  
21 re-sold, it would be re-sold to the new  
22 buyer out of the operating account.  
23 MR. NEWMAN: The funds from  
24 the new buyer would be transmitted  
25 directly to the LLC?

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1 DAVID SMITH  
2 THE WITNESS: To the operating  
3 account.  
4 MR. NEWMAN: Operating  
5 account. And you said it was on an  
6 amended Private Placement Memorandum  
7 provided to those resale customers. Was  
8 there any disclosure given to them by  
9 the LLCs about the current status of the  
10 LLCs from either an operational or  
11 investment standpoint or any other  
12 standpoint?  
13 THE WITNESS: Nothing that we  
14 provided other than what the broker  
15 might have said.  
16 MR. NEWMAN: And you knew as  
17 of 2006, based on your testimony  
18 yesterday and what we have seen in the  
19 way of the portfolio analysis, that some  
20 of the investments in the LLCs were  
21 non-performing or had been written off  
22 as of 2006?  
23 THE WITNESS: As of 2006, our  
24 position was and is, is that through the  
25 basic fall, later months of 2007,

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1 DAVID SMITH  
2 really, December of '07, we were very  
3 comfortable that the LLCs would perform.  
4 MR. NEWMAN: Notwithstanding  
5 what we discussed yesterday?  
6 THE WITNESS: Notwithstanding  
7 that there were a few write-downs and  
8 write-offs, that's correct.  
9 MR. NEWMAN: And we went  
10 through those yesterday?  
11 THE WITNESS: We went through  
12 a number of them, sure.  
13 MR. NEWMAN: The, we'll call  
14 them the resale purchasers, advised of  
15 those specific facts concerning the  
16 underlying investments in the LLCs?  
17 THE WITNESS: I don't know  
18 what the broker indicated. I doubt it  
19 because through the period that I just  
20 indicated, all of the funds were  
21 performing. That was the basis that we  
22 took. We felt comfortable that within  
23 the allotted time frame everything would  
24 eventually be okay. Wasn't until the  
25 latter part of '07 that our concern

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1 DAVID SMITH  
 2 picked up and it became a dramatic.  
 3 MR. NEWMAN: Why wasn't that  
 4 information disclosed to the resale  
 5 purchasers prior to the restructuring  
 6 period?  
 7 MR. FRANCESKI: Objection,  
 8 asked and answered.  
 9 THE WITNESS: I just said we  
 10 didn't have any concern for the ultimate  
 11 safety or the ability to pay the  
 12 allotted interest.  
 13 MR. NEWMAN: Even though  
 14 several of the underlying investments  
 15 were not performing as you had  
 16 anticipated?  
 17 MR. FRANCESKI: Objection,  
 18 asked and answered.  
 19 THE WITNESS: Every asset  
 20 manager of this sort has -- you are  
 21 going to have expectations of losses,  
 22 and you are going to have expectations  
 23 of winners, and at that time felt on a  
 24 net basis everything was fine.  
 25 MR. NEWMAN: Well, let me ask

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1 DAVID SMITH  
 2 you this, if in January of 2006 all of  
 3 the LLC investors wanted to redeem their  
 4 notes, would the LLC have had sufficient  
 5 funds, based on the investments that had  
 6 been made up to that point, to repay the  
 7 full principal amount back to those  
 8 customers?  
 9 THE WITNESS: Well, first of  
 10 all, all the investors weren't entitled  
 11 to redeem.  
 12 MR. NEWMAN: Even if the  
 13 ones -- say -- well, what is to say one  
 14 or more of the tranches wanted to  
 15 redeem, were there sufficient funds to  
 16 redeem?  
 17 THE WITNESS: It is not one or  
 18 more of the tranches. The only tranche  
 19 that would have had the right to redeem  
 20 would be the seniors. If the seniors  
 21 had sufficient assets to cover them,  
 22 there would be no concerns. So as long  
 23 as, theoretically, just 25 percent of  
 24 the portfolio was sufficient, one could  
 25 take that position.

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1 DAVID SMITH  
 2 I wouldn't take that position  
 3 if it was only 25 percent, but I  
 4 testified yesterday that it was our  
 5 belief at the end of '07 -- portfolio  
 6 values in the aggregate, there was  
 7 little difference between some of the  
 8 funds -- approached 73 percent.  
 9 So if one of the seniors  
 10 desired to redeem in '07, we would not  
 11 have had any concern that they would  
 12 have been capable of doing that. The  
 13 other tranches did not have the right to  
 14 redeem. If a substantial amount of the  
 15 third tranche, the equity tranche, the  
 16 10 and a quarter tranche, whatever you  
 17 want to call it, wanted to do that, and  
 18 a new investor was coming on board, he  
 19 would have been advised and we wouldn't  
 20 have let that happen.  
 21 MR. NEWMAN: Well, let me ask  
 22 it another way. As of January 2006, how  
 23 much total money had been raised from  
 24 the four offerings, approximately?  
 25 THE WITNESS: Approximately 85

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1 DAVID SMITH  
 2 million.  
 3 MR. NEWMAN: Did the aggregate  
 4 amount of the investments held in those  
 5 LLCs approximate \$85 million.  
 6 THE WITNESS: No.  
 7 MR. NEWMAN: And this is  
 8 January of '06 we are talking about?  
 9 THE WITNESS: That is correct.  
 10 MR. NEWMAN: What would be the  
 11 approximate value of the investments as  
 12 of January '06?  
 13 THE WITNESS: Probably  
 14 85 percent.  
 15 MR. NEWMAN: How about the  
 16 December 2006?  
 17 THE WITNESS: Maybe  
 18 80 percent, 82 percent. A year later  
 19 it's at 73, so I am just extrapolating,  
 20 and I shouldn't be guessing.  
 21 MR. NEWMAN: That's fine. I  
 22 understand you're approximating.  
 23 BY MR. JAGGS:  
 24 Q Mr. Smith, if you look to Bates Stamp  
 25 MGS 0004409, the first page of the questionnaire for

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1 DAVID SMITH

2 Werner Paul.

3 A I have 4426, Gary.

4 MR. FRANCESKI: It's in there.

5 They are not in Bates order.

6 BY MR. JAGGS:

7 Q Sorry about that.

8 A Okay.

9 Q On 4409, the bottom of the page, it  
10 appears to be that there's a little small line  
11 through the 500,000 to the one million?

12 A Yes.

13 Q And then has an X by greater than one  
14 million, and it states, updated per conversation,  
15 7-17-08, and it appears to be FHC.

16 Do you know who FHC is?

17 A I believe that would be Frank  
18 Chiappone, is a broker and more likely than not the  
19 broker for Mr. [REDACTED]

20 Q And did the firm have any procedures  
21 when information was being changed on the purchaser  
22 questionnaire, specifically requiring that the  
23 questionnaire be sent back to the customer for an  
24 additional signature?

25 A No. I think the procedure was, is

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1 DAVID SMITH

2 that information had to be updated in his file, on  
3 his New Account form, and there was sort of a push  
4 about that time, I think, by the FINRA and others  
5 that there be a, you know, more current update for  
6 all of the accounts, and I think at that time we were  
7 going through it.

8 I don't know what might have  
9 motivated Mr. Chiappone, whether it was regarding  
10 this particular offering or whether he had, in  
11 following that procedure for, you know, a number of  
12 accounts, including Mr. Werner, he just happened to  
13 have updated it and then as a result of that, when  
14 Mr. [REDACTED] -- not Mr. Werner, excuse me, when Mr. [REDACTED]  
15 was making the purchase, he updated -- could have  
16 been that the thing came back and Mr. Chiappone  
17 referred to him and talked about the situation.

18 As I said many times, investors  
19 either made mistakes or didn't understand what they  
20 were doing, and oftentimes the broker would clarify  
21 and, you know, to that point, he's initialed it and  
22 indicated he had a conversation on 7-17. And knowing  
23 Mr. Chiappone as I do, that would be sufficient.

24 MR. NEWMAN: Well, so you  
25 understand what updated per conversation

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1 DAVID SMITH

2 means by reading this?

3 THE WITNESS: Yes.

4 MR. NEWMAN: Your  
5 understanding is what?

6 THE WITNESS: That the  
7 indication that he had a net worth in  
8 the 500 to a million dollar range.  
9 There's a line through it greater than a  
10 million is now indicated, and  
11 Mr. Chiappone has initialed that change.

12 MR. NEWMAN: Do you know why  
13 there's not a checkmark next to the  
14 500,000 to \$1 million line under  
15 approximate net worth?

16 THE WITNESS: I think it was  
17 whited out. Looks to me like it was  
18 whited out, and, you know, changed and  
19 then initialed, so that Mr. Chiappone is  
20 initialing the change, which is  
21 appropriate.

22 MR. NEWMAN: The broker is but  
23 the customer is not initialing that?

24 THE WITNESS: That is correct.

25 MR. NEWMAN: And so the firm

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1 DAVID SMITH

2 did not have a requirement that when  
3 there was a change made to the purchaser  
4 questionnaire, that the purchaser -- the  
5 investor had to initial or acknowledge  
6 the change in writing?

7 MR. FRANCESKI: Objection,  
8 asked and answered.

9 THE WITNESS: Not that I am  
10 aware of, no. This is sufficient.

11 MR. NEWMAN: Now, in looking  
12 at this questionnaire, looking at the  
13 second page, this individual has  
14 indicated that they have an approximate  
15 gross income of 25,000 to 100,000. Do  
16 you see that?

17 THE WITNESS: I do.

18 MR. NEWMAN: And their gross  
19 income is 35 to a hundred, on five?

20 THE WITNESS: That will be for  
21 the preceding or for that particular  
22 calendar year, yes.

23 MR. NEWMAN: And yet their  
24 approximate net worth, according to  
25 brokers' initials, is greater than \$1

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1 DAVID SMITH  
 2 million?  
 3 THE WITNESS: (Nodding Head).  
 4 MR. NEWMAN: You need to  
 5 answer audibly. You shook your head.  
 6 THE WITNESS: You didn't ask  
 7 me a question yet. You shook your head.  
 8 MR. NEWMAN: Well, I asked you  
 9 do you see that?  
 10 THE WITNESS: I do see that.  
 11 MR. FRANCESKI: That's what  
 12 the question was.  
 13 MR. NEWMAN: As a compliance  
 14 officer and supervisor, does that raise  
 15 any red flags or questions in your mind,  
 16 given the disparity from the net worth  
 17 or the income from this customer?  
 18 THE WITNESS: It might, but  
 19 it's not unusual. Client could be  
 20 retired, getting just investment income  
 21 and have substantial net worth.  
 22 MR. NEWMAN: And at the point  
 23 you initialed or signed off on this, on  
 24 July 7th, 2008, according to the last  
 25 page?

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1 DAVID SMITH  
 2 THE WITNESS: That is correct.  
 3 MR. NEWMAN: So would that  
 4 have been a date you reviewed this  
 5 paperwork?  
 6 THE WITNESS: Well, it was  
 7 indicated that on -- that doesn't look  
 8 like my writing, the 7th day of July, so  
 9 that might have been the day that it was  
 10 sent to me. I might have signed it  
 11 subsequent. I might have sent it back  
 12 when the client didn't have an  
 13 accredited net worth, might have asked  
 14 for an explanation, in which case Mr.  
 15 Chiappone might have contacted the  
 16 client and indicated that, per his  
 17 conversation, that he was comfortable  
 18 that he had a net worth in excess of a  
 19 million dollars. Any of those  
 20 possibilities exist. I don't --  
 21 MR. NEWMAN: But right now  
 22 looking at the document, it says you  
 23 accepted this on July 7th, 2008?  
 24 THE WITNESS: That is correct,  
 25 yes.

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1 DAVID SMITH  
 2 MR. NEWMAN: And according to  
 3 the first page of this questionnaire,  
 4 the update was made on 7-17-08?  
 5 THE WITNESS: That is correct.  
 6 MR. NEWMAN: Was there any  
 7 procedure that McGinn Smith had  
 8 regarding revisions or changes to a  
 9 questionnaire made after the time in  
 10 which you had signed it on behalf of the  
 11 firm that required the individual making  
 12 the change or update to notify you of  
 13 the same?  
 14 THE WITNESS: No, but, I mean,  
 15 I've put forth what I think happened  
 16 here is because that's not my writing,  
 17 my guess is this came down to me on  
 18 July 7th. I didn't -- probably didn't  
 19 sign it then, probably sent it back, got  
 20 the update, and then signed it.  
 21 I mean, the 7th of July is not  
 22 my writing. The signature is.  
 23 MR. NEWMAN: Are you  
 24 speculating or do you know that for a  
 25 fact?

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1 DAVID SMITH  
 2 THE WITNESS: I don't know it  
 3 for a fact, but I am offering a  
 4 reasonable theory, not speculation.  
 5 MR. JAGGS: At this time Staff  
 6 would like to introduce Exhibit 16. It  
 7 is a subscription agreement for [REDACTED]  
 8 and [REDACTED] and their purchase  
 9 of a \$50,000 First Advisory Income Note  
 10 on December 6th, 2005 and the Bates  
 11 stamps are MGS 0001389 to MGS 0001393.  
 12 (Whereupon Exhibit 16 is  
 13 Marked.)  
 14 THE WITNESS: (Reviewing).  
 15 BY MR. JAGGS:  
 16 Q Mr. Smith, do you know [REDACTED] or  
 17 [REDACTED]?  
 18 A I do not.  
 19 Q If you look on page Bates stamp MGS  
 20 0001391, is that your signature on the bottom of the  
 21 page?  
 22 A I believe it is, yes.  
 23 Q And is that your handwriting for the  
 24 date December 6th?  
 25 A Does not look like my handwriting,

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1 DAVID SMITH  
2 no.  
3 **Q Do you recognize whose handwriting it**  
4 **is?**  
5 A I do not.  
6 **Q If you go on to the next page, bottom**  
7 **of the page, it appears that the approximate net**  
8 **worth has been changed from 250,000 -- from 250,000**  
9 **to 500,000 to greater than a million, and the**  
10 **initials next to it are -- appears to be PR.**  
11 **Do you know who that might be?**  
12 A I don't.  
13 **Q And on the next page, actually, the**  
14 **last page MGS 0001393, on top, Question Number 2, did**  
15 **your individual income exceed 200,000 in 2003 and**  
16 **2004, or did your joint income with your spouse**  
17 **exceed 300,000 in each of those years, that appears**  
18 **to have been changed from no to yes, also with a PR**  
19 **initial to it, and questions four and five, what was**  
20 **your approximate gross income for calendar year 2003,**  
21 **appears to have been changed from 25,000 to 100,000**  
22 **to 200,000 to 300,000, and that was also the same for**  
23 **number five.**  
24 **Do you recall seeing this purchaser**  
25 **questionnaire when you signed this document?**

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1 DAVID SMITH  
2 A I do not.  
3 **Q Does it concern you that the income**  
4 **and net worth was changed by apparently the**  
5 **representative?**  
6 A I don't recognize who the PR is.  
7 He's initialed it. I would -- there's a magnitude of  
8 change so that would cause some concern. I don't  
9 recall seeing this or having the conversation, and I  
10 am at a loss of who PR is. I apologize for that. I  
11 should know. I assume it is a representative of  
12 ours, but I can't, for the life of me, think of who  
13 it is.  
14 **Q For best practices, when there's been**  
15 **this many changes on a purchaser questionnaire, do**  
16 **you think it should be sent back to the client for**  
17 **signature?**  
18 A Depending on the circumstances. I  
19 mean, certainly should have been discussed with the  
20 broker and see what precipitated those changes,  
21 whether it was a client that was confused, or if  
22 there was just -- you know, depending on the outcome  
23 of that conversation, it might be, it might not be.  
24 MR. FRANCESKI: Gary, do you  
25 mind if I ask a clarifying question?

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1 DAVID SMITH  
2 MR. JAGGS: Sure.  
3 MR. FRANCESKI: PR, could it  
4 be Phil Rabinovich?  
5 THE WITNESS: Could be, yeah.  
6 That's right, it could be.  
7 MR. NEWMAN: Take a look at  
8 the first page of the questionnaire,  
9 1392 on the bottom. What is the  
10 occupation of this individual?  
11 THE WITNESS: Says personal  
12 assistant.  
13 MR. NEWMAN: And PR has  
14 indicated to you the net worth greater  
15 than a million dollars; is that correct?  
16 THE WITNESS: That's what is  
17 indicated there, yes.  
18 MR. NEWMAN: Now, according to  
19 this document it's signed by a customer  
20 or investor on January 22nd, 2006,  
21 second page?  
22 THE WITNESS: Yes.  
23 MR. NEWMAN: And looking at  
24 the acceptance by you, that's dated 6  
25 December 2005. Do you see that?

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1 DAVID SMITH  
2 THE WITNESS: That is correct.  
3 MR. NEWMAN: And it looks like  
4 on the preceding page, 139 on the  
5 bottom, it says the undersigned has  
6 executed the subscription agreement on  
7 the 6th day of December 2005. Do you  
8 see that?  
9 THE WITNESS: I do.  
10 MR. NEWMAN: Can you explain  
11 why there's a discrepancy between those  
12 dates and the two December dates and the  
13 January 22nd, '06 date? Why do the  
14 dates -- why do the dates differ on  
15 these documents?  
16 THE WITNESS: Possibly the  
17 client completed the subscription  
18 agreement on the 6th of December, which  
19 is what he indicates by his signature  
20 and his writing. Again, it would appear  
21 that the date of 6 December on  
22 Exhibit 1391 is the client's writing. I  
23 am not a handwriting expert but I do  
24 know it's not mine.  
25 So quite possibly got to my

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1 DAVID SMITH  
2 desk on that date, and maybe the  
3 questionnaire had not been in receipt  
4 yet, maybe the questionnaire went back  
5 to the client and was dated, you know,  
6 roughly a month and a half later, at  
7 which point I may very well have then  
8 executed it with the original date on it  
9 but I don't know that for a fact.  
10 MR. NEWMAN: Based on the  
11 practice, when you receive the  
12 subscription agreement, do you also  
13 receive the purchaser questionnaire at  
14 the same time?  
15 THE WITNESS: That would  
16 normally be the case, yes.  
17 MR. NEWMAN: And the  
18 requirement was, that when a customer  
19 wanted to invest, they would complete  
20 both the agreement and purchaser  
21 questionnaire at the same time?  
22 THE WITNESS: That is correct.  
23 In some instances if the customer was a  
24 prior customer and we already had one on  
25 file, it might not be required, and if

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1 DAVID SMITH  
2 there was a subsequent change, we would  
3 then require a new one. Those are  
4 possibilities that I don't know with any  
5 certainty.  
6 MR. RATTINER: Would the  
7 customer -- would you receive the  
8 resubmission by the customer of the  
9 January 2006 document?  
10 THE WITNESS: Well, it is a  
11 very unusual set of circumstances,  
12 Chris. Normally, as Mike had said, we  
13 get the questionnaire and the  
14 subscription document together. And I  
15 am -- you know, I'm looking at the dates  
16 and all that went on, and I am just  
17 trying to lay out a scenario that I  
18 can't remember, but normally they would  
19 come in together.  
20 In this case if they came in  
21 separately, we wouldn't accept the  
22 subscription because we need both of  
23 them, so. One theory is maybe the  
24 customer was a prior customer, we had a  
25 subscription agreement on file, and

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1 DAVID SMITH  
2 therefore -- and if the circumstances  
3 had changed, again, I don't know if they  
4 had or why, maybe we requested a new  
5 subscription agreement, or excuse me, a  
6 new questionnaire.  
7 MR. JAGGS: At this point the  
8 staff would like to introduce Exhibit  
9 Number 17.  
10 Exhibit 17 is a subscription  
11 agreement for [REDACTED] for a  
12 purchase of a \$30,000 Third Albany  
13 Income Note -- Third Albany Jr Note on  
14 April 22nd, 2005, and the Bates stamps  
15 MGS 0008309 to MGS 0008313.  
16 (Whereupon Exhibit 17 is  
17 Marked.)  
18 THE WITNESS: (Reviewing).  
19 BY MR. JAGGS:  
20 Q Mr. Smith, do you know [REDACTED]?  
21 A I do not, although the name is  
22 familiar with me, but I do not believe I have ever  
23 met her.  
24 Q If you go to the second page Bates  
25 Stamp MGS 0008310, it appears she, [REDACTED]

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1 DAVID SMITH  
2 dated the page April 13th, 2005; is that correct?  
3 A Well, that is the date on there. I  
4 have no idea what [REDACTED] did because I don't  
5 know.  
6 Q Do you know if it was anybody's  
7 practice in either any of the branches or the main  
8 office to fill in that date if a customer didn't fill  
9 it in?  
10 A I don't know that.  
11 Q If you go to the next page MGS  
12 0008311, is that your signature?  
13 A Again, my signature, not the date. I  
14 don't know whose signature that is.  
15 Q And do you recognize the handwriting  
16 for the date?  
17 A No.  
18 Q If you go to the next page, it is the  
19 purchaser questionnaire Bates Stamp MGS 0008312, and  
20 it appears the approximate net worth has been changed  
21 from 250,000 to 500,000 to greater than a million,  
22 and it appears to be initialed FHC; is that correct?  
23 A That is correct.  
24 Q Do you recall having any conversation  
25 with Frank Chiappone regarding this document?

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1 DAVID SMITH

2 A I don't. I believe the client may be  
3 the wife of one of his other clients who has a  
4 substantial net worth, but I don't know that for a  
5 fact, and I don't recall having the conversation with  
6 Mr. Chiappone.

7 Q And the last page it appears that  
8 [REDACTED] signed the second page of the  
9 questionnaire on April 12th, 2005; is that accurate?

10 A Well, again, what appears to be  
11 somewhat of a pattern with clients or else wise that  
12 there's a signature accompanying the date, but  
13 whether they were done on the same day, whether the  
14 client dated it, you are asking me to speculate. I  
15 don't know. Certainly, the date is there and her  
16 signature is there. Whether they were done at the  
17 same time, I don't know.

18 MR. NEWMAN: Looking at this  
19 document now, does it raise any  
20 supervisory concerns or questions for  
21 you?

22 THE WITNESS: Well, again, I  
23 know Frank Chiappone. He's worked with  
24 us for 20 years. He's, you know, a very  
25 thorough, honest broker, and anything

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1 DAVID SMITH

2 that has his initials by it, I would not  
3 normally raise any reservations about.

4 The pattern of the dates here  
5 and the different signatures for the  
6 dates, you know, just don't seem to  
7 be -- seem to be any pattern or  
8 consistency. I mean, we have got  
9 basically Miss [REDACTED] presumably signing  
10 the subscription date as the date on one  
11 document on the 22nd, and on another  
12 date the 13th.

13 Once in a while a  
14 questionnaire might come in at a  
15 different time than a subscription  
16 document, but I can't imagine that this  
17 page -- all subscribers must complete  
18 this page -- and the actual subscription  
19 date would come in different. So I  
20 don't know how to explain that.

21 MR. NEWMAN: How about the  
22 fact that this is an RN psychotherapist  
23 whose gross income is 25 to a hundred  
24 thousand dollars a year who has a net  
25 worth greater than one million,

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1 DAVID SMITH

2 according to the revision?

3 THE WITNESS: I did mention a  
4 few moments ago, without certainty, but  
5 certainly a possibility. The name  
6 [REDACTED] rings a bell. I think it is a  
7 very substantial customer in the Glen  
8 Falls area that could very well be --  
9 this is her -- or she is the wife of  
10 that Mr. [REDACTED], but I don't know.

11 MR. NEWMAN: But the  
12 questionnaire is only for her, correct,  
13 it's in her name?

14 THE WITNESS: Well, it's in  
15 her name but she could have a diminished  
16 income, and a joint tenant with a  
17 husband, she is entitled to get half of  
18 his net worth, and if he's worth \$5  
19 million, she is entitled to suggest she  
20 is worth more than a million.

21 MR. NEWMAN: Is that reflected  
22 on this questionnaire?

23 THE WITNESS: What, that she  
24 is married to a wealthy individual?

25 MR. NEWMAN: Yes.

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1 DAVID SMITH

2 THE WITNESS: No.

3 MR. RATTINER: Mr. Smith, when  
4 you receive this document and you place  
5 your signature on the page where the  
6 signature is required, what else are you  
7 doing with the document? Are you  
8 reviewing the document or are you solely  
9 signing the document?

10 THE WITNESS: No. I review  
11 the document and look for discrepancies  
12 that we talked about. What I don't have  
13 the ability to do, probably never did,  
14 certainly don't anymore, is to remember  
15 whether upon seeing a discrepancy I sent  
16 it back to Mr. Chiappone, and he gave me  
17 an answer and he initialed it, or  
18 whether the subscription document  
19 reflected that and he had a conversation  
20 and got a new questionnaire. I mean, I  
21 just don't have the recollection.

22 MR. RATTINER: Where do the  
23 original questionnaires exist? Where do  
24 they reside?

25 THE WITNESS: They reside in

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1 DAVID SMITH  
 2 our Clifton Park office.  
 3 MR. FRANCESKI: Mike, might I  
 4 follow up with a clarifying question?  
 5 Dave, on Page Bates Number  
 6 8311, the signature page to the  
 7 subscription agreement, there's a date  
 8 on there April 22nd, 2005. Do you see  
 9 that?  
 10 THE WITNESS: I do.  
 11 MR. FRANCESKI: Correct me if  
 12 I am wrong but that is the acceptance  
 13 date by Third Albany of the  
 14 subscription, isn't it? It purports to  
 15 be the acceptance date for the  
 16 subscription, correct?  
 17 THE WITNESS: Correct.  
 18 MR. FRANCESKI: I thought you  
 19 said earlier that you were thinking that  
 20 may be when Miss [REDACTED] signed that  
 21 document. Did I mishear you?  
 22 THE WITNESS: No. I think  
 23 when you look at these documents, it's  
 24 just there's no clear way to determine  
 25 because that's dated the 22nd. This is  
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1 DAVID SMITH  
 2 part of the document. My testimony was  
 3 is that this page would never come in  
 4 separate from these pages.  
 5 MR. NEWMAN: Just so --  
 6 MR. FRANCESKI: The witness is  
 7 referring to Bates Number 8310, bears a  
 8 date of April 13, 2005, I think.  
 9 THE WITNESS: Anything could  
 10 happen but the likelihood --  
 11 MR. FRANCESKI: That's not my  
 12 point. My point is I thought you said  
 13 earlier in your testimony that you were  
 14 thinking the April 22nd date was the  
 15 date [REDACTED] signed that  
 16 particular document?  
 17 THE WITNESS: Well, I did  
 18 because that is not my -- that's not my  
 19 handwriting for the date.  
 20 MR. FRANCESKI: Isn't that on  
 21 the line that is the acceptance date by  
 22 Third Albany rather than the signing  
 23 date by the customer?  
 24 THE WITNESS: Well, that is  
 25 correct, yes.

1 DAVID SMITH  
 2 MR. FRANCESKI: Then why would  
 3 you associate that date with the signing  
 4 customer?  
 5 THE WITNESS: Well, only  
 6 because that's not my handwriting.  
 7 MR. FRANCESKI: Okay.  
 8 THE WITNESS: So I -- I mean,  
 9 she may have signed it, filled it in,  
 10 and then, you know --  
 11 MR. FRANCESKI: Dave, do you  
 12 know whether that's her handwriting?  
 13 THE WITNESS: No, I do not.  
 14 MR. FRANCESKI: Would it not  
 15 be more logical that someone at McGinn  
 16 Smith filled it in or somebody else at  
 17 the LLC filled in the acceptance date  
 18 rather than the customer?  
 19 THE WITNESS: Well, there is a  
 20 pattern here that in virtually every one  
 21 of these that Gary gave me, that the  
 22 date on that line is not my handwriting.  
 23 MR. FRANCESKI: Right. Could  
 24 be somebody else's at McGinn Smith.  
 25 THE WITNESS: Maybe Patty's  
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1 DAVID SMITH  
 2 filling in the date the day she sends  
 3 them out. I don't know. Every time  
 4 it's not my writing.  
 5 MR. NEWMAN: And just so the  
 6 record is clear, you said the date on  
 7 what line, so we need to refer to the  
 8 document?  
 9 THE WITNESS: The date on the  
 10 execution by the subscriber.  
 11 MR. FRANCESKI: That's not the  
 12 execution by the subscriber, Dave. That  
 13 is the accepted line for Third Albany.  
 14 THE WITNESS: That is the  
 15 title. He's asking the title of the  
 16 page.  
 17 MR. FRANCESKI: No. He asked  
 18 what line you were reading the date  
 19 from, which is the accepted on behalf of  
 20 Third Albany line, is it not?  
 21 THE WITNESS: Okay. That is.  
 22 I defer to counsel.  
 23 MR. FRANCESKI: You don't have  
 24 to defer to me. You're the witness. I  
 25 am pointing to what is on the document.

1 DAVID SMITH  
 2 MR. RATTINER: Mr. Smith, are  
 3 there any documents that you accept on  
 4 behalf of the LLC that you would date?  
 5 THE WITNESS: If there wasn't  
 6 a date there, I probably would, yeah, I  
 7 mean --  
 8 MR. RATTINER: Do you recall?  
 9 THE WITNESS: I don't recall  
 10 and certainly might not date them, but,  
 11 you know -- I certainly wouldn't re-date  
 12 it if it was already dated.  
 13 MR. RATTINER: Even if that  
 14 date wouldn't match the date you were  
 15 signing it?  
 16 THE WITNESS: Yeah, I think  
 17 that is a fair assumption.  
 18 MR. JAGGS: Staff will  
 19 introduce Exhibit 18 which is a  
 20 subscription agreement for [REDACTED] and  
 21 [REDACTED] for the purchase of a  
 22 25,000 First Advisory Income Note Senior  
 23 Note dated November 1st, 2005 Bates  
 24 stamped MGS 0002537 to MGS 0002541.  
 25 (Whereupon Exhibit 18 is

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1 DAVID SMITH  
 2 Marked.)  
 3 THE WITNESS: (Reviewing).  
 4 BY MR. JAGGS:  
 5 Q Mr. Smith, do you know [REDACTED] and  
 6 [REDACTED]?  
 7 A I do not.  
 8 Q If you turn to the first page,  
 9 purchaser questionnaire, MGS 0002540, it appears the  
 10 approximate net worth has been changed from a hundred  
 11 thousand to 250,000 to greater than a million.  
 12 Do you recognize any of the initials  
 13 in the net worth box?  
 14 A I do not. Can't even tell you what  
 15 letters they are (Reviewing). I do not.  
 16 Q At the time that you signed the  
 17 subscription agreement did you have any concerns  
 18 regarding [REDACTED] true net worth?  
 19 A I don't recall. Again, the initials  
 20 indicate that there was a discussion, someone took  
 21 responsibility for it so.  
 22 MR. NEWMAN: What is the  
 23 significance of having a \$1 million  
 24 greater net worth in terms of  
 25 determining whether the customer is

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1 DAVID SMITH  
 2 accredited or non-accredited?  
 3 THE WITNESS: If the income  
 4 doesn't meet the qualification, then the  
 5 net worth does, and that is the  
 6 determinative factor.  
 7 MR. NEWMAN: So a million  
 8 dollars or more wouldn't make, under the  
 9 definition of accredited investor, would  
 10 make that investor accredited; is that  
 11 correct?  
 12 THE WITNESS: That is correct.  
 13 MR. NEWMAN: If the  
 14 information had been submitted in the  
 15 original form without the revisions,  
 16 would this customer, based on the  
 17 financial information presented, had  
 18 been classified as an accredited  
 19 investor?  
 20 THE WITNESS: They would not  
 21 have.  
 22 MR. JAGGS: We are going off  
 23 the record. We are going to take a  
 24 couple of minutes and readjust and then  
 25 we will start back up.

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1 DAVID SMITH  
 2 (Whereupon a Recess is Taken.)  
 3  
 4 EXAMINATION  
 5 BY MS. SMITH:  
 6 Q Earlier you testified that Patty  
 7 Sicluna would track the incoming accredited investors  
 8 as far as the subscription agreements?  
 9 A I believe that was kept track by  
 10 Patty through the questionnaires, yes.  
 11 Q Okay. At what point in time did you  
 12 review to see that the accredited investor, the  
 13 number was not exceeded?  
 14 A I think I kept in contact as the  
 15 offering was going on quite regularly.  
 16 Q And was that based on this database  
 17 that Patty Sicluna was maintaining?  
 18 A No. I believe that she, before it  
 19 was put into the database, I think she kept a list as  
 20 the subscription documents and questionnaires came  
 21 through, and then ultimately, of course, the client  
 22 is entered into the database, it's indicated whether  
 23 they are accredited or in some cases not accredited.  
 24 Q So what you are saying is there's two  
 25 tracking mechanisms, one in which she is collecting

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DAVID SMITH

the subscription agreements that would then be passed on to you and that you were signing off on, and then at another point in time there's another tracking of accredited investor, total count?

A No, I don't think that's the way it happened. I think Patty kept a separate list of accredited for a particular offering, okay. Once the offering was completed, that data is put into the database, whether it's done -- I think she puts it in virtually every day that what comes in, but I can't swear to that.

That becomes the permanent database. But to the best of my knowledge, while the process is going on, she has a sort of a separate side thing. Doesn't send it to me. I mean, as I indicated earlier this morning, I am in communication or was in communication with her a lot, you know. And we would want to know where the offering is in terms of sales and if there was any particular problem with the accredited versus non-accredited, any problems with documentation was -- you know, the tickets being done.

I mean, you monitor a lot of things in terms of brokers putting tickets in, where is the

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DAVID SMITH

those might be non-accredited.

**Q At what point in the process were revisions or modifications made to the subscription agreements?**

A Well, you are talking about some of the things that we just saw?

**Q Yes.**

A There's no pattern. I mean, that may have -- that modification may have been before it got to me or it may, as I have indicated earlier, may have been a result of me. You know if I get -- if I get the -- the questionnaire, excuse me, what we are referring to, and it was a discrepancy that, A, didn't make sense or somebody used the term red flag, you know, whatever it might be, I, more likely than not, would contact the broker and say, what is the deal here?

And as I have indicated earlier, sometimes those are filled out by the client. They are sent in. The client in many cases has sometimes two motivations for not filling those out accurately. One is he doesn't think it's that important, he doesn't understand the accreditation thing, or if he's been told he's forgotten, and he doesn't like

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DAVID SMITH

documentation after the ticket. Brokers sometimes like to save orders for themselves, and so we want to make sure that if they have indicated that this is a real ticket, and we give them a certain amount of time to get the subscription document in, then we start to question whether it's a real ticket.

**Q When you say real ticket, are we talking about whether or not the investor is accredited?**

A No, we are talking about to -- during an offering, the offering opens, the brokers have the opportunity to market it, sell it. When they get an order, as I'd indicate this morning, we actually have a ticket, just like you were buying anything else, it goes in.

Patty uses that ticket to, you know, monitor where we are. Subsequent to that ticket we have to get the documentation before we accept the authorization, or, excuse me, accept the subscription. So all I am saying is one of her tasks, along with the accredited investor, is she would keep me informed as to, A, how much has been sold vis-à-vis tickets, and how much has been sold vis-à-vis accepted subscriptions, and how many of

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DAVID SMITH

people to know that he's got a lot of money. There's a lot of people that don't like people to think they are millionaires.

The second thing is and probably more prevalent in regards to these things are, people have no concept, mostly the middle class, that they are worth over a million dollars. They have homes that are virtually paid off. They have a summer home up by Lake George that they bought 25 years ago at 25,000. It's now selling for 700. They have a pension account that they don't even know what the number is. They know they get a payment.

So, you know, they don't think of themselves -- the term millionaire is still a pretty big deal to people, and sometimes they don't think of it. So they send in, and you see levels of income, which we saw in some of these forms, people making fifty to a hundred, and all of a sudden they are a millionaire. And you say, well, that looks like a big disconnect, and it may be a big disconnect, but often it is not a disconnect. People just haven't registered.

So the broker would go back in a conversation, say, you know, Joe, I really think

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1 DAVID SMITH

2 you're underestimating your net worth. Have you  
3 thought about this? Have you thought about that?  
4 Don't you have a house up on Lake George? Yeah.  
5 What do you think it's worth? I don't know. That  
6 sort of thing.

7 **Q Wouldn't that be part of the**  
8 **suitability review that the broker is doing with the**  
9 **customer at the time they are completing out the**  
10 **subscription agreement?**

11 A It would but the subscription  
12 agreement might come in and independently get right  
13 by it, as I indicated earlier. Maybe the mail came  
14 in and he didn't see it. Yes, in his mind the  
15 customer is suitable because he believes and knows,  
16 not just believes, knows that the customer is worth a  
17 million dollars. And all of a sudden the customer  
18 sends it back and it doesn't register with what the  
19 real world is.

20 As I said earlier this morning, I  
21 have seen the same client register as an accredited  
22 investor and an unaccredited investor within a year  
23 and, you know, only one of them is right.

24 **Q So in that situation Patty Sicluna**  
25 **receives the subscription agreement, and she is**

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1 DAVID SMITH

2 **collecting the subscription agreements and sometimes**  
3 **those subscription agreements aren't accurate and**  
4 **that they needed to be revisited --**

5 A Hm-hm.

6 **Q -- and revised?**

7 **So at what point in time does that**  
8 **count -- when are they modified; and then secondly,**  
9 **who's keeping track of the revised documents?**

10 A Well, I think regarding the e-mail,  
11 that was not a regular thing. So, you know, it may  
12 very well have been that I asked Patty. I don't  
13 know. I can't even remember the e-mail. It was  
14 directed to me, so if it was directed to me, I  
15 probably asked for it. And, you know, I might have  
16 asked for it because as we are getting near the end  
17 of the offering, I want to know where we were.

18 So maybe she indicated, well, this is  
19 where we are, and looking at the pure  
20 subscription/questionnaires, we are at 39 instead of  
21 35. Okay. Well, how did that happen? Well, I mean,  
22 a lot of these things come in. I mean, I am doing  
23 them on a daily basis. We are sending them back, and  
24 maybe at the time we sent them back, we were under  
25 35, and then maybe a bunch came in and got over.

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1 DAVID SMITH

2 **entering it into whether it's an Excel spreadsheet or**  
3 **a database of some sort, and that's something we**  
4 **referred to earlier was an e-mail that Patty Sicluna**  
5 **had sent to Dave Rees, I believe it was?**

6 A I can't speak for Patty. I don't  
7 think she enters that data into -- into the database,  
8 I guess for lack of a better word, until the  
9 subscription is signed off on and completed.

10 So I think the process is she matches  
11 up the ticket. She matches up the subscription  
12 document. She matches up the questionnaire, and then  
13 she is not in a position to make decisions as to  
14 whether they are appropriate or not. They get sent  
15 down to by interoffice mail, and that's where I would  
16 review them.

17 Once I reviewed them and signed off  
18 on them, presumably signed off on them, they go back  
19 to Patty, and then Patty, I would believe, submits  
20 that data into the database.

21 **Q So the e-mail that we saw earlier,**  
22 **which implies that the number of accredited investors**  
23 **had exceeded the 35 accredited investors in some of**  
24 **the investment notes, you had said that that number**  
25 **was probably not correct because Patty is just simply**

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1 DAVID SMITH

2 Those are circumstances that I can't  
3 tell. I think the critical part is that somebody is  
4 keeping track of them and watching them and bringing  
5 them to my attention, and if somebody doesn't belong  
6 in there, then we have got to understand why.

7 MR. RATTINER: Does Patty  
8 understand the difference between  
9 accredited and non-accredited?

10 THE WITNESS: Yes.

11 MR. RATTINER: Who told her  
12 what she is looking for with that  
13 regard?

14 THE WITNESS: She's handled  
15 thousands of questionnaires, and the  
16 data is pretty simple, you know, joint  
17 income over 300, income of 200 for last  
18 year and the, you know, upcoming year  
19 and million dollars. So, and, you know,  
20 I don't know if any of the ones we  
21 looked at, I don't recall there was.

22 I know some questionnaires we  
23 actually then have a box of where we  
24 checked whether it was accredited or  
25 non-accredited but Patty -- Patty has

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1 DAVID SMITH  
 2 been with me for 27 years. She knows.  
 3 MR. RATTINER: What about her  
 4 knowledge with regards to Reg D and the  
 5 exception that the 35 would qualify for?  
 6 THE WITNESS: She knows that's  
 7 something that we are looking for, yeah.  
 8 I mean, she can't quote Reg D for you  
 9 but she knows what to look for.  
 10 MR. MCCARTHY: I just want to  
 11 clarify because sitting here I just want  
 12 to make sure I understand everything.  
 13 Can you explain to me a little bit  
 14 better, maybe help me out, how the  
 15 documents are altered and how you check  
 16 for that?  
 17 MR. FRANCESKI: Objection to  
 18 altered, but go ahead.  
 19 MR. MCCARTHY: I am not saying  
 20 they were altered. They are altered  
 21 documents. There is some alteration in  
 22 the document. Can you walk me through  
 23 that a little better because I am a  
 24 little confused?  
 25 THE WITNESS: Well, I guess I

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1 DAVID SMITH  
 2 don't -- on each specific one, I can't  
 3 recall, you know. I mean, I don't think  
 4 there's a pattern. I mean, the fact is,  
 5 is that -- and we will use the word  
 6 altered without suffering the indictment  
 7 of that name, right? Changed document.  
 8 That it may have come in to the broker,  
 9 and the broker had seen that it was, in  
 10 fact, not consistent with what he knew  
 11 the client to be, in the case of the net  
 12 worth, we would spend most of our time  
 13 on that. That's where most of the  
 14 errors are made.  
 15 He may have in one case, with  
 16 Chiappone, he indicated he had had a  
 17 conversation with the client. So a  
 18 reasonable pattern, if you will, would  
 19 be that he called the client and went  
 20 through maybe one of the conversations  
 21 that I just had with Jennifer regarding  
 22 what your real net worth is.  
 23 Client said, oh, yeah, can I  
 24 change it? He changes it, initials it.  
 25 That then finds its way to me. More

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1 DAVID SMITH  
 2 likely than not, I would pick up the  
 3 phone and say, hey, Frank, you got an  
 4 altered questionnaire here, you have  
 5 indicated you had a conversation with  
 6 the client, tell me what the  
 7 conversation was, you know. How is this  
 8 okay?  
 9 Again, going back to my  
 10 example, maybe Frank says, Joe forgot  
 11 that he has a half million dollar house  
 12 on Lake George. Okay. Good enough.  
 13 Another scenario might be that that  
 14 comes in to me and it hasn't been  
 15 changed yet and therefore it goes back  
 16 to the broker.  
 17 In some cases it might -- they  
 18 might send the client a new one and ask  
 19 for one. Maybe if the client is well  
 20 known to the firm, or quite comfortable  
 21 with the change, at that point the  
 22 broker calls and makes a change, and it  
 23 does the initialing. I don't think  
 24 there's any --  
 25 MR. MCCARTHY: I am just

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1 DAVID SMITH  
 2 trying to ask, in your supervision is  
 3 there a pattern? Are they supposed to  
 4 be initialed by the broker?  
 5 THE WITNESS: No.  
 6 MR. MCCARTHY: Not supposed to  
 7 be initialed by the broker? I see a  
 8 little bit of each. In fact, I see a  
 9 lot of each. So tell me how exactly are  
 10 you following this? Is there an initial  
 11 that's supposed to be indicated that  
 12 somebody altered this document or  
 13 documents that aren't initialed? How do  
 14 you know who altered it?  
 15 THE WITNESS: Well, if the  
 16 broker changes it, he's supposed to  
 17 initial it. If he has input to that  
 18 change, he's supposed to initial it. If  
 19 it's not initialed and it's changed,  
 20 more likely than not I will call the  
 21 broker and say, what is going on? And  
 22 he might say, you know, the client  
 23 crossed it out. He made a mistake. He  
 24 checked 250 to 500, and he's really  
 25 worth a million. So he X'd it out and

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1 DAVID SMITH  
 2 checked the new one and signed it. So  
 3 it is the client.  
 4 We do not have a procedure.  
 5 We take things on a case-by-case basis.  
 6 I mean, we are not going to, under those  
 7 circumstances, turn around and send  
 8 another one back to the client and say,  
 9 hey, sign a clean one for us because you  
 10 got this little cross-out here. We have  
 11 some faith in our people. We have some  
 12 understanding that people could possibly  
 13 have made a mistake, but it's certainly  
 14 going to come to my attention one  
 15 scenario or another if there is a change  
 16 out there, and I am going to want to  
 17 know. I am going to want to know why.  
 18 MR. MCCARTHY: As a supervisor  
 19 is there a percentage of documents that  
 20 come to you in an altered state that  
 21 would alarm you, that would be a red  
 22 flag to you?  
 23 THE WITNESS: Yes, if it was a  
 24 high percentage. I mean, I don't think  
 25 there's, you know, a high percentage. I  
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1 DAVID SMITH  
 2 don't know what sample you guys use, but  
 3 I wouldn't think there is a high  
 4 percentage.  
 5 MR. MCCARTHY: What would you  
 6 think would be a high percentage?  
 7 THE WITNESS: I would think  
 8 4 percent would be a high percentage,  
 9 5 percent.  
 10 MR. MCCARTHY: Did you  
 11 document any of these conversations with  
 12 the broker so that someone could look  
 13 back and evidence your supervision?  
 14 THE WITNESS: No.  
 15 MR. MCCARTHY: So there's  
 16 really no way to tell in many of these  
 17 instances if there was ever a  
 18 conversation between you and the broker  
 19 on an altered document?  
 20 THE WITNESS: Well, I guess  
 21 from an evidence standpoint, yeah, but  
 22 that's generally -- as I say, that's the  
 23 way it worked. If there was an altered  
 24 document, even when it was initialed, I  
 25 probably had the conversation because,  
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1 DAVID SMITH  
 2 you know, I want to know why.  
 3 But I am certainly a lot more  
 4 comfortable with an initial from the  
 5 broker that he makes a notation that  
 6 he's had a conversation than I am if it  
 7 comes in with nothing. But no, we  
 8 don't -- I don't document. We don't  
 9 have, you know, recordings, and, you  
 10 know, I don't -- every time I chat with  
 11 a broker, I don't make a memo.  
 12 But, I mean, I think in our  
 13 defense, if it's worth that, you know,  
 14 small firms -- that's not -- I mean my  
 15 focus -- I understand the importance of  
 16 compliance, okay. And I think over  
 17 29 years we have done a reasonably good  
 18 job in that, limited resources.  
 19 But I am a CEO. I am running  
 20 the company. I am doing a million  
 21 things. If I am trying to allocate my  
 22 time to talking to brokers and writing  
 23 up memos and sticking them in files,  
 24 that is not what I do, that's not what I  
 25 am going to do. If that's what I am  
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1 DAVID SMITH  
 2 doing, then I am not doing my job.  
 3 So for the most part our  
 4 brokers have been longtime associates of  
 5 ours, you know. If once in awhile you  
 6 get somebody that doesn't work out or  
 7 that you don't think much of, and  
 8 hopefully moves on or you move them on.  
 9 But Albany New York is not a  
 10 place like some of these big  
 11 Metropolitan areas. I mean, we know our  
 12 people. They are people that stay with  
 13 us for, you know, 10, 15, years. They  
 14 are not guys blowing in and out that we  
 15 don't know who the hell they are, I  
 16 mean, so --  
 17 MR. MCCARTHY: Did you have --  
 18 did you have a procedure or did you feel  
 19 it would be appropriate at some point to  
 20 spot-check some of these documents and  
 21 go directly to the customer?  
 22 THE WITNESS: Go to the  
 23 client, no. The answer is no.  
 24 MR. MCCARTHY: Did anyone in  
 25 your firm in a supervisory position ever  
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1 DAVID SMITH  
2 do that, do such a thing?  
3 THE WITNESS: Call the client  
4 and --  
5 MR. MCCARTHY: -- verify.  
6 THE WITNESS: -- verify  
7 whether his -- no, I don't believe so.  
8 MR. RATTINER: Based on the  
9 system that you had in place, how would  
10 you have been able to detect a pattern?  
11 THE WITNESS: From an  
12 individual broker?  
13 MR. RATTINER: Right.  
14 THE WITNESS: Well, I guess if  
15 we saw it frequently enough, and my  
16 memory was still working within  
17 reasonable limits, the red lights would  
18 go off or the red flags would go off.  
19 If a broker was doing that once every  
20 three years, would I suggest that is a  
21 pattern, no.  
22 I mean, I really don't think  
23 there was a lot of that stuff. I mean,  
24 I can't recall what -- you know, with  
25 exactitude, but if there was something

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1 DAVID SMITH  
2 that was -- you generally know the  
3 broker, and you know whether he's a guy  
4 that likes to, you know, get around the  
5 rules or whether he's, you know, the  
6 real deal, and I'd like to think that  
7 our guys, for the most part, are the  
8 real deal.  
9 MR. RATTINER: You stated two  
10 examples there, one in which there would  
11 have been a change for the document that  
12 you may have sent back to the broker,  
13 and one in which there was not a change.  
14 For the latter, why would you send the  
15 one without a change back to the broker?  
16 THE WITNESS: I think what I  
17 said, Chris, is if there was what  
18 appeared to be a major discrepancy,  
19 there was an example earlier where the  
20 client had an income, I think, between  
21 25 and \$50,000, and he had a million  
22 dollars, I testified that that's highly  
23 possible. I mean, there are people with  
24 substantial net worths. They are  
25 retired. I saw one guy in there, he was

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1 DAVID SMITH  
2 working at H&R Block. He's retired. My  
3 guess is he's killing time and he's  
4 doing some tax returns, you know.  
5 He's making 25 grand. That  
6 doesn't mean he can't be worth a million  
7 dollars. But contrary to that, it also  
8 might raise some questions. Generally,  
9 they are not paying guys at H&R Block a  
10 lot of money, and those guys don't over  
11 time accumulate \$1 million. So that  
12 might be a reason, and it might be, I  
13 would say, most of the time very simply  
14 resolved by you call the client or,  
15 excuse me, call the broker, say Frank,  
16 you're guy is showing 25,000, he's worth  
17 a million, what is the deal? Oh, he's a  
18 former chairman of the board of XYZ.  
19 He's bored to tears. He's worth a  
20 million dollars. Okay, thank you.  
21 That would be satisfactory  
22 enough for me. I would not call the  
23 client and, you know, press upon him as  
24 say I'm questioning his integrity to how  
25 he filled out the questionnaire.

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1 DAVID SMITH  
2 MR. RATTINER: Right. It's on  
3 a similar pattern that the 25 to 50,000  
4 H&R Block employee had a net worth of  
5 255,000, would you question that?  
6 THE WITNESS: Just, period?  
7 MR. RATTINER: In that  
8 example, you are saying if it was at a  
9 million, you might question it based on  
10 the income. But in that specific  
11 instance --  
12 THE WITNESS: No, I wouldn't  
13 because the 250 to 500, as I said  
14 repeatedly, is so easy today. I mean,  
15 the guy who lives in any kind of  
16 neighborhood that he's now 60 years old,  
17 he's owned the house at 25, the mortgage  
18 is paid off. He's got a half a million  
19 dollars in his house, forget anything  
20 else. So, no, those kind of numbers  
21 don't raise a lot of concerns.  
22 MR. RATTINER: So it's usually  
23 on the higher end in terms of if the  
24 customer overstates their income?  
25 THE WITNESS: Yeah, the bigger

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1 DAVID SMITH  
 2 the discrepancy, I mean, you know, it  
 3 just sort of follows.  
 4 MR. MCCARTHY: I want to  
 5 clarify just one other point. For each  
 6 investment, each new investment, would  
 7 you require that the customer send in an  
 8 updated questionnaire?  
 9 THE WITNESS: Sometimes yes,  
 10 sometimes no. I testified earlier that  
 11 customers that we know, that have been  
 12 around for a long time, and we clearly  
 13 know they are accredited, and they have  
 14 made private placements in the past, and  
 15 we have a questionnaire on file,  
 16 generally when the package goes out,  
 17 Bob, it goes out with a questionnaire.  
 18 Okay. There would certainly  
 19 be the potential for some instances  
 20 where the guy said, I am not filling it  
 21 out. I have been doing business with  
 22 you for 20 years. You know who the hell  
 23 I am. He sends back the subscription  
 24 document. The likelihood that we would  
 25 then harass him to give us another one  
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1 DAVID SMITH  
 2 is not likely.  
 3 On the other hand, if it's a  
 4 client that's fairly new to the firm,  
 5 maybe made one investment two years ago  
 6 and now he's making another investment,  
 7 yeah, we would require a new  
 8 questionnaire because circumstances may  
 9 have -- we don't know the guy that well,  
 10 you know, circumstances change, people's  
 11 fortunes.  
 12 MR. MCCARTHY: Is there any  
 13 written criteria anywhere on when you  
 14 would require a questionnaire and when  
 15 you wouldn't require a questionnaire?  
 16 THE WITNESS: I think the  
 17 times that we wouldn't require a  
 18 questionnaire are pretty limited. They  
 19 are pretty much limited to people who we  
 20 know and have known for some period of  
 21 time, you know. You will see in some of  
 22 these things, there's people who have  
 23 had a pattern for 10 or 15 years of  
 24 investing in these things. And they are  
 25 people in the community who we know of  
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1 DAVID SMITH  
 2 to be of means or certainly to be of,  
 3 you know, accredited nature.  
 4 MR. MCCARTHY: So if someone  
 5 is not that well known, I mean, the  
 6 circumstances change from year to year  
 7 to a person?  
 8 THE WITNESS: They could,  
 9 right.  
 10 MR. MCCARTHY: How are you  
 11 judging to making sure that that's still  
 12 suitable?  
 13 THE WITNESS: Well, that's  
 14 what I am saying, those guys we would  
 15 require a new questionnaire. It's only  
 16 the ones that we are very comfortable  
 17 with, that we know, and they have been  
 18 clients of ours for a long time. We  
 19 know their circumstances haven't  
 20 changed. I mean, maybe they are a  
 21 member of your club, you know, maybe  
 22 play some golf with them or whatever.  
 23 Again, it's a different sort  
 24 of environment in these Upstate  
 25 communities. I mean, you are not, you  
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1 DAVID SMITH  
 2 know -- you are not working out of a  
 3 40-story glass building. You had a  
 4 client on the books for 15 years and you  
 5 never met him. I mean, it is just a  
 6 different gig.  
 7 MR. MCCARTHY: Is there any  
 8 amount of time that you would go back  
 9 before requiring to do the  
 10 questionnaire?  
 11 THE WITNESS: Probably -- you  
 12 know, it is a judgment call. There's  
 13 nothing written, there's no, you know,  
 14 absolute thing that we do.  
 15 MR. FRANCESKI: Guys mind if I  
 16 follow up with a follow-up question?  
 17 MR. NEWMAN: Go ahead.  
 18 MR. FRANCESKI: You may have  
 19 just addressed this, Dave, in the last  
 20 day and a half, but it's been a long day  
 21 and a half, but for these particular LLC  
 22 investments, did the brokers have any  
 23 trouble generating sufficient interest  
 24 to fill out the offerings? I know you  
 25 said the fourth one wasn't totally  
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1 DAVID SMITH  
2 subscribed but overall?  
3 THE WITNESS: No. I mean, the  
4 fact was that I did testify to this some  
5 time long ago, yesterday. There was  
6 never a thought -- somebody asked the  
7 question, and probably Chris, how did  
8 this whole concept come about, and we  
9 talked about how I had gotten the idea  
10 in the spring of '03.  
11 In the spring of '03, I didn't  
12 think we were going to do First  
13 Independent Income Notes, and then we  
14 were going to immediately follow First  
15 Excelsior Income Notes, and then -- the  
16 fact was is that the offering sold out  
17 very quickly. There was a large demand  
18 for high yield stuff.  
19 We had a history, a long  
20 history of operating in that space in  
21 those types of offerings. And when the  
22 first offering sold quickly, we, you  
23 know -- we said, well, this is something  
24 our clients want, this is something that  
25 with scale makes sense, the more scaled,  
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1 DAVID SMITH  
2 the better off you will be. So we did a  
3 second offering and third. Finally, we  
4 ran out of steam a little bit, I guess.  
5 By the fourth offering, we didn't fill  
6 it out but --  
7 MR. RATTINER: Two follow-ups.  
8 I believe during the first break you had  
9 said you were going to get us some  
10 information. I can't recall whether it  
11 was regarding PSCP and the trust?  
12 THE WITNESS: I think it was  
13 with my wife's -- you are talking  
14 about -- Mike was interested in that,  
15 and I believe we covered it this  
16 morning.  
17 MR. RATTINER: I thought you  
18 were going to get some additional  
19 documentation. I thought you said  
20 during the break you were going to have  
21 access to it. I was just following up.  
22 THE WITNESS: Oh, you did.  
23 Yes, I did, excuse me, and I didn't.  
24 MR. RATTINER: All right.  
25 THE WITNESS: Yes, I said I  
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1 DAVID SMITH  
2 would get the -- Mike wanted the  
3 breakdown between the irrevocable trust  
4 and my wife's, and I said in the  
5 aggregate it was approximately  
6 10 percent or so, and one of them was  
7 75 percent of that, and one was 25, and  
8 I did indicate, and I failed to do that.  
9 MR. RATTINER: Okay. And my  
10 other follow-up is with regards to the  
11 integration you had mentioned you had  
12 discussions with Gersten Savage. At  
13 what point did those discussions happen?  
14 Was it pre-FIIN, post-FIIN?  
15 THE WITNESS: Pre-FIIN.  
16 MR. RATTINER: Okay. And if  
17 they were pre-FIIN, did you then also  
18 anticipate First Excelsior?  
19 THE WITNESS: No. The  
20 discussions related around all these  
21 kind of fixed income offerings, and we  
22 had been through the same process with  
23 those guys with our alarm deals, and we  
24 did not have a set idea we would do a  
25 follow-up deal.  
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1 DAVID SMITH  
2 But if you read the  
3 prospectus, they cover virtually every  
4 contingency. I mean, there's actually  
5 some language in there that says if, you  
6 know, you basically want to acquire a  
7 similar company or another company and  
8 merge it, then how would you do that?  
9 The notes had to be basically -- you  
10 couldn't change the rate of interest.  
11 You couldn't change the maturity, but if  
12 you, you meaning the managing member,  
13 wanted to do that, he didn't need a vote  
14 because these are bondholders; they are  
15 not equity people.  
16 So there was a discussion of,  
17 hey, what happens way out here? But  
18 there was nothing specific in mind. I  
19 mean, I didn't even know how the first  
20 offering would go. I mean, I had hopes  
21 that it would go well but I didn't know.  
22 MR. RATTINER: Okay.  
23 MR. NEWMAN: As the subsequent  
24 offerings are being rolled out --  
25 (Whereupon Cell Phone is  
Page 672



1 DAVID SMITH  
2 Ringing.)  
3 MR. NEWMAN: As those  
4 offerings are being rolled out, do you  
5 consult with Gersten Savage about  
6 whether or not there's an issue  
7 concerning integration?  
8 THE WITNESS: They did the  
9 legal work for all of them. I think the  
10 discussions, if any, and I think there  
11 probably were a few, certainly  
12 diminished. I know I negotiated my fee  
13 down because, you know, it wasn't that  
14 difficult to do, Number 2, number 3,  
15 number 4, was word processing stuff, and  
16 when you read the prospectuses, they  
17 pretty much read the same.  
18 MR. NEWMAN: I know. I agree  
19 with that. So the discussions, if any  
20 occurred, actually in First Independent  
21 Income Notes?  
22 THE WITNESS: That's where the  
23 vast majority of discussions and  
24 negotiations took place.  
25 MR. NEWMAN: Did you discuss

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1 DAVID SMITH  
2 with them the possibility that if First  
3 Independent Income Notes offering was  
4 successful, there would be subsequent  
5 similar offerings?  
6 MR. FRANCESKI: Wait. Can I  
7 hear that again? It wasn't an  
8 objection. I just wanted to hear the  
9 question again.  
10 (Whereupon the Question is  
11 Read Back.)  
12 MR. FRANCESKI: Hold on.  
13 Mike, if I interpret that question  
14 correctly, did he seek legal advice with  
15 respect to subsequent offerings, and  
16 that question I will allow. I don't  
17 want to abuse the privilege.  
18 MR. NEWMAN: Well, the  
19 question I have is that at the time he  
20 had his discussions with Gersten Savage,  
21 did he discuss with them the possibility  
22 of future offerings should the initial  
23 offering be successful?  
24 MR. FRANCESKI: That's okay.  
25 THE WITNESS: I don't believe

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1 DAVID SMITH  
2 so. I don't really recall, but I don't  
3 believe so.  
4 MR. NEWMAN: And all these  
5 offerings took place within what, two  
6 years of each other?  
7 THE WITNESS: Yeah.  
8 MR. NEWMAN: And what were the  
9 differences between the four LLC  
10 offerings other than the name, names of  
11 the offering, in terms of the terms?  
12 Can you explain to me any material  
13 differences you perceived in the four  
14 note offerings?  
15 THE WITNESS: There was  
16 mentioned this morning there was one  
17 difference between First Independent  
18 Income Notes and, I think, First  
19 Excelsior Income Notes, and that had to  
20 do with the senior subordinated tranche.  
21 And the first offering, I think it was,  
22 had a five-year maturity, carried a rate  
23 of around seven and a half percent, and  
24 there was no ability to get out short of  
25 maturity and then roll similar to the

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1 DAVID SMITH  
2 seniors.  
3 I think it was in First  
4 Excelsior Income Notes that we made the  
5 change that the senior subordinates went  
6 to a three-year maturity versus the  
7 five-year maturity, and then I believe  
8 the Third Albany and the First Advisory  
9 followed the same pattern in First  
10 Excelsior.  
11 MR. FRANCESKI: I am going to  
12 object and move to strike. I don't  
13 believe the witness's answer was  
14 responsive to the question.  
15 MR. NEWMAN: Well, this isn't  
16 a courtroom, so the witness has answered  
17 the way he's answered under oath.  
18 MR. FRANCESKI: I just want to  
19 make sure the record reflects that I  
20 don't believe the witness understood the  
21 question or answered it.  
22 MR. NEWMAN: The question  
23 is -- well, again --  
24 THE WITNESS: The question was  
25 there any material change?

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1 DAVID SMITH  
 2 MR. FRANCESKI: He was asking  
 3 you, for integration purposes, weren't  
 4 they all the same.  
 5 THE WITNESS: And he asked if  
 6 there was a material change, and I said  
 7 there was a material change between --  
 8 yes, okay.  
 9 MR. NEWMAN: I think the  
 10 witness understood and answered the  
 11 question.  
 12 MR. FRANCESKI: Still, I don't  
 13 think he understood. I think he didn't  
 14 understand the --  
 15 THE WITNESS: I don't worry  
 16 about the same structure being  
 17 integration. I have gone over that with  
 18 our counsel, and I have no concerns  
 19 whatsoever.  
 20 MR. NEWMAN: Okay. I  
 21 understand that. All I'm just asking  
 22 you is a specific question that involves  
 23 you telling us what material differences  
 24 there were between the four LLC  
 25 offerings, other than what you have  
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1 DAVID SMITH  
 2 already testified to?  
 3 THE WITNESS: Yeah, and I just  
 4 repeated the change.  
 5 MR. NEWMAN: You don't have to  
 6 repeat what you said. Let me finish my  
 7 question. Other than what you've  
 8 testified to, what other material  
 9 differences were there between the four  
 10 LLC offerings?  
 11 MR. FRANCESKI: Mean so as to  
 12 make them not integrated?  
 13 MR. NEWMAN: No. You're  
 14 putting that caveat. I'm asking a  
 15 specific factual question. What other  
 16 differences were there besides the name  
 17 of the offerings, other than what you  
 18 have already testified to?  
 19 THE WITNESS: In terms of the  
 20 structure?  
 21 MR. NEWMAN: Anything.  
 22 MR. FRANCESKI: No, no, Dave.  
 23 I think you're missing the point.  
 24 That's why I objected.  
 25 THE WITNESS: The major  
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1 DAVID SMITH  
 2 difference is that the investments or  
 3 the loans, which was the primary driving  
 4 force of the business, were going to be  
 5 to different parties, and they were  
 6 going to be financed by different  
 7 mechanism, different vehicles, whether  
 8 it be preferred stock, convertible  
 9 stock, whether it be, you know, bridge  
 10 loans, whether it be licensing  
 11 agreements, every asset within those  
 12 four operating companies had different  
 13 assets that they either put on their  
 14 balance sheet by purposes of loaning or  
 15 making an investment in, and in many  
 16 cases had a different approach to how  
 17 the financing was provided.  
 18 MR. NEWMAN: Okay. You've  
 19 already described and testified earlier  
 20 that there were overlapping investments  
 21 between all four notes, correct? Do you  
 22 agree with that?  
 23 THE WITNESS: In limited case,  
 24 yes.  
 25 MR. NEWMAN: We don't need to  
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1 DAVID SMITH  
 2 go through the list again of all the  
 3 different investments. I think that was  
 4 clear. You testified yesterday there  
 5 was some of the LLCs had the same  
 6 investments --  
 7 THE WITNESS: That is correct.  
 8 MR. NEWMAN: -- as each other,  
 9 correct? In the way the offering was  
 10 described to prospective investors in  
 11 the Private Placement Memorandum, what  
 12 were the material differences between  
 13 the four note offerings, if any, other  
 14 than the name of the offering?  
 15 THE WITNESS: Within the  
 16 private placement memorandum?  
 17 MR. NEWMAN: Yes.  
 18 THE WITNESS: The principal  
 19 difference that I can think of was the  
 20 one I just described a few moments ago,  
 21 the difference in the First Independent  
 22 and First Excelsior.  
 23 MR. NEWMAN: Besides that was  
 24 there anything else?  
 25 THE WITNESS: Not that I am  
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1 DAVID SMITH  
2 aware of.  
3 MR. NEWMAN: When you began  
4 selling the First Independent Income  
5 Notes, did you contemplate future  
6 offerings similar to what you were doing  
7 with the First Independent Income Notes?  
8 THE WITNESS: No.  
9 MR. NEWMAN: At what point did  
10 you decide you were going to sell First  
11 Excelsior Income Notes.  
12 THE WITNESS: When First  
13 Independent Income Notes was being so  
14 well received by our clients and our  
15 investors, the discussion with our sales  
16 force, our brokers was that they would  
17 like another offering, and so we at that  
18 point put one together.  
19 MR. NEWMAN: When was that,  
20 approximately?  
21 THE WITNESS: I think it was  
22 approximately October of '03. My  
23 recollection was that First Independent  
24 was in the September/October area, and  
25 the First Excelsior was somewhere around  
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1 DAVID SMITH  
2 November/December.  
3 MR. NEWMAN: Same year?  
4 THE WITNESS: Same year.  
5 MR. NEWMAN: When was First  
6 Excelsior LLC formed?  
7 THE WITNESS: I believe it was  
8 formed in approximately  
9 November/December '03.  
10 MR. NEWMAN: And it was formed  
11 for purposes of raising money through  
12 the LLC offering; is that correct?  
13 THE WITNESS: Yes.  
14 MR. NEWMAN: And when was the  
15 Third Albany -- when did you determine  
16 to create third -- excuse me. Let me  
17 rephrase that. When did you decide to  
18 create First -- Third Albany Income  
19 Notes?  
20 THE WITNESS: Similar pattern,  
21 First Excelsior was well received, sold  
22 out, best of my recollection; Third  
23 Albany was primarily offered in '04, and  
24 early months of '04, I think.  
25 MR. NEWMAN: When was Third  
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1 DAVID SMITH  
2 Albany formed?  
3 THE WITNESS: It would have  
4 been formed just prior to that.  
5 MR. NEWMAN: Was it formed  
6 while First Excelsior was still being  
7 sold?  
8 THE WITNESS: I don't know.  
9 MR. NEWMAN: Approximately?  
10 THE WITNESS: I mean, the fact  
11 was is that the offering came shortly  
12 after. The formation was nothing that  
13 took a great deal of thought or effort.  
14 You had to file and incorporate it, and  
15 that's something the attorneys had  
16 already done. So I don't know the exact  
17 date. It could have been the day after  
18 the other subscription was completed.  
19 MR. NEWMAN: Is it possible  
20 that Third Albany was created while  
21 First Excelsior was still being sold?  
22 THE WITNESS: Sure.  
23 MR. NEWMAN: Was First  
24 Excelsior created while First  
25 Independent Income Notes was being sold?  
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1 DAVID SMITH  
2 THE WITNESS: I don't know.  
3 MR. NEWMAN: Is it possible it  
4 was?  
5 THE WITNESS: Yes.  
6 MR. NEWMAN: And when was  
7 First Advisory Income Notes established?  
8 THE WITNESS: I think that was  
9 established in '05.  
10 MR. NEWMAN: Were Third Albany  
11 Income Notes still being sold at the  
12 time First Advisory was created?  
13 THE WITNESS: I don't know.  
14 MR. NEWMAN: Is it possible it  
15 was created while Third Albany Income  
16 Notes was being sold?  
17 THE WITNESS: It's possible.  
18 MR. NEWMAN: How would you  
19 know when it was created? What would  
20 you refer to?  
21 THE WITNESS: Date of  
22 incorporation.  
23 MR. NEWMAN: This is a Limited  
24 Liability Company, right?  
25 THE WITNESS: Correct.  
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1 DAVID SMITH  
 2 MR. NEWMAN: Where were the  
 3 LLCs created? What state?  
 4 THE WITNESS: New York.  
 5 MR. NEWMAN: Who prepared the  
 6 paperwork to create those?  
 7 THE WITNESS: Gersten Savage.  
 8 MR. NEWMAN: And who reviewed  
 9 those for the LLC? Who reviewed that  
 10 paperwork for the LLC?  
 11 THE WITNESS: The legal  
 12 paperwork?  
 13 MR. NEWMAN: The documents  
 14 that are used to form the LLC? Was any  
 15 of the review done by you? Did you  
 16 review those documents?  
 17 THE WITNESS: I don't recall,  
 18 you know, reviewing legal documents and  
 19 filing of the corporation papers. I  
 20 would have certainly seen them, and they  
 21 would have been presented to me. In  
 22 terms of a review, there's not much  
 23 review to be done.  
 24 MR. NEWMAN: Were you the  
 25 primary contact between the LLCs and

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1 DAVID SMITH  
 2 Gersten Savage?  
 3 THE WITNESS: I was.  
 4  
 5 EXAMINATION  
 6 BY MR. ROWEN:  
 7 **Q We spoke earlier about your ownership**  
 8 **in McGinn Smith & Company, the broker-dealer.**  
 9 **What is your current ownership in the**  
 10 **broker-dealer?**  
 11 A 50 percent.  
 12 **Q How much equity have you put into the**  
 13 **firm since its inception?**  
 14 A I don't know. I don't know. I mean,  
 15 it was capitalized with maybe a hundred thousand  
 16 dollars over time, various degrees. I have put some  
 17 money in for that, but I don't know the answer to  
 18 that. I have been there 29 years. I don't know.  
 19 **Q Initial was a hundred thousand**  
 20 **dollars?**  
 21 A That's -- and that's a -- I am  
 22 just -- that's my recollection. That was 29 years  
 23 ago, so.  
 24 **Q How about since 2004?**  
 25 A Maybe a couple hundred thousand.

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1 DAVID SMITH  
 2 **Q And how is your ownership in McGinn**  
 3 **Smith & Company held?**  
 4 **Common stock, preferred stock?**  
 5 A Common stock, yes.  
 6 **Q It's all in common stock?**  
 7 A I believe it is all in common stock,  
 8 yes. I might have some shares of preferred stock,  
 9 but it's non-voting stock, so all the significant  
 10 stock is common stock, yeah. In fact, I do own some  
 11 preferred shares, or my wife does, but my ownership  
 12 is all common stock.  
 13 **Q Preferred shares purchased recently?**  
 14 A No.  
 15 **Q Since 2004?**  
 16 A Possibly.  
 17 MR. RATTINER: How many  
 18 shares?  
 19 THE WITNESS: I think I have  
 20 got -- I think my wife has \$75,000  
 21 worth.  
 22 MR. RATTINER: Where are those  
 23 maintained?  
 24 THE WITNESS: I think they are  
 25 maintained -- oh, I know they are

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1 DAVID SMITH  
 2 maintained at NFS.  
 3 MR. FRANCESKI: And I'm sorry.  
 4 Did he say \$75,000 worth, because you  
 5 asked how many shares, then he answered  
 6 with dollars.  
 7 MR. RATTINER: Right.  
 8 BY MR. ROWEN:  
 9 **Q Have the four LLCs lent money to the**  
 10 **broker-dealer?**  
 11 A No.  
 12 **Q How about in May 2009?**  
 13 A No. There's never been a loan to  
 14 McGinn Smith & Company, no.  
 15 MR. ROWEN: Let's mark this as  
 16 Exhibit 19.  
 17 (Whereupon Exhibit 19 is  
 18 Marked.)  
 19 BY MR. ROWEN:  
 20 **Q I am handing you what's been marked**  
 21 **as Exhibit 19 in this matter. Exhibit 19 is a**  
 22 **four-page document. The first page is a copy of an**  
 23 **Excel download of a Quicken register report, within**  
 24 **the file titled FAIN for the account DF McGinn Smith**  
 25 **& Co. For this the staff has deleted totals and**

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1 **DAVID SMITH**

2 empty columns. The staff has also added a total at  
3 the bottom and the title FAIN at the top.

4 Staff has also highlighted one row.

5 The second page is a Quicken -- is a download of a  
6 Quicken register report and Excel spreadsheet for  
7 First Independent Income Notes with the account,  
8 other investments.

9 Again, the staff has deleted totals  
10 and empty columns, and staff has also added a balance  
11 or total at the bottom and the title FIIN at the top  
12 and it highlighted one row. The third page is an  
13 Excel spreadsheet of a download of the Quicken  
14 register report for First Excelsior, and specifically  
15 it's account DF McGinn Smith & Co. And staff has  
16 made similar adjustments to these spreadsheets to  
17 reflect for clarity, and it's titled it FEIN and  
18 highlighted one row.

19 And the forth page titled TAIN is an  
20 Excel spreadsheet of a download of the Quicken  
21 register report for Third Albany Income Notes for the  
22 account DF McGinn Smith & Co., and the staff has made  
23 similar adjustments for clarity.

24 Are you familiar with any of the four  
25 highlighted transactions?

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1 **DAVID SMITH**

2 error -- was this around -- yeah, it was around May  
3 or June or something. In May or June we were having  
4 a discussion with Andy Guzzetti and some of his  
5 colleagues in New York, and McGinn Smith was thinking  
6 about a different business model in terms of  
7 basically looking to get independence, and one of the  
8 financial arrangements with those fellows is that we  
9 were going to basically sell the franchise for  
10 \$750,000.

11 We got fairly far along. 250 of it  
12 was, in effect, going to be placed not to a loan to  
13 McGinn Smith but McGinn Smith Holdings, and I think  
14 probably that's where Brian made his error. The fact  
15 was is that the transaction fell apart somewhere  
16 August maybe, September, and we never picked up that  
17 he had, you know, misclassified it. We've  
18 re-classified it since then and reduced the fees that  
19 are due to us, but that is the explanation.

20 **Q How were these classified in the**  
21 **books of McGinn Smith & Company?**

22 A They are not because it was never a  
23 loan to McGinn Smith & Company.

24 **Q They were transactions, nonetheless.**  
25 **How were the transactions?**

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1 **DAVID SMITH**

2 A I am familiar with all four.

3 **Q Okay. Do they represent loans by the**  
4 **four LLCs to McGinn Smith & Co.?**

5 A They do not.

6 **Q What do they represent?**

7 A Fees owed to McGinn Smith & Company.  
8 It was mischaracterized by Mr. Cooper.

9 **Q And what were these specific fees**  
10 **for?**

11 A I believe these fees were fees due to  
12 McGinn Smith from either one of three categories,  
13 primarily the underwriting fees that were still owed  
14 to McGinn Smith.

15 **Q And the four in total total \$250,000?**

16 A 250,000, yes.

17 **Q Why would Mr. Cooper believe these to**  
18 **be loans?**

19 MR. FRANCESKI: Objection.

20 THE WITNESS: I can't speak  
21 for Mr. Cooper.

22 BY MR. ROWEN:

23 **Q Did he discuss -- did you discuss**  
24 **these transactions with him?**

25 A I think where Mr. Cooper made an

Page 690

1 **DAVID SMITH**

2 A Transactions are -- I think they came  
3 in as income.

4 MR. RATTINER: When did you  
5 learn that this was misclassified?

6 THE WITNESS: You know, I  
7 think within the last two months. You  
8 know, we started going over a lot of  
9 stuff, and I had Brian correct it. Part  
10 of it, I think, became when we were  
11 discussing the accrual of the fees and  
12 how various allocations should be made,  
13 and I brought that up, and I believe  
14 Brian said, you know, I've got that  
15 classified as a loan, and again the  
16 history was that we were, in fact, going  
17 to lend money under a licensing  
18 agreement. The money was going to be  
19 repaid by the gentleman that I referred  
20 to that was going to buy the franchise.  
21 That arrangement never was consummated,  
22 and we didn't pick up on it at the time.

23 MR. RATTINER: And these were  
24 fees that were earned pre-2007?

25 THE WITNESS: Yes.

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1 DAVID SMITH  
 2 MR. NEWMAN: Why were you  
 3 taking these fees in 2009 given the fact  
 4 there was this restructuring going on?  
 5 This is \$200,000.  
 6 THE WITNESS: Because this was  
 7 owed to us, and we needed the capital.  
 8 MR. NEWMAN: Money was owed to  
 9 the LLC investors too, correct?  
 10 THE WITNESS: Yeah, and  
 11 they're subordinate to our fees. We've  
 12 gone over this.  
 13 MR. NEWMAN: This 200,000 in  
 14 addition to the \$150,000 you testified  
 15 to yesterday?  
 16 THE WITNESS: Yes.  
 17 MR. NEWMAN: Okay. So your  
 18 fees for 2009 were \$350,000?  
 19 THE WITNESS: At least.  
 20 MR. NEWMAN: At least?  
 21 THE WITNESS: Yeah.  
 22 MR. NEWMAN: There's more than  
 23 that?  
 24 THE WITNESS: Oh, there's lots  
 25 more than that, yeah.

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1 DAVID SMITH  
 2 MR. NEWMAN: Why don't you  
 3 tell us about the rest of the money in  
 4 2009.  
 5 THE WITNESS: Roughly -- we  
 6 have gone over this yesterday but we can  
 7 go over it again. There's substantial  
 8 fees that were owed to the firm from the  
 9 three entities over a number of years.  
 10 They were not taken. They were used  
 11 either as collateral for related party  
 12 deals, which we talked about, and they  
 13 were just not taken. There's still  
 14 roughly 6 to \$700,000 that is owed to  
 15 us, we haven't taken.  
 16 MR. NEWMAN: All right. How  
 17 have you been tracking these fees that  
 18 you keep on talking about? How have you  
 19 been tracking that internally? What  
 20 documentation existed to show how much  
 21 is owed, when it's owed, and to what it  
 22 is owed?  
 23 THE WITNESS: Well, it's not  
 24 very difficult to track. We know what  
 25 the principal value is. We are capable

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1 DAVID SMITH  
 2 of multiplying 2 percent times that  
 3 value for the underwriting fees and  
 4 1 percent for the management fee and a  
 5 quarter of a percent for the trustee  
 6 fee.  
 7 MR. NEWMAN: Okay. So are  
 8 there any fees that you left out?  
 9 THE WITNESS: No, those are  
 10 the only three fees.  
 11 MR. NEWMAN: And those fees  
 12 are tracked how? All in your head or is  
 13 there some kind of record that's  
 14 maintained?  
 15 THE WITNESS: Well, I don't  
 16 think the record was precise, and that's  
 17 why I went to Chris's point several  
 18 months ago, we started to make sure that  
 19 we knew exactly what not only the fees  
 20 that were owed, what were pledged, what  
 21 categories were in, what other potential  
 22 liabilities against it, whether it be  
 23 legal fees or whether it be potential  
 24 underwriting fees. And so those  
 25 adjustments have been made over the last

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1 DAVID SMITH  
 2 couple of months, and I think the record  
 3 is totally complete as we speak.  
 4 MR. NEWMAN: This is for  
 5 offerings that began in 2003, these  
 6 fees?  
 7 THE WITNESS: Yeah, that's how  
 8 the business works. You get a  
 9 management fee every year.  
 10 MR. NEWMAN: So the records  
 11 that were made complete two months ago  
 12 to track an account for the fees?  
 13 THE WITNESS: The liability to  
 14 the firm, which is the FINRA was, I  
 15 believe, accrued every year. MS  
 16 Advisors, McGinn Smith Capital Holdings,  
 17 for the most part, I don't think we took  
 18 a lot of those fees. They were just  
 19 accruing.  
 20 MR. NEWMAN: How do you know  
 21 that? Is this in your head or is there  
 22 some kind of record?  
 23 THE WITNESS: Some kind of  
 24 record. I know exactly when we got  
 25 them. I mean, do you think I'd know not

Page 696

1 DAVID SMITH  
 2 of \$4 million, that I wouldn't be aware  
 3 of it?  
 4 MR. NEWMAN: What record do  
 5 you have that shows this?  
 6 THE WITNESS: I can show  
 7 exactly what was paid. You can look at  
 8 the Quicken records, and we've given  
 9 them.  
 10 MR. NEWMAN: We are looking at  
 11 the Quicken records, and the Quicken  
 12 records say loans.  
 13 THE WITNESS: Well, they are  
 14 not loans. I am telling you they are  
 15 not loans, and that's one instance, out  
 16 of \$12 million in fees, you're picking  
 17 on \$150,000?  
 18 MR. NEWMAN: So the way you  
 19 track, so I understand what you are  
 20 saying, is the way the firm tracked  
 21 internally the fees that were paid to  
 22 all of the different McGinn Smith  
 23 affiliates, companies, in connection  
 24 with these LLC offerings was through the  
 25 Quicken database?

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1 DAVID SMITH  
 2 MR. FRANCESKI: Objection, but  
 3 you may answer.  
 4 MR. NEWMAN: Was that the way  
 5 in which the firm tracked its fees?  
 6 THE WITNESS: I know that the  
 7 fees were tracked from the McGinn Smith  
 8 & Company in terms of its underwriting.  
 9 I don't know if MS Advisors accrued them  
 10 on the Quicken scale or not. I know  
 11 when they were paid that they were on  
 12 the Quicken scale. I don't know if we  
 13 kept an accrual. I know what it is,  
 14 because you asked me whether I can do  
 15 the math in my head, and the answer is  
 16 yes.  
 17 MR. NEWMAN: Why weren't the  
 18 fees tracked for some sort of record in  
 19 the system?  
 20 (Whereupon Cell Phone is  
 21 Ringing.)  
 22 MR. NEWMAN: Why weren't the  
 23 fees --  
 24 THE WITNESS: I knew in my  
 25 head at all times what my liabilities

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1 DAVID SMITH  
 2 were against those fees, and, I mean, I  
 3 don't know what other answer I can give  
 4 you. I knew what related party loans, I  
 5 knew what commissions were due to my  
 6 brokers, when they were going to have to  
 7 be paid. I knew what fees were entitled  
 8 to me, and, you know, when I take them  
 9 as a cash pay is my business.  
 10 MR. NEWMAN: All right. This  
 11 \$200,000 that was paid to McGinn Smith,  
 12 and 250 that was paid in May of 2009,  
 13 can you tell us what those fees  
 14 represented and what years?  
 15 THE WITNESS: I believe they  
 16 represented commissions pre-2008.  
 17 MR. NEWMAN: What years? You  
 18 said you had it all in your head.  
 19 THE WITNESS: 2007.  
 20 MR. NEWMAN: You know that for  
 21 a fact --  
 22 THE WITNESS: Yes.  
 23 MR. NEWMAN: -- or are you  
 24 just guessing? 2007. That 2007 covers  
 25 what, what particular fees?

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1 DAVID SMITH  
 2 THE WITNESS: McGinn Smith was  
 3 only entitled to underwriting fees,  
 4 2 percent.  
 5 MR. NEWMAN: So these funds or  
 6 these LLCs are paying to you an  
 7 underwriting fee in 2009 for 2007?  
 8 THE WITNESS: That is correct.  
 9 MR. NEWMAN: Even though  
 10 there's a restructuring going on at that  
 11 time?  
 12 THE WITNESS: Let's try it  
 13 again. There's an order of who has the  
 14 ability to get the money. The first  
 15 order is --  
 16 MR. FRANCESKI: Let me object  
 17 on the grounds that this has been asked  
 18 and answered.  
 19 THE WITNESS: How many times,  
 20 want to count, five, six?  
 21 MR. FRANCESKI: I think Mr.  
 22 Newman is just arguing with you at this  
 23 point. So go ahead and answer.  
 24 MR. NEWMAN: I am not arguing.  
 25 I'm asking questions.

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1 DAVID SMITH  
 2 MR. FRANCESKI: It's been  
 3 asked and answered many times.  
 4 MR. NEWMAN: So I am trying to  
 5 understand exactly how this is all being  
 6 tracked and accounted for. We are  
 7 talking about millions of dollars in  
 8 investor money that's going to you.  
 9 THE WITNESS: It's not  
 10 investor money. Let's get that  
 11 straight. Okay. That money belongs to  
 12 McGinn Smith, McGinn Smith Capital  
 13 Holdings and McGinn Smith Advisors.  
 14 It's not investor money. It's our  
 15 money. That's what is critical. That  
 16 is what you're missing, and let's get  
 17 this straight so if we are going to have  
 18 a conversation, it could be one with  
 19 some logic, okay.  
 20 MR. NEWMAN: Okay. I want to  
 21 know how McGinn Smith was tracking all  
 22 these different fees over the six-year  
 23 time period? That's what I want to know  
 24 from you. If you are telling us you  
 25 kept track of it in your head, that is

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1 DAVID SMITH  
 2 the fact, that's the truth, that's fine.  
 3 But we need to know what records were  
 4 maintained to track the amounts owed on  
 5 a year-by-year basis for each of these  
 6 different items that you are claiming  
 7 the firm was entitled to?  
 8 THE WITNESS: Some of them  
 9 were accrued on the Quicken records.  
 10 Some of them, I don't believe, were  
 11 because I don't think Brian Cooper was  
 12 told to accrue them. I don't know that  
 13 for a fact. I haven't looked at it.  
 14 Alls I know is that over the last two  
 15 months we have gone back, and because of  
 16 the various aspects of this business,  
 17 because of the various constraints that  
 18 we have had, because of the legal fees,  
 19 we are going to make sure that every  
 20 dollar is allocated properly, and that's  
 21 what I have asked them to do, and that's  
 22 what we are doing.  
 23 MR. NEWMAN: Why did it take  
 24 to 2009 for you to start doing this?  
 25 THE WITNESS: Because I didn't

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1 DAVID SMITH  
 2 have the problems in 2008 that I have in  
 3 2009.  
 4 MR. NEWMAN: What does that  
 5 mean?  
 6 THE WITNESS: Means I didn't  
 7 have the financial problems, I didn't  
 8 have the regulatory problems.  
 9 MR. NEWMAN: So you began  
 10 doing this more detailed accounting  
 11 after FINRA staff came into your offices  
 12 in Albany and began looking for these  
 13 records?  
 14 THE WITNESS: No. I began  
 15 doing it when I recognized that I had  
 16 some serious financial liabilities  
 17 facing me.  
 18 MR. NEWMAN: And when was  
 19 that?  
 20 THE WITNESS: That was  
 21 basically in December '08.  
 22 MR. NEWMAN: And when you said  
 23 serious financial liabilities, can you  
 24 be more specific?  
 25 THE WITNESS: That was when

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1 DAVID SMITH  
 2 the first lawsuit or arbitration was  
 3 filed by Dr. Chang for the sum of 2 1/2  
 4 million dollars.  
 5 MR. NEWMAN: So that's when  
 6 you began a detailed --  
 7 THE WITNESS: That's when I  
 8 started to seriously think of the  
 9 financial difficulties of McGinn Smith,  
 10 yes.  
 11 MR. NEWMAN: When was it that  
 12 you began actually trying to reconcile  
 13 and track this information in more  
 14 detail?  
 15 THE WITNESS: Mostly this  
 16 fall.  
 17 MR. NEWMAN: And that was  
 18 after the FINRA staff began asking you  
 19 for information regarding --  
 20 THE WITNESS: No, it wasn't  
 21 related. It was related to the Chang  
 22 arbitration.  
 23 MR. NEWMAN: And when did the  
 24 FINRA staff come to your offices for the  
 25 first time to review your records

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1 DAVID SMITH  
2 approximately?  
3 MR. FRANCESKI: February of --  
4 THE WITNESS: Well, they  
5 started in October of 2008. That was a  
6 regular audit. I basically had an exit  
7 interview end of December/January. That  
8 never quite got consummated. I think  
9 the next time the staff actually showed  
10 up -- there might have been an interval  
11 in time, but in June Mr. McCarthy and a  
12 number of his staff came, I think it was  
13 around June 1st, spent a number of days  
14 with us. They have been back in maybe  
15 September of '09. I think they have  
16 been back again maybe in November of  
17 '09.  
18 MR. NEWMAN: Okay. So the  
19 250,000 you've testified to as an  
20 underwriting fee, what does the \$150,000  
21 you testified to yesterday that was paid  
22 to McGinn Smith represent?  
23 THE WITNESS: Also  
24 underwriting fees.  
25 MR. NEWMAN: Okay. For which  
Page 705

1 DAVID SMITH  
2 offering?  
3 THE WITNESS: In the  
4 aggregate, I don't know how they were --  
5 all four of the offerings owed money.  
6 MR. NEWMAN: How did you come  
7 up with 150,000?  
8 THE WITNESS: That's what I  
9 needed.  
10 MR. NEWMAN: Oh, so does that  
11 relate to the offering or is that what  
12 you needed?  
13 THE WITNESS: No, relates to  
14 what is owed to me, and I needed  
15 \$150,000. That's what is owed to me. I  
16 have testified again that there is more  
17 money owed to me than that. So I didn't  
18 take it all but I took what I needed.  
19 MR. NEWMAN: So, and you can't  
20 tell us what offerings that 150 pertains  
21 to? Did it pertain to all four  
22 offerings or one or two?  
23 MR. FRANCESKI: Objection.  
24 Mike, you really don't understand this?  
25 MR. NEWMAN: Oh, I understand  
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1 DAVID SMITH  
2 it perfectly. I understand perfectly.  
3 MR. FRANCESKI: All you are  
4 doing is badgering the witness.  
5 MR. NEWMAN: I want to get  
6 some more clarity.  
7 MR. FRANCESKI: All you are  
8 doing is badgering the witness, and we  
9 are just going to call quits because  
10 that's not fair. You know, he's told  
11 you repeatedly. You want to argue with  
12 him, file an action, and we will see you  
13 before a Hearing Officer, and we will  
14 all dispute what this all means.  
15 But the facts are not going to  
16 change. He's made it clear what the  
17 facts are. You can do with them what  
18 you want.  
19 MR. NEWMAN: We will do what  
20 we want.  
21 MR. FRANCESKI: Then stop  
22 badgering him.  
23 MR. NEWMAN: That's your  
24 characterization.  
25 MR. FRANCESKI: And the record  
Page 707

1 DAVID SMITH  
2 will show.  
3 MR. NEWMAN: Exactly. What  
4 the record will show, I'm asking  
5 legitimate, relevant questions, and you  
6 can characterize them any way you want.  
7 I want to know for the \$150,000 what  
8 offerings that fee pertains to.  
9 THE WITNESS: I will provide  
10 you with a schedule. How is that?  
11 MR. NEWMAN: I thought you had  
12 it in your head. You told us that  
13 10 minutes ago.  
14 THE WITNESS: Let's remember  
15 what I said I could do in my head. I  
16 said I can multiply 2 percent times 85  
17 million in my head. I can multiply 1  
18 percent in my head. That's what I said.  
19 You asked me what the aggregate fees  
20 were. I said I can do them in my head.  
21 MR. NEWMAN: The \$250,000  
22 underwriting fee, what specific  
23 offerings does that pertain to?  
24 THE WITNESS: I don't know.  
25 MR. NEWMAN: And how would you  
Page 708

1 DAVID SMITH  
2 be able to tell us that?  
3 THE WITNESS: Because I do  
4 know back at my home office.  
5 MR. NEWMAN: What records  
6 would you look at to determine that?  
7 THE WITNESS: I would look at  
8 the records of payment as allocated, as  
9 a subtraction from what is earned.  
10 MR. NEWMAN: Do you have a  
11 record in your office which shows the  
12 fees --  
13 THE WITNESS: Yes.  
14 MR. NEWMAN: -- that you are  
15 entitled to for underwriting?  
16 THE WITNESS: Yes.  
17 MR. NEWMAN: And where is that  
18 record maintained?  
19 THE WITNESS: It's maintained  
20 at 99 Pine Street.  
21 MR. NEWMAN: And what is that  
22 record called? What is the document,  
23 database? What is it called?  
24 THE WITNESS: It's called  
25 accrued fees.

Page 709

1 DAVID SMITH  
2 MR. NEWMAN: And when was that  
3 document or document first prepared?  
4 THE WITNESS: It's been  
5 prepared, as I indicated, over time. I  
6 don't believe it was totally update. We  
7 have been working on the update over the  
8 last several months, and it is now  
9 complete.  
10 MR. NEWMAN: Who has access to  
11 that information besides yourself?  
12 THE WITNESS: Mr. McGinn.  
13 MR. NEWMAN: Is this an  
14 electronic record?  
15 THE WITNESS: And Mr. Cooper.  
16 Yes.  
17 MR. NEWMAN: Electronic  
18 record?  
19 THE WITNESS: Yes.  
20 MR. NEWMAN: Was this record  
21 provided to the staff?  
22 THE WITNESS: I don't believe  
23 the staff asked for it. It may have  
24 been on -- some of it may have been  
25 accrued on the balance sheets of the

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1 DAVID SMITH  
2 LLCs, not all of it. I don't know if  
3 all of it is. But it's now in record  
4 form and available to you upon request.  
5 MR. RATTINER: When did you  
6 find out that the record was not up to  
7 date?  
8 THE WITNESS: As I said, I  
9 knew what the fees were in general, that  
10 we hadn't collected them. I knew that  
11 there was a liabilities against them. I  
12 knew there was potential liabilities  
13 coming against them. I knew that the  
14 fees were far in excess of what I  
15 needed. They still are far in excess of  
16 what I need.  
17 But as things have started to  
18 unfold, and I knew I would have a demand  
19 on those fees, I have paid more  
20 attention to it in the last couple of  
21 months.  
22 MR. RATTINER: So back to the  
23 question, when did you learn that the  
24 record was not up to date?  
25 THE WITNESS: That would be

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1 DAVID SMITH  
2 the last couple of months. That's when  
3 I started to pay attention to it.  
4 MR. RATTINER: In December?  
5 THE WITNESS: I think it was  
6 before that.  
7 MR. RATTINER: And who alerted  
8 you to the fact that the record was now  
9 up to date?  
10 THE WITNESS: I spoke to Brian  
11 Cooper who basically does that work, and  
12 we started working on it.  
13 MR. RATTINER: What was his  
14 rationale for not keeping that record up  
15 to date?  
16 THE WITNESS: Well, again, his  
17 rationale as regards to McGinn Smith, I  
18 am not testifying that they weren't up  
19 to date. I think the fees due McGinn  
20 Smith were up to date. I don't think  
21 the fees due to McGinn Smith Advisors  
22 and McGinn Smith Capital Holdings were  
23 up to date.  
24 MR. RATTINER: These fees  
25 have -- do the fees have a time frame

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1 DAVID SMITH  
 2 where they eventually end?  
 3 THE WITNESS: Actually, they  
 4 don't. We have -- we have made a  
 5 decision which we think is a rational  
 6 decision. The underwriting fees end at  
 7 the maturity date of the LLCs,  
 8 certainly, when they expect to be paid  
 9 for any more than that.  
 10 The advisory fee would  
 11 normally be paid as long as you are  
 12 still advising and managing. We have  
 13 chosen not to take those fees anything  
 14 beyond that because we think that,  
 15 considering the condition of the LLCs  
 16 and the investors, that before that  
 17 is -- before we would take fees or even  
 18 suggest we deserve fees, we would think  
 19 that the note holders would either have  
 20 to approve that or be given the  
 21 opportunity to put in a new manager as a  
 22 result of where their financial status  
 23 is.  
 24 The third element, which is  
 25 the trustee fee, we have not extended  
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1 DAVID SMITH  
 2 that, either. That is one that I would  
 3 more rationally believe that we would  
 4 remain entitled to because you have to  
 5 cover tax expenses and other transfer  
 6 and expenses, but in no case have we  
 7 extended it beyond any of the maturities  
 8 of the notes.  
 9 MR. RATTINER: Now, when you  
 10 say maturities, you are basing maturity  
 11 based on the restructuring or the  
 12 maturity based on the --  
 13 THE WITNESS: No, on the  
 14 original.  
 15 MR. RATTINER: So have they  
 16 all matured at this point?  
 17 THE WITNESS: No. I think  
 18 FAIN doesn't mature till later this  
 19 year.  
 20 MR. RATTINER: So other than  
 21 First Advisory --  
 22 THE WITNESS: Yes.  
 23 MR. RATTINER: -- the other  
 24 three have matured?  
 25 THE WITNESS: That's correct.  
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1 DAVID SMITH  
 2 MR. RATTINER: And when do  
 3 they mature, if you could walk me  
 4 through?  
 5 THE WITNESS: First  
 6 Independent matured in December of '08.  
 7 First Excelsior matured in January of  
 8 '09. Third Albany matured in  
 9 December of '09, and I believe First  
 10 Advisory matures next November of 2010.  
 11 MR. RATTINER: Are you  
 12 currently accruing those fees?  
 13 THE WITNESS: They are  
 14 accrued, and as paid, they are  
 15 obviously, the accrual is reduced.  
 16 BY MR. ROWEN:  
 17 **Q Did the four LLCs loan money to other**  
 18 **entities where the money was used to make an**  
 19 **investment in the broker-dealer?**  
 20 A I don't recall other entities making  
 21 an investment in the broker-dealer. Help me out.  
 22 **Q How about McGinn Smith Transaction**  
 23 **Funding?**  
 24 A They have -- I don't believe they  
 25 have made an investment. They have paid some fees to  
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1 DAVID SMITH  
 2 it -- I don't know. I am not sure. I think there  
 3 was -- yes, I think there was a loan, and that's part  
 4 of the collateralized portion. I can't tell you  
 5 exactly what the breakdown is, but, yes, I think we  
 6 did.  
 7 **Q Are there multiple loans?**  
 8 A I don't think so, but I can't tell  
 9 you for sure without the record in front of me.  
 10 **Q And to be clear, those loans were**  
 11 **then used to invest in the broker-dealer?**  
 12 A No. The Transaction Funding  
 13 transaction, as part of the offering, made an  
 14 investment in a preferred in McGinn Smith but the  
 15 dollars didn't flow from the funds, the transaction  
 16 funding to McGinn Smith. It was -- they flowed to  
 17 Transaction Funding. Transaction Funding had its  
 18 own, as part of its -- and in the offering document  
 19 was always making it a preferred investment in McGinn  
 20 Smith.  
 21 **Q Did McGinn Smith Transaction Funding**  
 22 **need the loan from any of the four LLCs to make its**  
 23 **preferred stock investment in the broker-dealer?**  
 24 A I believe that the Transaction  
 25 Funding transaction received an equity subscription  
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1 DAVID SMITH

2 amount, and they had two functions. One was to make  
3 an investment in the preferred stock up to a million  
4 and a half, I believe was the number, and the rest of  
5 it was to use in their normal course of business. So  
6 I don't know the timing of it, but to suggest that it  
7 was needed, I don't think that's accurate.

8 **Q Why was McGinn Smith Transaction**  
9 **Funding borrowing funds from the four LLCs?**

10 A Again, McGinn Smith Transaction  
11 Funding, where there's a loan, was fully  
12 collateralized by the fees. We could have taken the  
13 fee income. Instead, we characterized it as a loan.

14 **Q How was McGinn Smith Transaction**  
15 **Funding due fees by the four --**

16 A The loan is collateralized by the  
17 fees. So if I had chosen not to take the loan, I  
18 could have just taken the fees.

19 **Q So why not invest it directly into a**  
20 **broker-dealer instead of going through McGinn Smith**  
21 **Transaction Funding?**

22 A Why not invest my fees directly into  
23 the broker-dealer?

24 **Q Well, I mean, you said you could?**

25 A Yeah. I guess I don't understand the

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1 DAVID SMITH

2 question.

3 **Q I don't know why money flowed through**  
4 **McGinn Smith Transaction Funding that would**  
5 **eventually end up in the broker-dealer?**

6 A Because as part of the offering, they  
7 were to commit a million and a half dollars.  
8 Transaction Funding was directly tied to the business  
9 of McGinn Smith & Company. It's just the nature of  
10 how we structured the investment.

11 **Q So if I am understanding this**  
12 **correctly, McGinn Smith Transaction Funding had**  
13 **pledged a million and a half dollars to the**  
14 **broker-dealer?**

15 A They -- I don't know if pledge is the  
16 right word --

17 **Q Committed?**

18 A -- but they had, as part of their  
19 offering, they could and would invest up to a million  
20 and a half dollars in the preferred, yes.

21 **Q But they did not have the cash on**  
22 **hand to do it?**

23 A At the time of the loan, is that what  
24 you are asking?

25 **Q Yes.**

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1 DAVID SMITH

2 A I don't know. Could be. Could be.

3 I mean, they may have already had dollars committed  
4 elsewhere. I mean, it was a certain -- as the money  
5 came in Transaction Funding, I don't know exactly how  
6 much flowed to the broker-dealer at that time, if  
7 there was -- you know, it was a percentage of the  
8 total commitment, and so maybe we didn't -- hadn't  
9 raised all the money. I can't remember the exact  
10 numbers.

11 MR. ROWEN: Okay. Can I have  
12 this marked as Exhibit 20.

13 (Whereupon Exhibit 20 is  
14 Marked.)

15 BY MR. ROWEN:

16 **Q I am handing you what's been marked**  
17 **Exhibit 20 in this matter. Exhibit 20 is a**  
18 **three-page document, and it is an Excel spreadsheet**  
19 **of a Quicken download in the file MSTF, of the**  
20 **account titled checking. Similar to the prior**  
21 **exhibits, the staff has deleted totals, rows and**  
22 **empty columns.**

23 **The staff has also added one total at**  
24 **the bottom of Page 3, the MSTF title at the top and**  
25 **has highlighted select rows.**

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1 DAVID SMITH

2 **Can you take a look at the**  
3 **highlighted rows, please?**

4 **Are these the transactions you were**  
5 **thinking of in our discussion?**

6 MR. FRANCESKI: These meaning  
7 all of these?

8 BY MR. ROWEN:

9 **Q The highlighted rows?**

10 A I am familiar on the second page, the  
11 250 against McGinn Smith Capital Holdings. I am not  
12 sure why it says MS Advisors, Inc. The 11/26/08,  
13 that may have just been a loan to McGinn Smith  
14 Capital Holding for \$150,000 from each of the -- each  
15 of the three LLCs, but I can't recall with any -- it  
16 would look like the Capital Holdings then bought  
17 preferred stock. That would seem to be the chain of  
18 events.

19 **Q These are the books of MSTF?**

20 A Oh, thank you. I was confused. I  
21 was thinking the books of -- okay, MSTF. Okay. So,  
22 (Reviewing). These are all entries from MSTF?

23 **Q Yes. This is MSTF's download of the**  
24 **checking register reports for all dates for MSTF.**

25 A Okay. Well, then I would -- I guess

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1 DAVID SMITH  
 2 these are the loans we were talking about then, yes.  
 3 **Q Okay. And for the record, on Page 1,**  
 4 **there are four rows highlighted, three of which show**  
 5 **an increase of \$50,000, which the category is titled**  
 6 **DF, MS Advisors and MSCH of which the descriptions**  
 7 **are TAIN -- sorry, Third Albany -- I better spell it**  
 8 **-- TAIN, FEIN, and FIIN respectively, and a negative**  
 9 **\$150,000 with the category MS Pref stock, and a**  
 10 **description McGinn Smith.**  
 11 **So what do you understand the series**  
 12 **of transactions to be?**  
 13 A I understand this to be, since it's  
 14 on the MSTF books, that those monies were lent to  
 15 MSTF, and they in turn purchased MS Preferred stock  
 16 per the offering document as anticipated.  
 17 **Q And these all occurred on the same**  
 18 **day, 11-26-2008?**  
 19 A That would appear to be the case,  
 20 yes, and on 4-14 looks like a similar transaction,  
 21 same thing, MSTF used the money to purchase the  
 22 preferred stock.  
 23 **Q On the same day?**  
 24 A Same day.  
 25 **Q And I will go back to my question.**

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1 DAVID SMITH  
 2 **Why don't the LLCs just purchase the**  
 3 **preferred stock?**  
 4 **Why did it go through MSTF?**  
 5 A Because MSTF as part of their  
 6 offering was committed to buy that stock. I mean,  
 7 this was a different preferred stock. This was a  
 8 preferred -- class preferred stock that was related  
 9 directly to MSTF. If we were to -- it wouldn't have  
 10 been available for purchase, if I had done it  
 11 strictly to the preferred stock, that has been  
 12 previously bought, is the 87 series, and that was, I  
 13 believe, fully subscribed for.  
 14 **Q Why is -- why did MSTF need the**  
 15 **money -- need loans from the LLCs to make this**  
 16 **investment that they were committed to under its PPM?**  
 17 **I am guessing the PPM is where it**  
 18 **spelled out the one and a half million?**  
 19 A Correct.  
 20 **Q Okay. So why did MSTF need to borrow**  
 21 **funds from the LLCs to make this investment that it**  
 22 **was committed to?**  
 23 A Because they had committed the other  
 24 dollars that were not committed to the preferred to  
 25 transactions that was part of their mission. They

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1 DAVID SMITH  
 2 didn't do it pari passu. In other words, X dollars  
 3 came in. Those dollars went out to commitments as  
 4 part of their business plan. There was still some  
 5 allocation of those dollars was available for the  
 6 preferred stock. I can't tell you with certainty,  
 7 but my guess is, is that that money was available to  
 8 be allocated to McGinn Smith, and McGinn Smith was in  
 9 need of some capital.  
 10 **Q Explain, you said the money was**  
 11 **allocated to McGinn Smith, I'm sorry, I didn't**  
 12 **understand that part.**  
 13 A In the offering document, and I don't  
 14 have the offering document with me, maybe you guys  
 15 do, a certain number of dollars were to be raised.  
 16 Best of my recollection, it was seven and a half, 8  
 17 million dollars. Don't hold me to that. That's  
 18 approximate.  
 19 Within the document, a million and a  
 20 half of the offering proceeds were committed, to use  
 21 your term, allocated, to use my term, to purchase a  
 22 certain series of preferred stock and 8 percent  
 23 preferred stock of McGinn Smith & Company, a new  
 24 issue. I don't know the numbers, but let's take for  
 25 a moment an example. At any of this point in time,

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1 DAVID SMITH  
 2 \$5 million comes in to -- let's make it easy, 6  
 3 million dollars comes in. So we've got 75 percent of  
 4 the money that has come in, right? 6 million out of  
 5 8, 75 percent.  
 6 If you did it on a pro rata basis,  
 7 which wasn't necessary, but then you would assume  
 8 that 75 percent of a million and a half would be  
 9 allocated to McGinn Smith to buy the preferred.  
 10 Now let's assume for a moment that  
 11 five and a half million came in and it went to  
 12 everything, other investments, other capital needs,  
 13 and it hadn't gone to McGinn Smith yet. So when we  
 14 put in new money, we were in effect playing catch-up  
 15 with the pro rata shares.  
 16 So as long as McGinn Smith  
 17 Transaction Funding did not invest more than a  
 18 million and a half dollars in McGinn Smith, when they  
 19 chose to do that was their business. No one else's.  
 20 I don't know for a fact, but my guess is, is that  
 21 most of the money that had come into Transaction  
 22 Funding at this time had been allocated elsewhere.  
 23 McGinn Smith needed capital. They had capital coming  
 24 from Transaction Funding. The money was fully  
 25 collateralized anyway, so it was of no risk to the

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1 DAVID SMITH  
 2 funds, so we chose to lend it to Transaction Funding.  
 3 **Q So is the simple story that McGinn**  
 4 **Smith Transaction Funding committed or allocated more**  
 5 **funds than it raised?**  
 6 A No, not at all. How would you -- in  
 7 fact, they never completed it. I don't think we  
 8 ended up raising 8 million dollars. I think we ended  
 9 up raising 6 and a half million dollars or something  
 10 like that.  
 11 **Q But it had committed funds to the**  
 12 **broker-dealer that it did not raise through its**  
 13 **offering?**  
 14 MR. FRANCESKI: Objection.  
 15 THE WITNESS: No. No. What I  
 16 said was -- what I said was is that  
 17 there would be a certain percentage of  
 18 allocation, and if, in effect, you had  
 19 used a greater percent of that  
 20 allocation to other activities, you  
 21 could play catch up football, and so  
 22 that's basically what happened.  
 23 MR. RATTINER: While Steve is  
 24 looking at that document, can we get  
 25 some background on MSTF, who were the

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1 DAVID SMITH  
 2 owners of the entity?  
 3 THE WITNESS: I believe the MS  
 4 Holdings.  
 5 MR. RATTINER: And what was  
 6 the purpose of the entity?  
 7 THE WITNESS: Purpose of the  
 8 entity was to provide bridge financing  
 9 to various transactions that we might be  
 10 involved in or to make investments in  
 11 areas outside of the equity markets.  
 12 MR. RATTINER: And how many  
 13 transactions occurred within MSTF?  
 14 THE WITNESS: It's run by Mr.  
 15 McGinn. I don't know. I am going to  
 16 guess four, five but I don't have that  
 17 knowledge.  
 18 MR. RATTINER: And how much  
 19 was invested?  
 20 THE WITNESS: I think it was  
 21 approximately 6 and a half million  
 22 dollars.  
 23 MR. RATTINER: And how much in  
 24 fees did you earn through any of the  
 25 entities?

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1 DAVID SMITH  
 2 THE WITNESS: Through McGinn  
 3 Smith Transaction Funding?  
 4 MR. RATTINER: Well, I guess  
 5 as a result of McGinn Smith Transaction  
 6 Funding, what sort of fees would you  
 7 have derived?  
 8 THE WITNESS: I think there  
 9 was a normal placement fee added, 7, 8  
 10 percent.  
 11 MR. RATTINER: In addition to  
 12 that, anything else?  
 13 THE WITNESS: I don't believe  
 14 so.  
 15 MR. RATTINER: What is the  
 16 current status of MSTF?  
 17 THE WITNESS: It's  
 18 operational, wholesome investments.  
 19 MR. RATTINER: And that was  
 20 done as a separate private placement?  
 21 THE WITNESS: Yes, it was.  
 22 MR. RATTINER: And how many  
 23 investors bought into that?  
 24 THE WITNESS: Maybe 10, 15.  
 25 There was one large investor for 2 1/2

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1 DAVID SMITH  
 2 million. Mostly investors were pretty  
 3 large.  
 4 MR. RATTINER: The two and a  
 5 half million dollars investment, was  
 6 that [REDACTED]?  
 7 THE WITNESS: Yes. You knew  
 8 the answer.  
 9 MR. RATTINER: And what is the  
 10 current status of payment back to the  
 11 investors?  
 12 THE WITNESS: They are current  
 13 but their interest -- I don't think the  
 14 notes are due for a year, year and a  
 15 half.  
 16 MR. RATTINER: And what is the  
 17 probability that those notes will pay  
 18 back in the year, year and a half?  
 19 THE WITNESS: Well, a great  
 20 deal will depend on the liquidity of  
 21 some of the investments. It's been  
 22 impaired certainly somewhat by the  
 23 status of McGinn Smith & Company, since  
 24 a million and a half dollars of it was  
 25 invested in our Preferred, and the

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1 DAVID SMITH  
2 fortunes in McGinn Smith & Company  
3 aren't particularly bright.  
4 MR. RATTINER: Even with that  
5 million and a half dollars invested in  
6 Preferred stock of McGinn Smith, the  
7 entity MSTF is still able to --  
8 THE WITNESS: MSTF has a --  
9 they have the preferred to McGinn Smith,  
10 of course, and then there's a -- it's  
11 basically a transactional contingency  
12 fee, that they get some percentage of  
13 what we earn on transactions. And,  
14 again, fortunes of McGinn Smith are  
15 going to be instrumental in how we go  
16 forward with that and restructure, and  
17 if McGinn Smith doesn't get additional  
18 opportunities pretty soon, we are going  
19 to have to rethink that.  
20 MR. RATTINER: You stated that  
21 you have been taking fees from accrued  
22 fees that were accrued pre-2007. How  
23 about the payments to the reps that earn  
24 those fees?  
25 THE WITNESS: We have, I

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1 DAVID SMITH  
2 mentioned this yesterday, and the total  
3 liabilities against all the fees that  
4 are owed to us, and we have allocated  
5 those in very specific ways in terms of  
6 date earned, date paid, those allocated  
7 to the collateral, those allocated to  
8 legal fees, and it is the last item,  
9 which you were asking about, I testified  
10 yesterday, I will repeat again, that we  
11 have set aside something like \$300,000  
12 of it to be paid to former employees, if  
13 upon advice from counsel, and a lot of  
14 ifs, that is considered a necessary  
15 payment and one that we desire to make.  
16 MR. RATTINER: And that  
17 \$300,000 represents payments from what  
18 year?  
19 THE WITNESS: Represents  
20 payments in pre-2000 -- no, those  
21 payments -- excuse me -- if we take  
22 those underwriting fees, I think the  
23 brokers have been paid their fees up  
24 through 2008. So I think the fees that  
25 they are looking at are any fees that we

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1 DAVID SMITH  
2 would take for 2009.  
3 MR. RATTINER: You're certain  
4 of the payment in 2008?  
5 THE WITNESS: I think -- no, I  
6 am not. Actually, we made a partial  
7 payment in 2008. Thank you. We -- and  
8 what we did was we indicated to the  
9 brokers, because of capital constraints,  
10 we would pay them out over time, and I  
11 believe through the course of 2009 we  
12 were making some of those payments. At  
13 some point as capital became critical,  
14 we stopped making those payments, and  
15 that's where there's a, I think roughly  
16 \$300,000, if you take the brokers and  
17 assume that they would have gotten paid  
18 through the entire process.  
19 MR. RATTINER: And are those  
20 fees being accrued, let's say, in early  
21 2009, late 2008?  
22 THE WITNESS: They are not  
23 being accrued because the understanding  
24 of the brokers is they are only going to  
25 get paid if we get paid, and even that's

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1 DAVID SMITH  
2 not a certainty. The brokers no  
3 longer -- when we made that arrangement  
4 with the brokers, they worked for McGinn  
5 Smith & Company. They no longer work  
6 for McGinn Smith & Company. So I am not  
7 sure, as I mentioned a moment ago,  
8 whether that -- whether that is a legal  
9 obligation, whether it's an ethical  
10 obligation. Those are all questions to  
11 be answered.  
12 MR. RATTINER: And were you  
13 aware the net capital impact in  
14 December of 2008 if you were to pay  
15 those reps, to the firm McGinn Smith,  
16 the broker-dealer?  
17 THE WITNESS: Well, if I got  
18 paid, I would have had the money to pay  
19 them.  
20 MR. RATTINER: Well, the  
21 payment is still due to the reps,  
22 obviously, and the fees are being  
23 accrued?  
24 THE WITNESS: No, it's not  
25 obvious at all.

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1 DAVID SMITH  
2 MR. RATTINER: Why is that?  
3 Is there an agreement with the reps  
4 saying that they agreed not to be paid  
5 until the broker-dealer is paid?  
6 THE WITNESS: The agreement  
7 with the reps was that we were not being  
8 paid by the funds and so therefore they  
9 were not being paid.  
10 MR. RATTINER: Is that in  
11 writing?  
12 THE WITNESS: In 2008 -- I  
13 think that is correct, maybe it was  
14 2000 -- maybe it was 2007, we paid the  
15 reps without taking the fees. We paid  
16 them out of capital. And so those fees  
17 accrued, and it was a large number. It  
18 was about 800 grand. You know what? I  
19 want to excuse myself.  
20 MR. NEWMAN: Off the record.  
21 (Whereupon a Recess is Taken.)  
22 MR. RATTINER: So back on the  
23 record. I think we left off with,  
24 Mr. Smith, we were talking about whether  
25 or not you had a written agreement with  
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1 DAVID SMITH  
2 the reps that would indicate they are  
3 foregoing their payment based on the  
4 underwriting fee -- or the annual  
5 commission fee, whatever you want to  
6 term the 2 percent?  
7 THE WITNESS: If that's a  
8 question, we have no written agreement.  
9 MR. RATTINER: Okay. How did  
10 you determine that you were not  
11 violating the capital rules by not  
12 paying the reps or booking the  
13 liability?  
14 THE WITNESS: Because they are  
15 only due and payable if the commissions  
16 are collectable.  
17 MR. RATTINER: And how did you  
18 base that determination?  
19 THE WITNESS: That is the  
20 policy of the firm. We don't pay unless  
21 we are paid.  
22 MR. RATTINER: And how does  
23 that coincide with the net capital rule  
24 with 15c3-1, for instance?  
25 THE WITNESS: Well, if we  
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1 DAVID SMITH  
2 don't have a liability, we don't have a  
3 net capital violation.  
4 MR. RATTINER: You have a  
5 payable due to the broker-dealer.  
6 THE WITNESS: No, we don't  
7 have a payable due.  
8 MR. RATTINER: Why is that?  
9 THE WITNESS: We only have a  
10 payable due if we are paid.  
11 MR. RATTINER: You have an  
12 accrued payable?  
13 THE WITNESS: No, we don't  
14 have an accrued payable because the  
15 commissions are paid when collected.  
16 MR. RATTINER: Right, but the  
17 broker-dealer is owed those funds for  
18 the 2 percent per year. As you stated  
19 before, you are now taking some of those  
20 monies currently based on accrued  
21 numbers from previous years.  
22 THE WITNESS: But what you are  
23 talking about is whether I have a  
24 payable to my brokers, and the policy  
25 with my brokers is, unless I collect the  
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1 DAVID SMITH  
2 cash, they don't get paid. So I don't  
3 have a payable, therefore I don't have a  
4 net capital violation.  
5 MR. RATTINER: And how did you  
6 determine that that is acceptable  
7 practice within the net capital rules,  
8 is my question?  
9 MR. FRANCESKI: What is that?  
10 MR. RATTINER: Mr. Smith has  
11 determined that if there is no payment  
12 made to him, he's not going to pay his  
13 brokers, and that is your policy?  
14 THE WITNESS: That's our  
15 policy. So if I am not going to pay my  
16 brokers, I don't know why I would have a  
17 payable on my books. I don't understand  
18 the logic.  
19 MR. RATTINER: So my question  
20 is did you receive counsel or advice  
21 from anyone to say that that's an  
22 acceptable practice?  
23 THE WITNESS: No.  
24 MR. RATTINER: Okay. If you  
25 were to book that liability back in 2008  
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1 DAVID SMITH  
2 to the -- payable to the brokers, would  
3 that have impaired your capital?  
4 THE WITNESS: I would think  
5 so. If we -- but, you know, in that  
6 logic, you could say that from 2002 --  
7 or, excuse me, 2003 I had a payable for  
8 the next four years, and I should have  
9 accrued that on my books, and I don't  
10 think anybody would suggest that's  
11 logical.  
12 MR. RATTINER: Did you ever  
13 indicate to any of your reps that this  
14 would be the case in writing, to the  
15 reps -- not an agreement, per se, but  
16 actually just in writing that this is  
17 going to be the payout structure?  
18 THE WITNESS: No.  
19 MR. RATTINER: And who did you  
20 have discussions with to determine that  
21 this was an acceptable practice within  
22 McGinn Smith? Did you discuss this with  
23 anyone?  
24 MR. FRANCESKI: Who do you  
25 mean by anyone, Chris?

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1 DAVID SMITH  
2 MR. RATTINER: Anyone within  
3 the firm, within the broker-dealer?  
4 THE WITNESS: The decision was  
5 made at the highest levels of  
6 management, which would be myself and  
7 Mr. McGinn.  
8 MR. RATTINER: And how about  
9 the FINOP, which would have been Mr.  
10 Rees at this time?  
11 THE WITNESS: We discussed it  
12 with him, but I guess it's fair to say  
13 he didn't have a bone.  
14 MR. RATTINER: Okay. I am  
15 going to introduce the next exhibit.  
16 MR. NEWMAN: Let me go back to  
17 that.  
18 MR. RATTINER: I am not going  
19 to introduce the next exhibit.  
20 MR. NEWMAN: Did Mr. Rees  
21 offer an opinion about that issue?  
22 THE WITNESS: I don't believe  
23 so.  
24 MR. RATTINER: I am now going  
25 to introduce the next exhibit,

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1 DAVID SMITH  
2 Exhibit 21.  
3 (Whereupon Exhibit 21 is  
4 Marked.)  
5 BY MR. RATTINER:  
6 **Q Mr. Smith, in front of you is an**  
7 **e-mail from yourself to Mr. Guzzetti. It's dated**  
8 **December 10th, 2008 at 10:43 a.m., and the subject is**  
9 **note commissions.**  
10 A (Reviewing).  
11 **Q Take a moment to review that.**  
12 A Okay.  
13 **Q Did you write this e-mail?**  
14 A I did.  
15 **Q Do you remember writing this e-mail?**  
16 A Now that I see it, yeah.  
17 **Q And what was the reason for the**  
18 **e-mail?**  
19 A Well, I guess if you read the first  
20 paragraph, evidently despite us paying the brokers  
21 without receiving payments in '08 -- remember, this  
22 is December of '08, so we didn't take any of those  
23 fees during the entire year of '08. It's fairly  
24 self-explanatory. We were -- we were capital  
25 constrained.

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1 DAVID SMITH  
2 I had told the brokers repeatedly  
3 that there was -- not going to pay them. We would  
4 try to pay them out on a schedule basis the best we  
5 could. We did do that. Somewhere along the line in  
6 '09 we were unable to continue to meet that schedule,  
7 and we informed them of such.  
8 **Q The last paragraph says, we have a**  
9 **net pay of approximately \$360,000 due. Is that for**  
10 **commissions from 2008?**  
11 A That is the remaining commissions,  
12 which I think in most part would be 2008 and 2009.  
13 It was for the remaining commissions due on the LLCs.  
14 **Q Are commissions payable once a year**  
15 **with regard to the LLCs?**  
16 A Yes.  
17 **Q And when was that payment typically**  
18 **made in 2007?**  
19 A It was typically made in December.  
20 **Q So in December '07 a payment was**  
21 **made?**  
22 A Correct.  
23 **Q And how much was that payment?**  
24 A I think those payments approximated  
25 about \$800,000.

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1 DAVID SMITH  
2 MR. FRANCESKI: You two seem  
3 to know what you are talking about, but  
4 are we talking about commissions to the  
5 brokers?

6 THE WITNESS: Don't ever  
7 assume that we know what we are talking  
8 about.

9 MR. FRANCESKI: You seem to be  
10 having a nice conversation. Was it  
11 commissions to the brokers?

12 MR. RATTINER: Correct.

13 THE WITNESS: Yes. There's a  
14 net and a gross. We would get paid the  
15 gross, the firm would, and then the net  
16 would be payable to the brokers.

17 BY MR. RATTINER:

18 **Q So based on that \$800,000 payment,**  
19 **does that mean that 440,000 was paid at some time**  
20 **prior to December of 2008 for 2008?**

21 A I think that's -- I think the reason  
22 the amount is less, Chris, is because remember, a  
23 couple of funds had matured. First Independent  
24 income had matured, and First Excelsior, if it hadn't  
25 matured, it was going to mature, I think, in

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1 DAVID SMITH

2 the whistle.

3 **Q So percentage-wise, out of the 360,**  
4 **how much would have been paid based on this --**

5 A Well, if we kept to the schedule, and  
6 I don't know if we did, but if you assume that we  
7 were going to pay 16 and two-thirds of it, that would  
8 be roughly -- 16 and two-thirds, two-thirds of --

9 **Q \$16,000?**

10 A -- of the net pay, 2.78 a month  
11 (Mumbling) looks like we probably would have paid  
12 about 35, \$40,000, and I think -- I think that fits  
13 with my understanding of where we are because I am  
14 quite certain the number that I've reserved, and I've  
15 talked about here this afternoon, is 304,000. So if  
16 you net that off of 360, that means we paid roughly  
17 56,000 in that time frame. That sounds about right?

18 **Q Now, that reserve does not include**  
19 **the 2009, however?**

20 A That's it. That is what is owed for  
21 these guys forever including -- including FAIN up  
22 through '10 if it was paid. That's all that's  
23 possibly owed.

24 **Q Well, I am confused there. If this**  
25 **360 reflects 2008 and 2009, we have an additional --**

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1 DAVID SMITH

2 January '09.

3 The fees were actually payable  
4 2 percent a year for four years even though the funds  
5 were five years. So FIIN and FEIN had already been  
6 paid. So what we are talking about here is Third  
7 Albany Income Notes and First Advisory.

8 **Q And how about for 2009? What would**  
9 **be payable in December of '09? Similar number?**

10 A No, it wouldn't be a similar number  
11 because the only thing that would be left, I think,  
12 had we paid them, and I guess that's your assumption,  
13 the only one that would be left would be First  
14 Advisory.

15 **Q And what would that payment be?**

16 A 1 percent of 5 million is 50,000.  
17 2 percent of (Mumbling), probably would have been --  
18 probably this. Probably this number here, yeah.

19 **Q So at this point out of this 360,000**  
20 **identified on this exhibit, how much of that was**  
21 **paid, based on this payment plan right above that**  
22 **paragraph?**

23 A I don't know. I think -- I think we  
24 were able to make those payments through maybe April  
25 or May. I think it was sometime there that we blew

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1 DAVID SMITH

2 A That just reflects what -- in 2008.

3 This is written in December 2008. We had remaining a  
4 net pay of \$360,000 due, and I think that was what  
5 was going to be due in -- I think there's very little  
6 due in '09, because there's nothing left. The only  
7 thing that's left that would be payable in '09 would  
8 be FAIN, okay.

9 **Q Right. I thought you said that was**  
10 **360,000?**

11 A No, that sounds too high. That's  
12 impossible. Oh, I know why, because I did it at  
13 gross. You've got \$5 million at 1 percent so that's  
14 \$50,000 at roughly a 50 percent payout, so that's 25  
15 grand, write that down. And we've got \$15 million at  
16 2 percent, so that's \$300,000, at a 50 percent  
17 payout, that's 150.

18 So it would be -- looks like it would  
19 be about 175, and then what's more critical, which I  
20 didn't think about, is that I don't get paid or  
21 McGinn doesn't get paid. Any of our clients, we  
22 never took -- we never took commission. We just  
23 earned salaries. We never got -- all commissions  
24 that were due went to the firm.

25 So this number is a net number that

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1 DAVID SMITH  
2 would be due to the brokers, and that's why it's  
3 lower. So that is the explanation.  
4 **Q So based on --**  
5 A So based on what I am saying is the  
6 175 that I just threw at you --  
7 **Q -- plus the 300?**  
8 A Yeah, it's going to be a lot lower  
9 than that because a lot of those notes were sold by  
10 myself and therefore they would be counted.  
11 **Q Percentage-wise, how many of the 300**  
12 **do you think would be your sales?**  
13 A Oh, boy. I don't know because you  
14 are just talking about FAIN. I mean, I -- you know,  
15 I don't know.  
16 **Q Is it a small, I mean, 10 percent, 50**  
17 **percent?**  
18 A Yeah. Well, yeah -- no, it's not 50  
19 percent, no. It may be 15 percent, something like  
20 that.  
21 **Q Okay.**  
22 A But that's, that is the old WAG.  
23 **Q So a total there somewhere in excess**  
24 **of \$400,000 currently owed to brokers?**  
25 A No. Right now -- right now I know

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1 DAVID SMITH  
2 the number. It's 304,000 because I've had it  
3 reconciled with Cooper. So that's --  
4 **Q Right. That doesn't jibe with the**  
5 **math we are doing here.**  
6 A Well, I guess the math that I did  
7 here is that if we owed \$360,000 in December 10th of  
8 '08, and we now owe 304,000, that would suggest that  
9 I paid roughly -- I, McGinn Smith & Company, paid  
10 roughly \$56,000 in this payment plan.  
11 **Q Right.**  
12 A So now if you want to see did we  
13 actually come up with \$56,000, if we can assume that  
14 we paid it for six months, and I don't know that for  
15 a fact, but I think it was somewhere in May or June,  
16 and we were, in effect, for that six months paying  
17 the 16 and two-thirds due in seven-eighths of the  
18 money owed, so 16 and two-thirds of \$360,000 is  
19 two-thirds of 360, is -- 24 -- excuse me, 16 and  
20 two-thirds, I apologize, is one-sixth. I've got to  
21 go back to school.  
22 So one-sixth of 360 is \$60,000 which  
23 gets us pretty damn close to 304, doesn't it?  
24 **Q Okay.**  
25 A Did I lose you there?

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1 DAVID SMITH  
2 **Q Yeah, that's all right.**  
3 A No. I made that -- I was looking at  
4 16 and two-thirds, and I am getting tired, and I was  
5 thinking -- 16 and two-thirds is one-sixth, right?  
6 So one-sixth of \$360,000 is \$60,000.  
7 **Q Right.**  
8 A And if we started with 360 and we  
9 minus 60, and we are down to 300, and my number is  
10 304.  
11 **Q Right. I guess what I'm missing is**  
12 **that number is not taking into account 2009, the 175**  
13 **we just came up with?**  
14 A I don't know if anything was due in  
15 2009. I am saying that the funds only have four  
16 years that we pay them. They have a five-year life.  
17 **Q That's fine. That's fine. So**  
18 **somewhere in excess of 300,000 is owed the brokers?**  
19 A That is correct.  
20 **Q Did you indicate to Mr. Rees not to**  
21 **accrue that amount of money?**  
22 A I did.  
23 **Q And when did that conversation take**  
24 **place?**  
25 A I don't think we had -- again, I

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1 DAVID SMITH  
2 don't think we ever accrued that money. I mean, the  
3 policy -- if you take the position that you folks  
4 seem to be taking, you know, that you have some  
5 desire of taking, you could go back to 2003 and tell  
6 me that I had an accrual for the next five years to  
7 pay brokers, pick a number, \$4 million.  
8 So, you know, who handles their books  
9 and records that way? I mean, we don't even know we  
10 are going to be alive in four years. I mean, the  
11 fact is, is that brokers are paid when they get a  
12 commission. He's got a mutual fund that he sold, and  
13 he's looking for trailers, I don't say, for the next  
14 five years you are going to get trailers, I am going  
15 to accrue that, just --  
16 **Q Okay. But, again, you didn't**  
17 **determine that based on the rule, you determined that**  
18 **based on your own procedure --**  
19 A Okay.  
20 **Q -- is that correct?**  
21 A I guess that's been the rule in the  
22 practice of 29 years in the business. I don't  
23 think -- nobody's ever told me --  
24 **Q That's fine.**  
25 A -- we have been through lots of

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1 DAVID SMITH  
2 audits, that you are supposed to accrue future  
3 commissions.

4 **Q Okay.**

5 A I think it payable within a certain  
6 period of time. Isn't it 30 days or something?  
7 Nobody will give me an answer.

8 MR. ROWEN: We have the  
9 answers. We just can't give them to you  
10 on the record.

11 MR. RATTINER: Any questions?

12 EXAMINATION

13 BY MR. ROWEN:

14 **Q I want to tie a few things together**  
15 **with regards to MSTF. I will take the e-mail back,**  
16 **but we can look at Exhibit 20 if we need to. You**  
17 **spoke of a specific class of preferred stock that**  
18 **MSTF was allocated.**

19 **Could any other entity or person**  
20 **purchase that class of preferred stock of McGinn**  
21 **Smith & Company?**

22 A No.

23 **Q From what I can tell, and what I**  
24 **guess we've discussed, the LLCs paid monies or loaned**  
25

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1 DAVID SMITH  
2 created a new class of preferred stock for any  
3 investors to buy, including MSTF, then the answer is,  
4 yeah, could have done that.

5 **Q And including the LLCs?**

6 A They could have -- yeah, they could  
7 have been eligible to buy it, sure.

8 **Q Okay. So the LLCs were holding cash,**  
9 **the broker-dealer was in need of cash?**

10 **Is that our starting point and our**  
11 **end point?**

12 A Well, I think -- I think it is a  
13 statement that I would support, yeah, at that time.  
14 I mean, I don't have the balance sheet in front of me  
15 but I think that was -- I mean, if you go back to --  
16 what was this time period? (Reviewing), basically in  
17 '09 -- certainly, in April '09 I know we were in cash  
18 needs. I can't tell you with any certainty whether  
19 November of '08. I don't know what the balance sheet  
20 was, but I know in April of '09 we were in difficulty  
21 because I was coming back from Florida, and I got a  
22 call from NFS that we were, you know, under their  
23 minimum or something. We were under the 250. So I  
24 think we were at around 175.

25 So we were -- I specifically remember

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1 DAVID SMITH  
2 **monies to MSTF that would have been otherwise due to**  
3 **MS Advisors, MS Capital Holdings, perhaps the**  
4 **broker-dealer?**

5 A That is correct.

6 **Q And MSTF used those funds to purchase**  
7 **said class of preferred stock?**

8 A Correct.

9 **Q Rather than go through multiple**  
10 **entities, could a new class of preferred stock of**  
11 **McGinn Smith have been created for the four funds to**  
12 **directly invest in?**

13 A I think so. I don't see why not.

14 **Q Why was the path chosen to go through**  
15 **MSTF instead of a direct one?**

16 A Didn't really give that a lot of  
17 thought. I don't think the -- you premised or  
18 prefaced your remarks by saying we would have created  
19 a special class of preferred for the LLCs to buy.  
20 There was never any intent that the LLCs were, in  
21 effect, going to do that at the time we did MSTF. I  
22 mean, MSTF was a transaction that stood on its own,  
23 and there was no commitment by the LLCs to do that.

24 So, you know, I guess if you framed  
25 the question differently and said could we have

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1 DAVID SMITH  
2 having a cash need in April of '09.

3 **Q What was the cause of your NFS**  
4 **balance to go below a certain threshold?**

5 A That would be expenses in excess of  
6 revenues.

7 **Q That were paid out of the NFS**  
8 **account?**

9 A No. No. I mean, obviously every  
10 month one has to compute their net capital. NFS had  
11 a requirement for us to have a net capital of 250.  
12 We dipped below that, and they got out of sorts with  
13 that.

14 **Q So it's not specific to any certain**  
15 **NFS account balance?**

16 A No. No. Just, we were not  
17 generating enough income to, you know -- let's assume  
18 the month before our net capital was 250, and we lost  
19 \$75,000 we were down to 175. They took exception to  
20 that.

21 **Q So the broker-dealer, at least we**  
22 **know in 2009, needed the cash, and the LLC had the**  
23 **cash.**

24 **I guess I am still trying to figure**  
25 **out why don't you paint a direct line and use the**

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1 DAVID SMITH

2 **LLCs funds to purchase preferred stock in the**  
3 **broker-dealer since you could create a new class for**  
4 **anyone to invest in, why involve another entity?**

5 A You know, I don't know. I don't have  
6 an answer for it. I mean, I could have -- I put a  
7 hundred grand of my own money into the firm around  
8 that April time, and I ask myself every day why I  
9 didn't take the fees and put it in and not put my own  
10 money in. So I don't know the answer but that's the  
11 way we did it.

12 MR. NEWMAN: As we sit here  
13 today, how much did you earn in the way  
14 of fees, McGinn Smith?

15 THE WITNESS: Regarding these  
16 LLCs?

17 MR. NEWMAN: Yeah.

18 THE WITNESS: Over the period  
19 of time, five years, six years?

20 MR. NEWMAN: Yeah.

21 THE WITNESS: I think the  
22 total of fees from the three entities  
23 were about \$12 million, and payable for  
24 the brokers were -- you know, that was  
25 probably -- half of that was brokerage

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1 DAVID SMITH

2 netting that number with a number of  
3 things including the collateralized, as  
4 you referred to them, loans.

5 MR. NEWMAN: \$12 million is  
6 the aggregate gross financial benefit  
7 that McGinn Smith and all its affiliates  
8 from the LLC offerings?

9 THE WITNESS: I believe that  
10 is the number, yes.

11 MR. NEWMAN: That would  
12 include all the loans and investments  
13 made to different companies?

14 THE WITNESS: That is the  
15 gross number, and then off of that, what  
16 I am saying is you are going to allocate  
17 those fees that weren't taking that are  
18 covering those, and then the commissions  
19 and all of that, and so, you know, at  
20 the end of the day you have a number  
21 that's, you know, seriously diminished.

22 MR. NEWMAN: What do you mean  
23 seriously diminished?

24 THE WITNESS: Well, it's not  
25 \$12 million.

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1 DAVID SMITH

2 fees and probably 60 percent of that was  
3 payable to them. So it's probably at  
4 least three and a half million went to  
5 the brokers. So over time the firm  
6 would have earned the difference.

7 MR. NEWMAN: Do you feel that  
8 you benefited financially from the LLC  
9 offerings?

10 THE WITNESS: McGinn Smith &  
11 Company?

12 MR. NEWMAN: Yeah.

13 THE WITNESS: That is a  
14 business that we pursued, yeah. I mean,  
15 that's the business we are in is  
16 creating investment opportunities, and  
17 we sell them, and we get paid for them.  
18 That's what we do.

19 MR. NEWMAN: Does that \$12  
20 million include all the monies that were  
21 loaned and paid to all the affiliated  
22 companies from the LLCs or is that the  
23 pure fees?

24 THE WITNESS: That is the  
25 gross number. So you are going to be

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1 DAVID SMITH

2 MR. NEWMAN: So when we see  
3 the books and records showing payments  
4 being made, that that money was never  
5 paid?

6 THE WITNESS: Yeah, that's  
7 exactly right. Yeah. I think about 7  
8 million was paid, and about 5 million  
9 was not.

10 MR. NEWMAN: So 7 million is  
11 paid represents what?

12 THE WITNESS: Primarily  
13 commissions but some monies to MS  
14 Advisors and some money to MS Capital  
15 Holdings.

16 MR. NEWMAN: Those were the  
17 offering fees. We are not talking about  
18 monies, we are talking --

19 THE WITNESS: No, I am talking  
20 all the fees. I am talking the offering  
21 fees, which were basically 2 percent a  
22 year for four years.

23 MR. NEWMAN: Right.

24 THE WITNESS: MS Advisors was  
25 entitled to 1 percent a year --

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1 DAVID SMITH  
 2 MR. NEWMAN: Right.  
 3 THE WITNESS: -- for five  
 4 years. And McGinn Smith Capital  
 5 Holdings was entitled to one quarter of  
 6 1 percent for five years. The aggregate  
 7 of all of those fees, because I have  
 8 just recently looked at the schedule, is  
 9 approximately \$12 million.  
 10 Of that \$12 million, at the  
 11 time the schedule was presented to me,  
 12 we had paid about \$7 million. That  
 13 leaves \$5 million. Against that  
 14 \$5 million, there is, in loans, about \$3  
 15 million, and then there are, against  
 16 that, there's some other due to,  
 17 to/from's, there's the brokers, and I  
 18 believe the net number that is now owed  
 19 to the entities, the aggregate entities,  
 20 if you will, is approximately \$700,000.  
 21 MR. NEWMAN: 700, I'm sorry?  
 22 THE WITNESS: \$700,000.  
 23 MR. NEWMAN: And that's owed  
 24 by whom to whom?  
 25 THE WITNESS: That's owed by  
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1 DAVID SMITH  
 2 the funds, in the aggregate funds, the  
 3 LLCs in the aggregate, to, in the  
 4 aggregate, the three entities of McGinn  
 5 Smith & Company.  
 6 MR. NEWMAN: You said you  
 7 looked at a schedule recently. What  
 8 schedule did you look at?  
 9 THE WITNESS: The schedule  
 10 that was put together for me by Brian  
 11 Cooper.  
 12 MR. NEWMAN: And where is that  
 13 schedule?  
 14 THE WITNESS: It's in our  
 15 office.  
 16 MR. NEWMAN: Okay. We  
 17 would -- FINRA will request a copy of  
 18 that schedule be provided pursuant to  
 19 FINRA Rule 8210.  
 20 When was the schedule  
 21 prepared?  
 22 THE WITNESS: It's been -- I  
 23 testified earlier that we've been  
 24 working on it for a couple of months.  
 25 The one I am referring to, the last one  
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1 DAVID SMITH  
 2 I saw I think was dated 1-26. So that's  
 3 seven days ago.  
 4 BY MR. ROWEN:  
 5 **Q Is this the same document you**  
 6 **referred to that was titled accrued fees?**  
 7 A That was my title. I don't know if  
 8 that was the exact title. You were asking for some  
 9 name, and I don't know what the file is. That is a  
 10 logical title, but I don't know, yeah, but that's the  
 11 one we are talking about, yes.  
 12 MR. NEWMAN: How lengthy is  
 13 the schedule? Is it multiple pages?  
 14 THE WITNESS: Oh, no. It's  
 15 two pages.  
 16 MR. NEWMAN: And what  
 17 information is on that schedule?  
 18 THE WITNESS: It shows the  
 19 fees earned under the three categories:  
 20 Underwriting, advisory, trustee and  
 21 capital holdings. Broken down by fund,  
 22 then the next box shows all the fees  
 23 that were paid up through 2007. There's  
 24 another category for fees earned  
 25 post-2007, fees paid since 2007,  
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1 DAVID SMITH  
 2 allocation of the liabilities that we  
 3 have spoken about in the last couple of  
 4 days. And the last category is the one  
 5 that Chris and I have been talking about  
 6 as to whether that is an accrual that's  
 7 necessary.  
 8 MR. NEWMAN: And that's  
 9 prepared by Mr. Cooper on your behalf?  
 10 THE WITNESS: Yes.  
 11 MR. NEWMAN: Where did Mr.  
 12 Cooper obtain the information for the  
 13 schedule?  
 14 THE WITNESS: Well, I mean, he  
 15 knows the aggregate dollars that the  
 16 offerings are, he knows what the fees  
 17 are, so we know what the gross fees are  
 18 due. We know what has been paid because  
 19 they are in the Quicken records, and  
 20 therefore one simply subtracts one from  
 21 the other to see what the net is.  
 22 MR. NEWMAN: Did you give him  
 23 any information for the schedule?  
 24 THE WITNESS: No. The only  
 25 other information I gave him was -- I  
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1 DAVID SMITH  
2 was contradictory, wasn't I? I said no,  
3 and then I started to tell you what  
4 information. I went over the loans and  
5 related investments to make sure that he  
6 had attributed all of those to our fees  
7 so that there was no misunderstanding,  
8 and we talked about the commissions and  
9 then he put it together.

10 MR. NEWMAN: Why did you  
11 prepare the schedule?

12 MR. FRANCESKI: Why did he?

13 THE WITNESS: Why did he or  
14 why did I?

15 MR. NEWMAN: Why was the  
16 schedule prepared?

17 THE WITNESS: I said we are,  
18 A, want to make sure that we, on the  
19 collateralized loan side, we are going  
20 to be redoing balance sheets, and we  
21 want to make sure that everything is  
22 accounted for when we do that.

23 We want to make sure that any  
24 fees that actually come to us are within  
25 the time frame and within the

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1 DAVID SMITH  
2 constraints that we laid out as relates  
3 to either legal fees, or what have you,  
4 and I don't want to make -- I don't want  
5 to have any errors.

6 MR. NEWMAN: Why are you  
7 redoing the balance sheets?

8 THE WITNESS: Because I think,  
9 and this hasn't been totally thought  
10 out, and it will have to be consulted  
11 with counsel, but I think in light of  
12 the number of arbitrations and  
13 litigations as a result of the  
14 non-performance of the funds, that we  
15 are going to have to basically put a  
16 restructuring plan to the note holders.

17 The attempt that I made by  
18 Fiat, if you will, by proposal, you  
19 know, we haven't paid anybody but the  
20 seniors so there's been no impact on the  
21 waterfall of monies due, but I am  
22 concerned that if we follow through with  
23 the structured plan as proposed that  
24 seniors who I had always indicated to my  
25 communication, you know, had a

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1 DAVID SMITH  
2 legitimate beef, if you will, because  
3 they are first on the waterfall, they  
4 deserve to be paid before anybody else,  
5 and it's pretty apparent that we are not  
6 going to be able to do anything without  
7 litigation.

8 And once one starts down that  
9 path, you are not going to be able to  
10 collect money back from people who then  
11 is determined you shouldn't pay. And so  
12 we are going to take the position, I say  
13 we, I have not thought it totally  
14 through, but I think we will present any  
15 restructuring plan to all the note  
16 holders, seek their approval, and make  
17 sure that anything that's put together  
18 is done the way the indenture requires  
19 it and so we avoid any legal questions  
20 at least as regards to the  
21 restructuring.

22 MR. NEWMAN: How are you going  
23 to redo the balance sheets?

24 THE WITNESS: Well, we are  
25 going to, you know, basically try to

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1 DAVID SMITH  
2 assess how we should carry some of those  
3 assets. As I have said repeatedly and  
4 continue to take that position, it's  
5 not -- it's not black and white. I  
6 mean, there are assets that, you know,  
7 they are very hard to measure as to what  
8 they are worth. I have used the example  
9 with, I think with Mike last time he was  
10 up in December, I virtually had written  
11 off one of our investments because, you  
12 know, there was no operating cash. The  
13 CEO had left. Quite frankly, I thought  
14 the investment was gone.

15 December we were successful in  
16 selling it to a public company for  
17 \$450,000. You know, had I written that  
18 off, it would have been nice to get it  
19 back, you know, if I was faced with that  
20 decision today and I didn't have any  
21 potential buyer, I'd probably still  
22 write that one off. But it's not a  
23 perfect world. You don't know what you  
24 are going to do. But I am certainly  
25 going to take a much harder look than we

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1 DAVID SMITH  
 2 have because I think if you are going to  
 3 present a plan to your investors, I  
 4 think it will have to be far more on a  
 5 disclosure basis.  
 6 I think you will have to not  
 7 only put the balance sheet out and the  
 8 total income statement and all the fees  
 9 that have been paid and will have been  
 10 paid, try to give some write-up of every  
 11 investment to some degree as to what you  
 12 think it's worth and what the potential  
 13 is, if any, and try to be far more  
 14 transparent. If you are going to ask  
 15 people to vote on something, they have  
 16 to have information to vote on it.  
 17 And whether they choose, armed  
 18 with that information, to remove the  
 19 advisor of the trustee, which they both  
 20 have the ability to do with a majority  
 21 vote, I don't know. I don't know if  
 22 anybody will lead that bandwagon. I  
 23 don't think it is a particularly good  
 24 idea, but it doesn't mean they might not  
 25 do it. And we are just not prepared to

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1 DAVID SMITH  
 2 put ourselves in harm's way anymore. We  
 3 have suffered through these things, and  
 4 there seem to be no end to them.  
 5 MR. NEWMAN: You say we  
 6 suffered. You've received millions of  
 7 dollars from these LLC offerings?  
 8 THE WITNESS: Yeah. Well --  
 9 MR. NEWMAN: That is  
 10 suffering?  
 11 THE WITNESS: Yeah, I am  
 12 suffering, because I don't have a  
 13 business anymore. I don't have an  
 14 income. I just got hit with an \$805,000  
 15 award, so, yeah, I say that's suffering.  
 16 MR. FRANCESKI: I am going to  
 17 object to anything further on this,  
 18 Mike. Unless you've got a real point to  
 19 make here other than --  
 20 THE WITNESS: This is the  
 21 point that he's made from the Goddamn  
 22 day we walked in here two days ago.  
 23 He's got a hard-on that somebody is  
 24 getting some money, and he isn't, and I  
 25 am -- you know, the last time I walked

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1 DAVID SMITH  
 2 out of this room was because I watched  
 3 you rolling your eyes, giving me this  
 4 crap every time I made a statement to  
 5 Chris or Steve.  
 6 I don't need that shit, you  
 7 know. So you either act professionally  
 8 and address this the way you should, or  
 9 we are out of here, and we will deal  
 10 with the consequences later. Is that  
 11 the way you want to do it?  
 12 MR. NEWMAN: The record should  
 13 reflect the witness is raising his voice  
 14 and pointing his finger at me when he's  
 15 making that statement.  
 16 MR. FRANCESKI: And the record  
 17 should reflect that Mr. Newman, during  
 18 Mr. Smith's testimony, was guffawing,  
 19 rolling his eyes, shaking his head as to  
 20 almost every answer that Mr. Smith gave  
 21 in the last 10 minutes before he took a  
 22 break. That's what the record should  
 23 reflect.  
 24 MR. NEWMAN: That's your  
 25 characterization.

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1 DAVID SMITH  
 2 THE WITNESS: And that is my  
 3 characterization.  
 4 MR. NEWMAN: That's not mine.  
 5 MR. FRANCESKI: Actually, it  
 6 wasn't my characterization because I  
 7 wasn't looking at Mr. Newman.  
 8 THE WITNESS: All right, guys.  
 9 It's quarter of 6. You got to get home,  
 10 I got to get home.  
 11 MR. NEWMAN: We are not  
 12 finished with our questioning so.  
 13 THE WITNESS: I am finished.  
 14 MR. NEWMAN: So you are going  
 15 to walk out?  
 16 THE WITNESS: I am going to  
 17 walk out. I am not real happy with the  
 18 way I have been treated. I don't think  
 19 I have been treated professionally. I  
 20 don't think I have been given any  
 21 respect, and I'm not going to put up  
 22 with it. I don't need this. You guys  
 23 work for us. You're FINRA. I am a  
 24 member of FINRA. You got a job to do.  
 25 I respect it. I come down here, but

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1 DAVID SMITH  
 2 when I come down here, I expect respect.  
 3 I don't expect you to look at me every  
 4 time I make a statement and suggest that  
 5 I am either lying through my teeth or I  
 6 have no credibility, and you give me  
 7 this stuff and you roll your eyes and  
 8 you put your books down. You have been  
 9 doing it for two days, Mike, two days.  
 10 Maybe you don't even know you are doing  
 11 it.  
 12 MR. NEWMAN: Let me say this.  
 13 There are investors here who put  
 14 millions of dollars into your company,  
 15 and we have every legitimate right to  
 16 ask questions how those investment  
 17 monies have been spent. Every question  
 18 has been asked has been a fair question,  
 19 a relevant question from our standpoint,  
 20 whether you like it or not. We think  
 21 you have been treated fairly. The fact  
 22 you don't like -- the fact you don't  
 23 like you have been asked about certain  
 24 transactions, that has nothing --  
 25 THE WITNESS: I didn't say

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1 DAVID SMITH  
 2 that. I have not -- I have not made a  
 3 comment about the level of questions or  
 4 the kind of questions.  
 5 MR. NEWMAN: Any question that  
 6 has been raised has been difficult. Let  
 7 me talk now. Any question I have been  
 8 asked has been difficult. You've argued  
 9 and become combative and argumentative.  
 10 MR. FRANCESKI: I'm sorry,  
 11 Mike, but this is a question and answer  
 12 session. This is not a speech between  
 13 either of you. This is not productive.  
 14 I am not suggesting my client should be  
 15 making a speech, but neither should you,  
 16 and particularly you, given that you  
 17 know what your job is here.  
 18 You are not to give speeches  
 19 to my client. You are here to ask  
 20 questions, and my client is to answer  
 21 questions.  
 22 MR. NEWMAN: No, your client  
 23 is making accusations. I am entitled to  
 24 respond to those accusations.  
 25 MR. FRANCESKI: Not in this

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1 DAVID SMITH  
 2 forum.  
 3 MR. NEWMAN: Yes, I can.  
 4 MR. FRANCESKI: Not in this  
 5 forum.  
 6 MR. NEWMAN: I can respond on  
 7 the record to his comments.  
 8 MR. FRANCESKI: Not on this  
 9 forum. Well, then we are finished  
 10 because that's not going to be  
 11 productive, Mike. It's not productive  
 12 for you two to argue with each other.  
 13 If you want to ask a question, if you  
 14 want to get an answer, we can do that.  
 15 MR. NEWMAN: I was asking a  
 16 question, and you interrupted or he  
 17 interrupted with his speech. He was  
 18 being asked a question.  
 19 MR. FRANCESKI: You know what?  
 20 What he said was completely accurate,  
 21 but I don't want to get into that.  
 22 That's not what we are here for. Either  
 23 we do something productive, or you  
 24 should have the courtesy to call it a  
 25 day and come back another day.

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1 DAVID SMITH  
 2 MR. NEWMAN: We have a few  
 3 more questions, and then we will call it  
 4 a day.  
 5 Going back, I want to ask you  
 6 some questions about Mr. Cooper and what  
 7 his role is with McGinn Smith. What is  
 8 Mr. Cooper's role with McGinn Smith.  
 9 THE WITNESS: He works in the  
 10 finance section. He's an assistant to  
 11 Brian Shea. He keeps track of our  
 12 payments and expenses as regards to  
 13 transactions that we have done, and in  
 14 particular he tracks using the Quicken  
 15 system, the finances of the four LLCs.  
 16 MR. NEWMAN: And how long has  
 17 he been employed by McGinn Smith?  
 18 THE WITNESS: I think about  
 19 three years.  
 20 MR. NEWMAN: Is he  
 21 fingerprinted?  
 22 THE WITNESS: I don't know the  
 23 answer to that.  
 24 MR. NEWMAN: And when you  
 25 refer to the schedule that Mr. Cooper

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1 DAVID SMITH  
2 has prepared for you on January 26th,  
3 you said, 2009, had he prepared a  
4 similar --  
5 THE WITNESS: That would be  
6 2010.  
7 MR. NEWMAN: 2010, had he  
8 prepared a similar schedule for you  
9 prior to that?  
10 THE WITNESS: Yes.  
11 MR. NEWMAN: Can you explain  
12 what that document was and when it was  
13 prepared?  
14 THE WITNESS: The same  
15 schedule. It's been kind of a moving  
16 schedule over the last month or two  
17 months since when, as I have indicated,  
18 asked him to do that, and I don't know,  
19 maybe seen two or three versions.  
20 MR. NEWMAN: When was the  
21 first schedule he prepared like that?  
22 THE WITNESS: Maybe a month  
23 ago.  
24 MR. NEWMAN: And why was that  
25 prepared initially?

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1 DAVID SMITH  
2 THE WITNESS: At my request.  
3 MR. NEWMAN: And is it similar  
4 in form to what was prepared on  
5 January 2010?  
6 THE WITNESS: Yes.  
7 MR. RATTINER: Prior to that  
8 schedule being prepared in December,  
9 what was utilized with similar  
10 information, if there was anything?  
11 THE WITNESS: I think there  
12 was other schedules that were presented  
13 to me but not with the importance that I  
14 stressed on this. I can't tell you  
15 prior to the last month or two when the  
16 last one was, but similar in nature,  
17 similar in form.  
18 MR. RATTINER: Okay. I guess  
19 as part of our request we will request  
20 both schedules.  
21 MR. FRANCESKI: Put it in  
22 writing. We will review the request.  
23 MR. MCCARTHY: I have a couple  
24 of quick things.  
25

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1 DAVID SMITH  
2 EXAMINATION  
3 BY MR. MCCARTHY:  
4 **Q Can you tell me how many different**  
5 **classes of McGinn Smith preferred stock there are,**  
6 **McGinn Smith the broker-dealer?**  
7 A There would be just two. There is  
8 the one that was the 87 series, which has been with  
9 us, obviously, since '87, and this recent one that  
10 was associated with the Transaction Funding.  
11 **Q And what -- can you describe it?**  
12 A It's an 8 percent coupon. I don't  
13 know what we call it. Call it the -- I guess we'd  
14 call it the 2009 series.  
15 **Q 8 percent coupon. And is that to be**  
16 **paid annually, quarterly?**  
17 A I believe it is a quarterly payment,  
18 yes.  
19 **Q And when was that stock issued?**  
20 A I think we did Transaction Funding  
21 sometime in the spring of '09. I think. No -- had  
22 to be earlier than that, didn't it? Maybe '08.  
23 Maybe it was '08.  
24 **Q And are the payments to Transaction**  
25 **Funding current?**

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1 DAVID SMITH  
2 A You mean to McGinn Smith?  
3 **Q From McGinn Smith & Co. for the**  
4 **preferred stock?**  
5 A They are not current as of the last  
6 quarter.  
7 **Q Was the last quarter the first**  
8 **quarter that the payments were missed?**  
9 A I believe so, yes.  
10 **Q And just help me with the fees. I**  
11 **just want to make sure I did understand. The one**  
12 **aspect of the fees, the fees to -- let me preface**  
13 **that. The fees that were due to McGinn Smith and**  
14 **Co., or McGinn Smith Advisors from the four notes**  
15 **funds --**  
16 A LLCs?  
17 **Q -- LLCs, were they calculated on a**  
18 **par basis or an actual value?**  
19 A Par basis.  
20 **Q So, for instance, if the actual value**  
21 **of the funds was half, you would still get the**  
22 **calculation?**  
23 A Based on the book value of capital  
24 contributions, yes.  
25 **Q Okay. That is the same with the**

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1 DAVID SMITH

2 **payments to the reps, would be based on the par?**

3 A Yes, that is correct.

4 MR. RATTINER: Quick. You  
5 mentioned Miss Sicluna was  
6 fingerprinted, yesterday. Did she go by  
7 another name previously, I don't know if  
8 that's a married name?

9 THE WITNESS: Yes, Patty  
10 Atanasio.

11 MR. RATTINER: I don't know  
12 how to spell that one.

13 THE WITNESS: I don't either.  
14 I would say A-t-a-n-a-s-i-o. But she's  
15 been Sicluna for quite some time.

16 MR. RATTINER: Since '82?

17 THE WITNESS: No, not since  
18 '82.

19  
20 EXAMINATION

21 BY MR. ROWEN:

22 **Q I just wanted to, when we were on**  
23 **MSTF, I just had one more area I wanted to discuss,**  
24 **and that was does MSTF pay fees to McGinn Smith**  
25 **Advisors, McGinn Smith Capital Holdings?**

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1 DAVID SMITH

2 But I would have to refer to the  
3 prospectus to know that exactly.

4 **Q And so that we are clear, when you**  
5 **use the term investors there, whose investors are you**  
6 **speaking of?**

7 A The investors that invested in McGinn  
8 Smith Transaction Funding.

9 **Q And you used the word "we" in regards**  
10 **to fees.**

11 **Who is the "we"?**

12 A Regarding the fees?

13 **Q I believe it was either we earned or**  
14 **we received?**

15 A I am referring to McGinn Smith  
16 Transaction Funding. That is their business. They  
17 earn -- a percentage of fees -- maybe I was referring  
18 to we when I was talking about McGinn Smith &  
19 Company.

20 McGinn Smith & Company does a  
21 transaction, and they earn an investment banking fee,  
22 and the portion -- some portion of that fee is  
23 allocated to Transaction Funding to meet its  
24 obligations that get returned to its investors. So  
25 when McGinn Smith & Company is doing transactions and

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1 DAVID SMITH

2 A No.

3 **Q Does it pay any trustee fees?**

4 A No.

5 **Q Advisory fees?**

6 A No.

7 **Q Did it pay underwriting fees?**

8 A Yes. It was placement fees, yes.

9 **Q Does it pay legal fees?**

10 A Of their own or on behalf of McGinn  
11 Smith?

12 **Q Let's start --**

13 A The answer is no, I don't think they  
14 have paid any legal fees, so that's an easy answer.  
15 I am not aware of any legal fees that they have paid.

16 **Q And on behalf of McGinn Smith?**

17 A No.

18 **Q Any transaction-based fees?**

19 A Yes. That is the whole gist of it  
20 that the investors get a percentage of the fees that  
21 we earn on investment banking transactions, not  
22 placement fees but investment banking fees, and I  
23 think -- I think they are entitled -- it is a sliding  
24 scale, but I think it starts at 15 percent of the  
25 fees up to a certain amount, and then it goes down.

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1 DAVID SMITH

2 doing them successfully, that's how the investors and  
3 Transaction Funding is paid -- are paid.

4 **Q Is that in lieu of dividends?**

5 A It's in addition to.

6 **Q In addition to dividends. Does**  
7 **McGinn Smith Transaction Funding pay fees to anyone**  
8 **else in connection to investments it purchases?**

9 A No.

10 MR. RATTINER: Just a real  
11 quick one, in terms of arbitrations.  
12 You mentioned [REDACTED] yesterday,  
13 and I know as of yesterday nothing had  
14 been rendered as an opinion?

15 THE WITNESS: Actually, that's  
16 not true. I found out this morning that  
17 it had been rendered.

18 MR. RATTINER: Okay. So as of  
19 today, what was that?

20 THE WITNESS: It wasn't good.

21 MR. RATTINER: What were the  
22 results?

23 THE WITNESS: I haven't seen  
24 the attachment so I haven't seen the  
25 whole thing. I just got an e-mail from

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1 DAVID SMITH  
 2 our attorney, and I believe the award  
 3 was \$455,000.  
 4 MR. RATTINER: Okay.  
 5 MR. MCCARTHY: Just one more.  
 6 I just -- I got sidetracked, so I didn't  
 7 ask you about the other one.  
 8 BY MR. MCCARTHY:  
 9 **Q The other preferred stock, the McGinn**  
 10 **Smith preferred stock, can you give me the terms of**  
 11 **that?**  
 12 A Yes. Again, that's been around since  
 13 1987. It's an intrastate offering. It has the  
 14 ability to trade publicly, as long as its within New  
 15 York State resident. It is a floating rate interest  
 16 that's set every year. It's three and a half --  
 17 350 basis points over the seven-year treasury note as  
 18 of April 1st of that particular year.  
 19 **Q And is that in arrears or is that**  
 20 **currently --**  
 21 A That was current for 88 consecutive  
 22 quarters until this last quarter.  
 23 **Q Last quarter. And that's in arrears**  
 24 **currently?**  
 25 A That's right.

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1 DAVID SMITH  
 2 **Q Is there an adjustment to the**  
 3 **valuation that you are making on the books and**  
 4 **records of the entities that own these stocks to**  
 5 **reflect the arrears?**  
 6 A There will be. That's clearly  
 7 something we are going to have to do. We hadn't up  
 8 until now because they were current, and we were  
 9 under the impression that McGinn Smith would survive  
 10 another 29 years. Doesn't appear to be the case.  
 11 **Q The date of the arrears, the date of**  
 12 **the first payment that was in arrears for --**  
 13 A I believe the October payment was the  
 14 first payment in arrears. It may be the July  
 15 payment, but we are talking about the 87 series.  
 16 **Q Okay. So the 87 series?**  
 17 A I think October was the first one we  
 18 missed, but possibly July also.  
 19 **Q And you are saying there should be a**  
 20 **subsequent valuation to reflect the arrears?**  
 21 A Well, I think -- I think it's only  
 22 fair to say that there has to be a subsequent  
 23 evaluation of McGinn Smith preferred. Now, the good  
 24 news from the funds are is that they are secured by  
 25 the collateral account. But if it was in a different

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1 DAVID SMITH  
 2 entity, for example McGinn Smith Transaction Funding,  
 3 that clearly is going to have to be adjusted down.  
 4 **Q Okay.**  
 5 A Thank you.  
 6 MR. NEWMAN: While we are on  
 7 the record, we asked for a copy of this  
 8 agreement dealing with the  
 9 collateralized fees. Did you have a  
 10 chance to check on that?  
 11 THE WITNESS: We mentioned it  
 12 to Mr. McGinn. He was going to look for  
 13 it. We will see how, what kind of good  
 14 luck he had.  
 15 MR. NEWMAN: Right now you  
 16 don't know if that agreement exists?  
 17 THE WITNESS: I remember I  
 18 told you yesterday that we -- both was  
 19 drafted back in '04, '05. I haven't  
 20 seen it since that I know. Obviously,  
 21 we have been accruing the liability  
 22 since that time, so we know it's in  
 23 force.  
 24 MR. NEWMAN: Okay. And we  
 25 also discussed off the record that we

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1 DAVID SMITH  
 2 have additional questions for you. You  
 3 have indicated that you are unavailable  
 4 tomorrow morning because of an  
 5 appointment and some other personal  
 6 issues, and so we will attempt through  
 7 your counsel to arrive at a mutually  
 8 agreeable date to continue your  
 9 testimony.  
 10 So that's what we are doing.  
 11 We are continuing your testimony. We  
 12 ask that you don't discuss your  
 13 testimony with anybody other than  
 14 counsel, obviously, if we do continue to  
 15 expect this OTR at a later date.  
 16 So with that, unless there's  
 17 anything else -- any other information  
 18 or statements or questions that counsel  
 19 would like to make, we will conclude the  
 20 OTR at this time.  
 21 THE WITNESS: I will go on the  
 22 record apologizing for my outburst to  
 23 Mr. Newman.  
 24 MR. NEWMAN: Apology accepted.  
 25 (Concluded at 5:30 p.m..)

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1 I, S. Arielle Santos, C.S.R., a Registered  
2 Professional Reporter, Certified Shorthand Reporter,  
3 Certified LiveNote Reporter do hereby certify:  
4 That prior to being examined, the witness named in the  
5 forgoing deposition, was by me duly sworn to testify the  
6 truth, the whole truth, and nothing but the truth.  
7 That said deposition was taken before me at the time and  
8 place set forth and was taken down by me in shorthand and  
9 thereafter reduced to computerized transcription under my  
10 direction and supervision, and I hereby certify the foregoing  
11 deposition is a full, true and correct transcript of my  
12 shorthand notes so taken.  
13 I further certify that I am neither counsel for nor  
14 related to any party to said action nor in anywise interested  
15 in the outcome thereof.

16  
17 \_\_\_\_\_  
S. Arielle Santos  
18 Registered Professional Reporter  
Certified Shorthand Reporter - #2116  
19 Certified LiveNote Reporter  
Notary Exp. 4/201

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