SECURITIES AND EXCHANGE COMMISSION

In the Matter of:

DONALD J. ANTHONY, JR.,
FRANK H. CHIAPPONE,
RICHARD D. FELDMAN,
WILLIAM P. GAMELLO,
ANDREW G. GUZZETTI,
WILLIAM F. LEX,
THOMAS E. LIVINGSTON,
BRIAN T. MAYER,
PHILIP S. RABINOVICH, and
RYAN C. ROGERS,

Respondents.

ADMINISTRATIVE PROCCEDING

File No. 3-015514

RESPONDENT ANDREW G. GUZZETTI'S PREHEARING BRIEF

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Respondent Andrew G. Guzzetti, by and through his attorneys, Sallah Astarita & Cox, LLC, hereby submits this Prehearing Brief to address some, but not all, of the issues that will be presented at the upcoming hearings in this matter.

RELEVANT FACTS

The facts of this case have been discussed throughout the pleadings and various motions in this matter. We will not repeat those facts here. By way of a brief review, the Division of Enforcement has filed the subject OIP in relation to an alleged theft of investors' funds conducted by Timothy McGinn ("McGinn') and David Smith ("Smith"). McGinn and Smith operated McGinn Smith & Co. ("MS & Co."), a broker-dealer based in Albany, NY, before losing their securities licenses and eventually being convicted of their crimes in February of 2013. The Division of Enforcement does not allege that Mr. Guzzetti was aware of, participated in, or benefited from the crimes of McGinn and/or Smith.

The OIP is focused on the offer and sale of four income note offerings, 20 trust offerings, and one LLC offering, by MS & Co. As to Mr. Guzzetti, the OIP alleges that he failed in his duty to supervise the other Respondents, by not preventing alleged violations of the other Respondents. As will be discussed in greater depth below, the Division erroneously identifies Mr. Guzzetti as being the supervisor of all of the Respondents in the OIP.

In addition, the OIP mistakenly classifies Mr. Guzzetti as being responsible for the supervision of the private placements at issue in this matter. Finally, the Division uses the benefit of hindsight to classify normal occurrences, considering the market conditions at the time, as "red-flags" that should have caused Mr. Guzzetti to take action, despite the fact that he had no legal or professional obligation to do so.[1]

ARGUMENT

To successfully make a claim under Section 15(b)(6) of the Securities Exchange Act of 1934 ("Exchange Act"), incorporating by reference Section 15(b)(4)(E), the Division bears the burden of "showing that, under all of the circumstances, [Respondent] failed to exercise reasonable supervision." *In the Matter of Arthur James Huff*, 1991 SEC LEXIS 551, 5-6, 50 S.E.C. 524, 526 (S.E.C. 1991). Section 15(b)(4)(E) also "provides that no person shall be deemed 'to have failed to reasonably supervise any other person' if that person 'reasonably discharged the duties and obligations incumbent upon him by reason of [his firm's] procedures.'" *Id.*

In *Huff*, the Commission also held that "different supervisors may have different responsibilities depending on how each firm devises its compliance program" and that the "statute only requires reasonable supervision under the ***attendant circumstances***." *Id.*, at 528; [emphasis added]. A "factual analysis is required in each case," due to that fact that what could be considered a "reasonable discharge of supervisory duties in one case can be unreasonable in another." *Id.*

Based on the facts of the matter at hand, the Division cannot meet the burden described above. First, Mr. Guzzetti was never given the duty or obligation from MS & Co. to supervise the other Respondents' offer and sale of the private placements at issue in this matter. Second, it seems axiomatic that the Division must show there was actually a violation before it can be

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[1] We are attempting to limit this memorandum to the issues that relate directly to Mr. Guzzetti. The other Respondents have presented detailed discussions and arguments regarding this matter, and to the extent those discussions and arguments apply to claims against Mr. Guzzetti, we respectfully incorporate those arguments and discussions.

shown that Mr. Guzzetti failed to prevent that violation. Third, the alleged "red-flags" referenced in the OIP are not of a nature that would have caused a reasonable supervisor to take corrective action. Finally, those obligations that Mr. Guzzetti did have, which were akin to those of a sales manager, were executed in accordance with all applicable securities laws. As a result, the Division's claims against Mr. Guzzetti must fail.

I. **Mr. Guzzetti Was Not Responsible For Supervising The Transactions At Issue.**

The OIP erroneously alleges that Mr. Guzzetti failed to adequately supervise the activities of the 9 other Respondents in this matter, who were located in multiple offices in three states. Specifically, the OIP's allegations are centered on 26 different private placements offered during a 6 year time period from 2003 to 2009, by 9 different MS & Co. brokers, located in three separate offices, in three states. *See*, OIP.

As the Division states in the OIP, Mr. Guzzetti was first employed by MS & Co. in 2004, which eliminates an entire year of transactions involved in this matter. During his time with the firm, Mr. Guzzetti had numerous responsibilities. However, none of these responsibilities ever included the supervision of the offer or sale of the private placements at issue. Throughout Mr. Guzzetti's time with the firm, the supervision of the private placements at MS & Co. was directly handled by David Smith and Timothy McGinn. The Division's own hearing exhibits will establish this fact.

Mr. Guzzetti did not supervise any individuals at MS & Co. until October 2008, when he became branch manager of the firm's Clifton Park, office. It was only after this move that Mr. Guzzetti had any supervisory responsibilities. Only 4 of the 9 other Respondents were actually employed at the Clifton Park office: Gamello, Chiappone, Feldman, and Anthony, Jr. However, even following the move to Clifton Park, and the assumption of limited supervisory duties, Mr.

Guzzetti was not responsible for supervision of MS & Co.'s private placements. Supervision of these sales still remained with Mr. Smith and/or Mr. McGinn, depending on the offering at issue.

According to the 2007 MS & Co. compliance manual, the relevant portion of which is attached hereto as Exhibit A, all non-NYC brokers were under the supervision of David L. Smith, all brokers in the NYC office were under the direct supervision of Brian Mayer, and all brokers in the Clifton Park office were under the direct supervision of Carl Nicolosi. In addition, the compliance manual also states that both Brian Mayer and Mr. Nicolosi are under the direct supervision of David L. Smith.

The 2007 MS & Co. compliance manual also describes the process governing investments in private placements. The manual states that every subscription agreement for a private placement was to be approved by a designated principal. In the over 10 million pages of documents produced in this matter and the almost 600 premarked exhibits identified by the Division, we have been unable to locate a single private placement investment that was approved by Mr. Guzzetti.

For these reasons, it is evident that Mr. Guzzetti was not the supervisor of the offer and sale of the MS & Co. private placements at issue in this matter.

II. <u>The Outcome of the Division's Claims Against the Other Respondents Will Directly Affect the Division's Burden Related To Its Claims Against Mr. Guzzetti.</u>

As was discussed above, according to Section 15(b)(4)(E), and the holding in *Huff*, a "factual analysis is required in each case," based on "all [of] the circumstances" of the underlying violation. *See*, *Huff*, 1991 SEC LEXIS 551, 5-6, 50 S.E.C. 524 (S.E.C. 1991). Currently, no such factual analysis can occur in this matter. The Division has yet to prove that any actual violation took place that Mr. Guzzetti should have prevented. Only if the Division is successful proving its claims against the other Respondents can "all [of] the circumstances" be considered in a factual analysis of the claims against Mr. Guzzetti. After all, if there was no underlying violation, then there was no failure to prevent that non-existent violation.

The Division has made blanket allegations of loosely defined misrepresentation and omissions in relation to hundreds of separate transactions, in 26 separate private placements, spanning several years. In accordance with the statute at issue, and the holding in *Huff*, more specific information is necessary before a factual analysis can even be conducted.

For example, what misrepresentations or omissions were actually made, when were they actually made, specifically by which of the Respondents, to which individual clients, in reference to which offerings, when did Mr. Guzzetti become aware of these specific misrepresentations, how did he become aware of them, what actions did Mr. Guzzetti take or not take in relation to each of these specific misrepresentations or omissions, and the manner in which the compliance program at MS & Co. operated, to name just a few. For these reasons, the Division's claims against Mr. Guzzetti must fail.

III. The "Red Flags" Identified In The OIP Would Not Cause A Reasonable Supervisor To Take Corrective Action.

The OIP vaguely identifies and defines what it calls "red flags." These alleged "red flags" form the basis of the Division's claims against the other Respondents and Mr. Guzzetti. However, for the reasons described below, the "red flags" identified by the Division would not cause a reasonable supervisor to take corrective action or be put on notice of possible violations of applicable laws, rules, and regulations.

A. Any Misrepresentations Contained In The Offering Documents Cannot Be Classified As "Red Flags."

Considering the allegations contained in the OIP, and the actual facts of this matter, any allegation that Mr. Guzzetti is somehow responsible for, or had a duty to prevent, misrepresentations within the PPM is preposterous. The Division incorrectly alleges that Mr. Guzzetti was responsible for supervising the sale of the private placements at issue in this matter. However, the Division does not, and cannot, allege that Mr. Guzzetti was the supervisor of the compliance, or investment banking department. These are the areas of the firm, along with the legal department, that were responsible for determining the accuracy of the disclosures made within offering documents.

Furthermore, there is no rule or regulation requiring a sales supervisor to independently verify the accuracy of a PPM. That responsibility belongs to the MS & Co. employee responsible for conducting the due diligence review of private placement offerings. In short, even if Mr. Guzzetti was responsible for supervising the sale of the private placements at issue, which he was not, that would not make him responsible for any misrepresentations or omissions contained within the offering documents.

B. <u>The "Redemption Policy" Was Seen As A Natural Reaction To External Market Forces.</u>

Leading up to, and during, one of the greatest financial collapses in history, MS & Co. began experiencing liquidity issues in some of the offerings, and began to limit redemptions. This was not rare or uncommon in the financial services industry during this time period. Although the Division refers to this as a "redemption policy" and attempts to classify it as a "red flag," and a violation of the offering documents, the Division completely ignores the fact that the private placement memoranda (PPM) disclosed this exact possibility.

As an example, the First Excelsior Income Notes, LLC (FEIN) private placement memorandum, dated January 6, 2004, discloses that as a result of adverse economic conditions, the fund "may not be able to generate sufficient cash flow from operations to satisfy all of [its] obligations." See, Relevant Portion of First Excelsior Income Notes, LLC Private Placement

Memorandum, at 13, attached as Exhibit B. In addition, the PPM also clearly states that "a prolonged downturn in the economy could have a material adverse impact" on the funds ability to "perform [its] obligations under the note." Id., at 14.

The allegations based on the so called "redemption policy" are all related to what the Division refers to as the "Four Funds." In addition to the offering described above, included in the Division's definition of the "Four Funds" are the First Independent Income Notes, LLC (FIIN); Third Albany Income Notes, LLC (TAIN); and First Advisory Income Notes, LLC (FAIN). The PPMs for each of these offerings contain the same disclosures as those discussed above.

With hindsight, it certainly appears today that the actions of David Smith and Tim McGinn caused these liquidity issues. However, their criminal acts were carefully hidden from everyone, and the Division does not allege that the Respondents were aware of those actions. During these events, there were significant changes occurring in the financial markets that would have colored the perception of anyone operating in the financial services industry. It was completely reasonable at the time for someone in Mr. Guzzetti's position to believe that limiting, or even eliminating, redemptions from the Four Funds was a normal reaction to the negative forces that were present in the markets, and was a possibility that had been disclosed to these investors. Redemption issues were not isolated to MS & Co. alone at this time, and any limits that were placed on redemptions were not "red flags," despite the position of the Division. After all, nearly 5 years removed from the bottom of the market, there are still areas of the economy that have yet to fully recover.

C. <u>The Experience of David Smith Was Not A "Red Flag."</u>

Another alleged "red flag" discussed by the Division in the OIP is the experience of David Smith. Specifically, the division alleges that the brokers and Mr. Guzzetti should have conducted a deeper investigation into the Four Funds because, according to the Division, David Smith did not have experience running funds as large, or with as much investment freedom.

There are two major problems with the Division's position. First, and most importantly for Mr. Guzzetti, he did not become a supervisor in any capacity until October of 2008, and was never responsible for supervision related to the private placements at issue. According to the list of transactions provided by the Division's Second Disclosure in Response to Respondents' Request for more information, there was not a single transaction made by any of the Respondents in the Four Funds after October of 2008. Mr. Guzzetti was not a sales supervisor of any brokers prior to that time, and as noted below, any evidence regarding transactions prior to September 2008 are barred by the statute of limitations.

Therefore, assuming *arguendo* that Mr. Guzzetti was the sales supervisor for the private placements at issue, as erroneously claimed by the Division, no sales of the Four Funds occurred after the date at which he became a supervisor. Therefore, even if the experience of David Smith was a "red flag," Mr. Guzzetti was not a supervisor in any capacity during the time period that the other Respondents sold the Four Funds.

Second, as noted in the filings of the other Respondents, Mr. Smith had managed numerous successful investments spanning many years. A larger fund was seemingly a natural progression for someone in his position. In view of the track record of MS & Co. offerings, there was no reason to expect that Mr. Smith would not be able to successfully manage the fund. For these two reasons, the investing experience of Mr. Smith is not a "red flag" at all.

D. <u>The Bankruptcy of Firstline Was An Isolated Occurrence, Not A "Red Flag."</u>

The Division also claims that the bankruptcy of one of the trusts was a "red-flag" that should have led Mr. Guzzetti to not allow the further sale of MS & Co. offerings by the other Respondents. However, according to the depositions of Respondents, and Tim McGinn, the Firstline bankruptcy was hidden from a majority of employees at MS & Co., including Mr. Guzzetti and the other Respondents for quite some time.

The firm had been successfully offering similar investments to their clients for decades. The failure of one fund is not cause to immediately assume that all of the other offerings were somehow less than what they appeared to be. There was no reason to assume that the failure of one offering meant that the other offerings were fatally flawed. This is especially true when the economy was in the midst of what can be considered to be the equivalent of a 100 year flood. This was not a "red flag" as the Division claims in the OIP.

IV. <u>Deal Availability Emails.</u>

While employed at MS & Co., Mr. Guzzetti's responsibilities were akin to that of a sales manager, not a sales supervisor. One of the duties or obligations belonging to Mr. Guzzetti was to insure that the brokers were aware of those offerings that had room for additional investments. Mr. Guzzetti would receive this information from another employee at the firm and provide it to the MS & Co. brokers in the form of deal availability emails.

The Division makes much of one particular email that was sent by Mr. Guzzetti in February 2006. In that email, Mr. Guzzetti stated that "there are many investors sitting in money market accounts (fear of higher interest rates) who are losing return (cost of waiting). Our FAIN's offer a way of locking in higher returns with $ sitting in money markets waiting for the 'top' in interest rates."

At the time this email was sent, it is important to remember that the Four Funds were performing well. There were no limitations on redemptions at this time and there was no reason to believe that the funds would not continue to perform well in the future. Many, if not all, of the alleged "red flags" discussed in the OIP had not even occurred at this point.

Furthermore, as testified by others in their sworn testimony, Mr. Guzzetti is not suggesting that the brokers ignore the concepts of suitability and knowing your customer. This was not a diabolical effort to have MS & Co. brokers blindly move clients from money market accounts into an investment in FAIN. Mr. Guzzetti is not comparing the risk of a money market account to an investment in the FAIN offering or instructing the brokers on how to sell the offering.

The purpose of this particular email, as was the purpose with the countless deal availability emails sent by Mr. Guzzetti during his time with the firm, was to educate the brokers as to what investments were available. He is simply attempting to motivate the brokers at MS & Co. to take a look at the FAIN offering and see if it is suitable and appropriate for any of their clients who may have money in a money market account. There is nothing nefarious about this email, or any of the deal availability emails Mr. Guzzetti sent to the other Respondents.

V. **Statute of Limitations.**

According to 28 U.S.C. § 2462, "a proceeding for the enforcement of any civil fine, penalty or forfeiture . . . shall not be entertained unless commenced within five years from the date when the claim first accrued. The OIP in this matter was filed on September 23, 2013. Therefore, all claims made by the Division that accrued prior to September 23, 2008 "shall not be entertained."

According to a recent Supreme Court decision, a claim accrues under § 2462 "when the plaintiff has a complete and present cause of action." *Gabelli v. SEC*, 133 S. Ct. 1216, 1220-1221 (2013). The only reasonable interpretation is that if a claim allegedly accrues on multiple occasions, it accrues for purposes of § 2462 at the moment the first cause of action is "complete" or "comes into existence." Even multiple instances of the same violation would have to be viewed as accruing at the moment the first claim "comes into existence."

Reviewing the allegations of the OIP, it is replete with instances of allegations concerning incidents that occurred before the cutoff date of September 23, 2008. *See*, OIP, at ¶¶ 15, 22, 38 (fn. 3), 43-45, 46, 51, 63, and 64. In fact, there is not a specific date contained in the OIP, beyond the offering dates of a few of the investments at issue, which occurred after September 23, 2008. Rather amazingly, some of the dates referenced in the OIP stretch as far back as the year 2000. *See*, OIP, at 38, fn. 3.

As opposed to private plaintiffs, the SEC is not provided with the benefit of the discovery rule where enforcement actions are concerned. *See, Gabelli*, 1222; (The SEC, for example, is not like an individual victim who relies on apparent injury to learn of a wrong. Rather, a central 'mission' of the Commission is to 'investigat]e] potential violations of the federal securities laws.'").

In addition, the Division of Enforcement may not recover any civil fine, penalty, or forfeiture related to such alleged violations. *See. SEC v. Jones,* 476 F. Supp. 2d 374, 381 (S.D.N.Y 2007) (civil monetary penalties are "unquestionably a penalty" under § 2462); *See also, Riordan* v. *SEC,* 627 F.3d 1230 (D.C. Cir. 2010) (disgorgement is a forfeiture covered by § *2462); SEC v. Bartek,* 484 F. App'x 949, 957 (5th Cir. 2012) (permanent injunction is a penalty under § 2462).

Throughout this matter, the Division of enforcement has relied on *SEC v. Quinlan* as support for its position that its request for a permanent injunction against Mr. Guzzetti is not considered a "penalty" under 28 U.S.C. § 2462. See, Division's Opposition to Respondents' Motion for a More Definite Statement, p. 11, fn. 5, citing *SEC v. Quinlan*, No. 08-2619, 373 Fed. Appx. 581, 587 (6th Cir. 2010). However, there is case law supporting the argument that a permanent injunction may be considered a penalty under 28 U.S.C. § 2462. *See*, *Bartek,* at 957 (permanent injunction may be considered a penalty under 28 U.S.C. § 2462 and be limited by the applicable statute of limitations.)

In *Bartek*, the Court upheld a lower Court's analysis of "the extent of collateral consequences that would result from the O/D bars and injunctions, how this relief would remedy the alleged damages caused . . . and whether the remedy focused on future harm." *Bartek*, at 957. As it is unclear of the nature of the injunction sought by the Division, i.e., length of time and other parameters, it is difficult to conduct the above analysis.

However, it is clear that an injunction will have dire consequences for Mr. Guzzetti. Mr. Guzzetti, who has been personally and professionally damaged as a result of the criminal actions of David Smith and Tim McGinn, will be unable to earn a living in an industry he has operated in, without incident, for decades. Furthermore, the remedies sought will provide no remedy for the alleged damages caused in this matter; the true perpetrators of this fraud have already been arrested, tried, and convicted. Finally, although the Division claims that an injunction is being sought to prevent future harm, there is no allegation that Mr. Guzzetti took part in the fraud of Smith and/or McGinn.

As a result, it is clear that the relief requested by the Division is a penalty under § 2462 and the 5 year time limitation is applicable to the matter at hand. As a result, all claims that accrued prior to September 23, 2008 must be denied in their entirety.

CONCLUSION

For the reasons stated herein, all claims against Mr. Guzzetti contained in the OIP should be denied in their entirety, and Mr. Guzzetti should be awarded all further relief that is deemed just and proper.

Dated: January 17, 2014
Verona, NJ

Respectfully submitted,

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EXHIBIT A

McGinn, Smith & Co., Inc.

Supervisory Compliance Manual

David L. Smith
Chief Compliance Officer

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PRIVATE PLACEMENTS/LIMITED PARTNERSHIPS

There are certain rules which must be followed in making offers or sales of these products to be sure that the offering qualifies for exemption from SEC registration requirements.

1. The RR must qualify his customer in advance to be sure that the customer is either an accredited investor or otherwise a suitable person.
2. Customers may only be sent material cleared for public distribution. Guidelines:
   a. Mail or provide such material only to existing customers or lawyers, accountants or investment advisors, but not to their clients.
   b. Hold generic informational meetings on the general subject of limited partnerships and tax advantage investments.
3. RRs may not engage in general solicitations. This means that limited partnerships are not a prospecting tool. Advise RRs of the following:
   a. No cold calling.
   b. No advertisement, article, notice or other communication can be published in any newspaper, magazine, newsletter or similar media or broadcast on TV, radio or cable.
   c. No seminars or meetings may be held with regard to any current offering unless each invitee is known and qualified in advance.
   d. No mention of any specific offering or past performance may be made at generic seminars (i.e. seminars to discuss the general concept of such investments).
4. No split fees with non-registered people such as lawyers, accountants or investment advisors.

Due Diligence Procedures

When McGinn, Smith acts as underwriter in connection with limited partnership and/or private placement offerings, it will make a reasonable investigation of the project to include inspection of completed projects, conversations with in-house counsel where applicable, a complete examination of financial documents and any other documents deemed necessary to deal fairly with the investing public. Paperwork recording the due diligence will be kept in the legal files.

Subscription Procedures

Subscription documents and checks are collected for each investor. All documents must be signed before they can be received by the firm. Each subscriber must be reviewed and accepted by a principal of the firm, with acceptance indicated by a principal signature on each Subscription Agreement. Subscription Agreements are to be printed with the acceptance language in place for such signature. Information for each offering investor is to be recorded and kept on computer and/or hard-copy files.

All checks are to be made payable to a Bank or Federal Depository as Escrow Agent and deposited into the escrow account, completing the transaction. If a check is received payable to McGinn, Smith & Co., it must be promptly returned to the client with a letter stating that checks must be made payable to the Escrow Agent.

To be in compliance with SEC Rule 15c 2-4, any offering that fails to close and there are funds to be returned from the bank escrow agent to customers, those funds will be paid directly by the escrow agent and not first returned to McGinn, Smith.

Patty Sicluna will supervise the collection of subscription documents and will ensure that they are complete and that all requested information is recorded. She will also oversee that any customer funds will be returned promptly to the customer, if necessary. Ms. Sicluna will also confirm that all orders for private placements, all subscription agreements and all monies collected for private placements be executed and/or received no later than the last date of the specified offering period for the private placement.

Bank Accounts

Monthly reconciliation must be made on all accounts from the bank statements, and a running list of disbursement activity must be kept for year-end accounting purposes. It is the duty of the Assistant Controller to oversee these and report discrepancies to David Rees, the CFO. Escrow statements are mailed from the bank quarterly to the Controller for reconciliation.

Payments

Payment on private placement securities issued through McGinn, Smith follow this pattern:

- funds are accumulated through the issuing entity over a period of time;
- verification of necessary funds prior to issuance of investor checks;
- changes in investor registration or address are performed as needed;
- all accounts are reconciled monthly with David Rees, Controller as supervisor.

Secondary Trades

As mandatory by May 15, 1996, McGinn, Smith & Co. began using standardized forms issued by the NASD to transfer interests in limited partnership securities pursuant to amendments of Sections 1(a)(v) and 73 of the NASD Uniform Practice Code approved by the SEC in January, 1996.

> Sec. 1(a) All over-the-counter secondary market transactions in securities between members shall be subject to the provisions of this Code except: (i) through (iv) No change.
>
> (v) transactions in Direct Participation Program securities as defined in Article III, Section 24 of the Association's Conduct Rules, except as otherwise provided in this Code.
>
> Sec. 73. Each member who participates in the transfer of limited partnership securities, as defined in Article III, Section 34 of the Association's Conduct Rules, shall use standard transfer forms in the same form as set forth in Exhibit A of this Section. This section shall not apply to limited partnership securities which are traded on the Nasdaq Stock Market or a registered national securities exchange.

The forms include Transferor's (Seller's) and the Transferee's (Buyer's) Application for Transfer, Registration Confirmation Form, and Distribution Allocation Agreement. When the completed forms are returned to the firm from the client, they are forwarded to the general partner of the partnership. This is a contract between buyer and seller regarding unpaid distributions. It also prevents Broker/dealers from settling trades without knowledge of the respective rights to distributions.

ORGANIZATIONAL CHART

MCGINN, SMITH & CO., INC.

David L. Smith – 50%
Timothy M. McGinn – 30%
Thomas E. Livingston – 20%

David L. Smith – President & CEO, Director
Timothy M. McGinn – Chairman of the Board, Director
David Rees – Controller
Thomas E. Livingston – Executive Vice President
Andrew Guzzetti – Managing Director, Private Client Group
Frank Chiappone – V.P. / Sales Manager
Timothy M. McGinn – Investment Banking
Stephen Smith – Compliance
David McQuade – Operations Manager
Patricia Sicluna – Office Manager
Joe Gomes – Research Analyst

All Non-NYC brokers are under David L. Smith's direct supervision.

All brokers in the NYC office are under Brian Mayer's direct supervision.

All brokers in the Clifton Park office are under Carl Nicolosi's direct supervision.

Brian Mayer and Carl Nicolosi are under David L. Smith's supervision.

EXHIBIT B

CONFIDENTIAL PRIVATE PLACEMENT MEMORANDUM

FIRST EXCELSIOR INCOME NOTES LLC

$1,000,000 Minimum Offering
$20,000,000 Maximum Offering

5.0% Secured Senior Notes due 2005
7.5% Secured Senior Subordinated Notes due 2007
10.25% Secured Junior Notes due 2009

We are offering up to $20 million aggregate principal amount of our 5.0% secured senior notes due 2005 (the "original senior notes"), 7.5% secured senior subordinated notes due 2007 (the "original senior subordinated notes") and 10.25% secured junior notes due 2009 (the "junior notes" and together with the senior notes (as defined below) and the senior subordinated notes (as defined below), the "notes"). Upon the maturity of the original senior notes, we may continue to issue additional senior notes (the "additional senior notes" and together with the original senior notes, the "senior notes") with a one-year maturity date and an interest rate of the then current prime rate +1% up to one year prior to the maturity date of the original senior subordinated notes, provided that the aggregate principal amount of the outstanding notes at any one time does not exceed $20 million. The original senior notes will mature on January 30, 2005 and any additional senior notes will mature on January 30, 2006 or 2007, respectively. Similarly, upon the maturity of the original senior subordinated notes, we may continue to issue additional senior subordinated notes (the "additional senior subordinated notes" and together with the original senior subordinated notes, the "senior subordinated notes") with a two-year maturity date and an interest rate of 7.5%, provided that the aggregate principal amount of the outstanding notes at any one time does not exceed $20 million. The original senior subordinated notes will mature on January 30, 2007 and any additional senior subordinated notes will mature on January 30, 2009. The junior notes will mature on January 30, 2009. We will pay interest on the notes quarterly on the 30th day of April, July, October and January, commencing on April 30, 2004. The notes are secured by all of the various public and/or private investments that we may acquire, which may include, without limitation, debt securities, collateralized debt obligations, bonds, equity securities, trust preferreds, collateralized stock, convertible stock, bridge loans, leases, mortgages, equipment leases, securitized cash flow instruments, and any other investments that may add value to our asset portfolio (individually an "Investment" and collectively, the "Investments"), and any cash proceeds from the offering that are not used to acquire an Investment, after deducting commissions, fees and expenses. The senior subordinated notes and the junior notes are subordinated in right of payment to the senior notes. Additionally, the junior note holders' right to payment is subordinated in right of payment to the senior subordinated note holders. At our option, we may redeem a pro rata portion of the notes upon the removal, whether voluntary or involuntary, of an Investment from our portfolio.

The notes will be sold through McGinn, Smith & Co., Inc., which is acting as our placement agent for the notes. No public market exists with respect to the notes.

The notes are not certificates of deposit or similar obligations of, and are not guaranteed or insured by, any depository institution, the Federal Deposit Insurance Corporation or any other governmental or private fund or entity. Investing in the notes involves a high degree of risk. See "Risk Factors", beginning on page 5, for a discussion of risks that you should consider before making a decision to invest in the notes.

THE NOTES HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE "SECURITIES ACT"), OR ANY APPLICABLE STATE OR FOREIGN SECURITIES LAWS, NOR HAS THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE OR FOREIGN SECURITIES COMMISSION OR OTHER REGULATORY AUTHORITY PASSED UPON THE ACCURACY OR ADEQUACY OF THIS DOCUMENT OR ENDORSED THE MERITS OF THIS OFFERING. ANY REPRESENTATION TO THE CONTRARY IS UNLAWFUL. THE NOTES ARE OFFERED BY VIRTUE OF EXEMPTIONS PROVIDED BY SECTION 4(2) OF THE SECURITIES ACT, REGULATION D PROMULGATED UNDER THE SECURITIES ACT, CERTAIN STATE AND FOREIGN SECURITIES LAWS AND CERTAIN RULES AND REGULATIONS PROMULGATED PURSUANT THERETO. THE NOTES MAY NOT BE RESOLD OR OTHERWISE TRANSFERRED UNLESS WE RECEIVE AN OPINION OF COUNSEL OR OTHER DOCUMENTATION ACCEPTABLE TO US AND OUR COUNSEL THAT SUCH REGISTRATION IS NOT REQUIRED, OR THERE IS AN EFFECTIVE REGISTRATION STATEMENT UNDER THE SECURITIES ACT AND ANY APPLICABLE STATE AND FOREIGN SECURITIES LAWS.

	Per note	Total
Offering price	100%	100%
Placement agent commissions	2%	2%
Proceeds to First Excelsior Income Notes LLC, before expenses	98%	98%

McGinn, Smith & Co., Inc. has agreed, as our placement agent, to offer the notes on a "best efforts, all or none" basis with respect to the minimum offering of $1,000,000, and on a "best efforts" basis thereafter until the earlier of the termination of the offering or the completion of the maximum offering.

We will issue the notes in certificated form. We expect that delivery of the notes will be made in Albany, New York on or about February 23, 2004. McGinn, Smith Capital Holdings Corp. will act as trustee for the notes. See "Affiliated Transactions."

McGINN, SMITH & CO., INC.

The date of this Private Placement Memorandum is January 16, 2004.

PENGAD 800-631-6989 PLAINTIFF'S EXHIBIT Ent 6 5-10-2011

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Risk Factors Relating to FEIN

FEIN Is A Newly-Formed Limited Liability Company. *We have no historical financial information or results of operations on which you can base your investment decision.*

FEIN was organized in New York in 2004. We have no historical financial statements or results of operations. As a result, you have no historical data on which to base your estimation of our likelihood success in achieving our business and financial goals.

We May Be Unable To Finance Our Operations. *If we are unable to generate a sufficient cash flow, our results of operations and financial condition would be materially and adversely affected and we may be unable to make payments on the notes.*

We require a substantial amount of cash liquidity to operate our business. Among other things, we use such cash liquidity to:

- pay incentive commissions to our managing member's salesmen at the rate of 2% of the aggregate principal amount of the notes per year over the term of the notes;
- pay our managing member a portfolio management fee of 1% of the aggregate principal amount of the notes per year over the term of the notes;
- pay our servicing agent a fee for administering the notes of 0.25% of the aggregate principal amount of the notes per year over the term of the notes;
- satisfy working capital requirements and pay operating expenses, including accounting and legal expenses that we estimate to equal 0.25% of the aggregate principal amount of the notes per year; and
- pay interest expense.

Our cash flow is wholly dependent on our ability to find and acquire suitable Investments. We cannot assure you that our business strategy will succeed or that we will achieve our anticipated financial results. We may not be able to find such opportunities and our ability to generate cash flow depends on market and other factors beyond our control. These factors include:

- the current economic and competitive conditions; and
- any delays in implementing any strategic projects we may have.

Depending upon the outcome of one or more of these factors, we may not be able to generate sufficient cash flow from operations to satisfy all of our obligations, including the notes. If we are unable to pay our debts, we will be required to pursue one or more alternative strategies, such as selling assets, or refinancing or restructuring our indebtedness. These alternative strategies may not be feasible at the time or prove adequate.

We Are Subject To Rate Fluctuations. *Rate fluctuations between instruments may materially and adversely affect our results of operations, financial condition and cash flows and our ability to make payments on the notes.*

Our profitability is largely determined by the difference, or "spread," between the effective rate we pay on the Investments we acquire and the full rate received on such Investments. We may not be able to receive the same rate of return on all of our Investments. If one of our Investments is redeemed, prepaid, liquidated or sold prior to maturity, we may not be able to find a comparable Investment to replace it that would generate the same yields.

We Will Be Adversely Affected When Investments Are Prepaid Or Defaulted. *If an Investment is prepaid or experiences a default, our results of operations, financial condition and cash flows and our ability to make payments on the notes could be materially and adversely affected.*

Our results of operations, financial condition, cash flows and liquidity, and consequently our ability to make payments on the notes, depend, to a material extent, on the performance of the Investments that we purchase. A portion of the Investments that we acquire may default or prepay. We bear the risk of losses resulting from payment defaults and may not realize the full value of our investment. Our income can also be adversely affected by prepayment of an Investment in our portfolio. Our revenue is based on a percentage of the outstanding principal balance of an Investment in our portfolio. If an Investment is prepaid or charged-off, then our revenue will decline while our servicing costs may not decline proportionately.

We Depend On Our Managing Member And On Key Personnel. *The success of our operations depends on our managing member and on certain key personnel.*

Our future operating results depend in significant part upon the continued service of our managing member, to which we pay 1% of the aggregate principal amount of the notes per year over the term of the notes to act as our portfolio manager and give us investment advice. We rely solely on the expertise of our managing member to make the proper investment decisions to generate cash flow.

Our future operating results also depend in part upon our ability to attract and retain qualified management, technical, and sales and support personnel for our operations. Competition for such personnel is intense. We cannot assure you that we will be successful in attracting or retaining such personnel. The loss of any key employee, the failure of any key employee to perform in his or her current position or our inability to attract and retain skilled employees, as needed, could materially and adversely affect our results of operations, financial condition and cash flows.

Our Industry Is Competitive. *Increased competition could materially and adversely affect our operations and profitability.*

We may have to compete with other investors. These competitors may have greater financial resources than we do or have better relationships or offer other forms of financing or services not provided by us. Our ability to compete successfully depends largely upon establishing and maintaining relationships in the investment community and acquiring suitable Investments.

We May Be Harmed By Adverse Economic Conditions. *Adverse economic conditions could materially and adversely effect our revenues and cash flows.*

A prolonged downturn in the economy could have a material adverse impact upon us, our results of operations and our ability to implement our business strategy. Similarly, adverse economic conditions or other factors might adversely affect the performance of our Investments, including the level of delinquencies, which could materially and adversely affect our results of operation, financial condition and cash flows and our ability to perform our obligations under the notes. These economic conditions could result in severe reductions in our revenues or the cash flows available to us and adversely affect our ability to make payments on the notes.

We Are Subject To Regulations. *Failure to materially comply with all laws and regulations applicable to us could materially and adversely affect our ability to operate our business and our ability to make payments on the notes.*

We believe that we are in compliance in all material respects with all such laws and regulations, and that such laws and regulations have had no material adverse effect on our ability to operate our business. However, we will be materially and adversely affected if we fail to comply with:

- applicable laws and regulations;
- changes in existing laws or regulations;
- changes in the interpretation of existing laws or regulations; or
- any additional laws or regulations that may be enacted in the future.