



# Department of Justice

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Northern District of New York

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## **FOUNDERS OF MCGINN, SMITH & CO., INC. INDICTED ON FRAUD AND TAX CHARGES**

*Defendants Timothy M. McGinn and David L. Smith Alleged to Have Engaged in Mail, Wire and Securities Fraud, and to Have Filed False Income Tax Returns*

Albany, New York —United States Attorney Richard S. Hartunian, Victor W. Lessoff, Acting Special Agent-in-Charge, Internal Revenue Service, Criminal Investigation, New York Field Office, and Clifford C. Holly, Special Agent-in-Charge, Federal Bureau of Investigation, Albany Division announced that a grand jury sitting in the Northern District of New York returned an indictment today charging TIMOTHY M. MCGINN, age 63, of Clifton Park, New York, and DAVID L. SMITH, age 66, of Saratoga Springs, New York, with (1) one count of conspiracy to commit mail and wire fraud, in violation of Title 18, United States Code, Section 1349; (2) seventeen counts of mail and wire fraud, in violation of Title 18, United States Code, Sections 1341 & 1343; (3) six counts of securities fraud, in violation of Title 15, United States Code, Sections 78j(b) & 78ff and Title 18, United States Code, Section 2; and (4) three counts each of filing a false income tax return, in violation of Title 26, United States Code, Section 7206(1).

Count 1 charges the defendants with conspiracy to commit mail and wire fraud. The indictment alleges that the purpose of the conspiracy was to mislead investors regarding the safekeeping and use of investor money raised by 17 trusts and one corporation, the risks of the trust offerings, the performance of the underlying income streams, the source of investor payments, and the improper diversion of investor money in order to obtain money from investors and enrich themselves. As a result of the defendant's conduct, the investors were not aware that the defendants

had diverted approximately \$4.1 million in connection with transactions related to the trusts for their own benefit and the benefit of another person. If the defendants are convicted of Count 1, the maximum potential penalties they face include imprisonment for 30 years, to be followed by supervised release for 5 years, and a fine of the greater of \$1,000,000 or twice the gross pecuniary gain or loss.

Counts 2 through 18 charge the defendants with mail and wire fraud. The maximum potential penalty for each of Counts 2 through 18 is imprisonment for 30 years, supervised release for 5 years, and a fine of the greater of \$1,000,000 or twice the gross pecuniary gain or loss. Counts 2 through 6 and 8 through 11 relate to the Firstline Series B Trusts, which raised money from investors in connection with a loan of \$2.4 million to Firstline Security, Inc., a company that generated alarm contracts. The Indictment alleges that the defendants knew that Firstline was facing litigation with its dealer, but did not disclose that to investors, or tell them when Firstline filed for bankruptcy and defaulted on loans. Instead, the defendants directed that investors receive \$2 million of lulling payments by transferring money from other entities controlled by McGinn and Smith, and their firm sold approximately \$600,000 of one of the Firstline investments without any disclosure of the bankruptcy or defaults.

Counts 7 and 12 relate to the Integrated Excellence Trusts, for which the defendants raised about \$1.2 million from investors in connection with a loan to benefit Integrated Excellence, Inc., which generated alarm contracts. The Indictment alleges that the defendant knew that the payments received from the loan were not sufficient to pay investors, but they directed that investors receive lulling payments by transferring money from other entities controlled by McGinn and Smith.

Counts 13 through 16 and 18 are wire fraud charges related to the misuse of investor money held in escrow accounts. Counts 13 and 14 involve the diversion of approximately \$142,000 of investor money from an escrow account to make payments to investors in other trusts. Counts 15, 16, and 18 involve approximately \$115,000 that McGinn and Smith took directly from escrow accounts holding investor funds. These transactions violated their duties as officers and owners of the company acting as the trustee for the Trusts, and they failed to disclose these transactions to investors.

Count 17 is a wire fraud charge related to approximately \$230,000 McGinn took from McGinn Smith Transaction Funding Corp. between August 22, 2008 and July 8, 2009. McGinn repaid \$100,000 of the money. When Smith discovered that McGinn had taken this money, he directed that a false accounting entry be made to conceal it.

Counts 19 through 24 relate to the failure to disclose improperly diverted fees to investors in violation of federal securities laws. Counts 19 and 20 relate to \$100,000 in fees paid in connection with TDM Verifier Trust 08, and counts 21 through 24 relate to approximately \$855,000 in fees paid in connection with Fortress Trust 08. All of these transaction fees were paid with investor money. The maximum potential penalty for each of Counts 19 through 24 is imprisonment for 20 years, supervised release for 3 years, and a fine of \$5,000,000.

Counts 25 through 30 are tax charges arising from the failure of McGinn and Smith to declare the improperly diverted money on their personal tax returns for 2006 through 2008. McGinn and Smith later described the money as "loans," but did not list them as such on personal financial statements. When the Financial Industry Regulatory Authority, Inc. ("FINRA") discovered the false loan accounting entries for the diverted money, the defendants misled FINRA by directing the

creation of backdated promissory notes. The maximum potential penalty for each of Counts 25 through 30 is imprisonment for 3 years, supervised release for 1 year, and a fine of \$100,000.

The Indictment includes allegations for forfeiture of \$8 million in proceeds of the offenses charged.

McGINN and SMITH are expected to be arraigned tomorrow, January 27, 2012, at 2:00 p.m. before the Honorable Randolph F. Treece, United States Magistrate Judge at the Federal Courthouse in Albany. The investigation is ongoing.

This case is being investigated by the Internal Revenue Service, Criminal Investigation and the Federal Bureau of Investigation. This case is being prosecuted by Assistant United States Attorneys Elizabeth C. Coombe and Rick Belliss.

The charges are merely accusations and the defendants are presumed innocent until and unless proven guilty.

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