

UNITED STATES DISTRICT COURT  
NORTHERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION,

*Plaintiff,*

v.

10 Civ. 457 (GLS)  
(DRH)

McGINN, SMITH & CO., INC.,  
McGINN, SMITH ADVISORS LLC,  
McGINN, SMITH CAPITAL HOLDINGS CORP.,  
FIRST ADVISORY INCOME NOTES, LLC,  
FIRST EXCELSIOR INCOME NOTES, LLC,  
FIRST INDEPENDENT INCOME NOTES, LLC,  
THIRD ALBANY INCOME NOTES, LLC,  
TIMOTHY M. MCGINN, DAVID L. SMITH,  
LYNN A. SMITH, DAVID M. WOJESKI, Trustee of  
the David L. and Lynn A. Smith Irrevocable  
Trust U/A 8/04/04, GEOFFREY R. SMITH,  
LAUREN T. SMITH, and NANCY MCGINN,

*Defendants, and*

LYNN A. SMITH, and  
NANCY MCGINN,

*Relief Defendants and:*

DAVID M. WOJESKI, Trustee of the  
David L. and Lynn A. Smith Irrevocable  
Trust U/A 0/04/04,

*Intervenor.*

RECEIVER’S RESPONSE TO CIT  
LENDING SERVICES CORPORATION  
MOTION TO INTERVENE AND VACATE STAY  
(74 STATE STREET PROPERTY)

William J. Brown, as Receiver (“Receiver”), by his counsel, Phillips Lytle LLP,  
files this Receiver’s Response to CIT Lending Services Corporation’s Motion (“Motion”) to

Intervene Under Rule 24(a) and For a Lift of the Temporary Restraining Order<sup>1</sup> as to the real property located at 74-76 State Street, Albany, New York (Docket No. 169), and respectfully states as follows:

### **INTRODUCTION**

1. The Receiver was appointed in this action pursuant to a Preliminary Injunction Order dated July 22, 2010 (Docket No. 96).
2. Third Albany Income Notes, LLC (“TAIN”), one of the Receivership entities, has a substantial financial interest in the real property commonly known as 74-76 State Street (“Real Property”) at which a hotel presently operates.
3. In February 2010, CIT Lending Services Corporation (“CIT”) commenced a foreclosure action in New York State Supreme Court, Albany County (Index No. 1608-10) of its mortgage lien on the Real Property. The CIT foreclosure action has apparently been dormant since that time other than for service of process.
4. For the reasons set forth below, the Receiver believes the stay should be lifted subject to certain conditions.

### **TAIN AND FIIN LOANS AND INTERESTS**

5. On June 6, 2005, TAIN entered into a Loan Agreement with State Street Hospitality, LLC (“SSH”), the owner of the Real Property, and 74 State, LLC (“74 State”). Pursuant to the Loan Agreement, TAIN agreed to make two loans to SSH and 74 State, one in the amount of \$1,400,000 (“Loan No. 1”) and one in the amount of \$1,100,000 (“Loan No. 2”). Loan No. 1 is secured by a second mortgage lien encumbering the Real Property (subordinate to the lien of CIT). The Note evidencing Loan No. 1 was replaced on December 31, 2007 with two

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<sup>1</sup> Any Order granting intervention should be expressly limited to the purpose of foreclosing CIT’s lien upon

Promissory Notes, one in the amount of \$1,100,000 and the other in the amount of \$300,000.

The \$1,100,000 Promissory Note provides for quarterly interest payments with principal payable on December 30, 2012. The \$300,000 Promissory Note provides for quarterly interest payments, for "Additional Principal" payments if payment in full is not made by specified dates, and for principal payable on December 30, 2012. Payments with respect to this Promissory Note can be deferred to December 30, 2012 if the Borrower does not have "Sufficient Cash Flow". SSH and 74 State are joint obligors with respect to Loan No. 1 and Loan No. 2. No payments on these loans have been made since the Receiver's appointment, and they have reportedly been in payment default for an extended period of time.

6. As apparently contemplated by the Loan Agreement and by the Operating Agreements of both SSH and 74 State, Loan No. 2 was paid off or, in effect, replaced on November 30, 2005 by an entity known as 74 State Capital, L.P. ("74SC") which then became the Preferred Class A Member of both SSH and 74 State, holding a 40% membership interest in each entity. The Preferred Class A member is entitled to a 6% per annum distribution in priority over other Members as well as a pro rated distribution of available Qualified Empire Zone, Real Property and Wage Tax Credits. 74SC also holds Warrants to purchase a 15% membership interest in both SSH and 74 State for \$10 upon the earlier of the redemption of the Preferred Class A Membership Interest or July 5, 2010.

7. There appears to be approximately 29 limited partners in 74SC. The general partner of 74SC is McGinn, Smith Holdings, LLC.

8. On January 8, 2009, First Independent Income Notes, LLC also made a loan jointly to 74 State and SSH in the principal amount of \$95,000. \$79,080.82 of principal remains outstanding.

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the real property located at 74-76 State Street, Albany, New York.

**CIT'S COMMUNICATIONS  
WITH THE RECEIVER**

9. On October 5, 2010, the Receiver was contacted by attorneys for CIT who expressed CIT's intent to proceed with its dormant foreclosure action and requested that the Receiver agree to lift the stay. The Receiver informed them that a motion to lift the stay was not necessarily required because the Receiver explained he could consent to vacating the stay with court approval. If he did consent, however, the Receiver also explained that he envisioned parameters on that consent such as marketing the hotel in a professional manner rather than allowing CIT to rely solely on the N.Y. Real Property Actions and Proceedings Law to lessen the likelihood that no surplus would be left for any of the Receiver's estates upon foreclosure. CIT's counsel agreed to consider such a request.

10. On October 8, 2010, the Receiver sent an email to CIT's counsel as a settlement proposal. In relevant part, it stated:

In broad concept, as Receiver, I would consent to a lifting of the stay if we could implement a process, preferably with the borrower's cooperation, to list the hotel for sale while there is an orderly judicial foreclosure process. In my mind, at this point, there is a possibility that there is equity for the junior lien and investors. I would also envision that our agreement would contemplate a structure for the disposition of the hotel should that become possible. I am also open to the possibility of a deed in lieu of foreclosure under appropriate circumstances.

A complete copy of the October 8 email is attached as **Exhibit A**.

11. CIT's counsel did not respond specifically to the Receiver's request and never engaged in any further discussion about it except as stated in an exchange of emails on October 27, 2010, a copy of which is attached as **Exhibit B**.

12. During the last three weeks of October, the Receiver had direct conversations with CIT's business representative and George Schultz, the person understood to

be overseeing 74 State Street. A settlement offer made by 74 State Street to CIT was being considered by CIT, and the Receiver was led to believe by CIT on October 29 that if it were approved by CIT's management, the foreclosure would be avoided.

13. The Receiver has since been unable to obtain a report from CIT on whether the offer was acceptable or not. CIT's Motion was filed on November 5, 2010.<sup>2</sup>

### **THE RECEIVER'S POSITION**

14. The Receiver has reviewed financial information and hotel performance reports provided to him by 74 State. The Receiver has also requested but not yet received the appraisals on the Real Property recently prepared for CIT. The Real Property appears to be significantly over encumbered, although that does not preclude a restructuring of the debt to preserve some chance for TAIN and FIIN investors to realize a partial recovery of those loans, although admittedly it would be difficult to do.

15. The Receiver understands it is CIT's intention to seek the appointment in the foreclosure action of a state court receiver ("Hotel Receiver"). If an experienced hotel operator were to be appointed by the state court as a receiver in the foreclosure action, such a person would have the best chance to determine if the "market" supports a better sale prospect than simply permitting a classic New York real property foreclosure action to proceed.

16. The Receiver has offered to accept (subject to Court approval) a "Hope Note" if the owner's compromise offer to CIT could be effected. Failing that, the Receiver believes that the lifting of the stay should be conditioned on the following:

- a. The retention of an experienced hotel operator as a state court receiver who is reasonably satisfactory

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<sup>2</sup> Exhibit E is missing from the CIT foreclosure complaint filed with this Court. That exhibit per paragraph "Eighth" of the Complaint is to list the amounts owed to CIT. The Receiver has been informed by CIT that it asserts it is owed more than \$9 million.

to the Receiver. The Hotel Receiver would operate the hotel and provide reporting and be available to communicate with both CIT and the Receiver.

- b. Within two weeks of his appointment, the Hotel Receiver would list the Real Property for sale through ordinary commercial means in an effort to expose the property to the market and obtain the highest and best price for the Real Property while the Hotel Receiver attempts to improve hotel operating performance during the state court foreclosure action.
- c. CIT's delivery to the Receiver if not previously provided of all of its appraisals for the property.

Dated: November 29, 2010

PHILLIPS LYTTLE LLP

By       /s/ William J. Brown        
William J. Brown (Bar Roll #601330)  
Todd A. Ritschdorff (Bar Roll #512601)  
Counsel for Receiver  
Omni Plaza  
30 South Pearl Street  
Albany, New York 12207  
Telephone No. (518) 472-1224

and

3400 HSBC Center  
Buffalo, New York 14203  
Telephone No.: (716) 847-8400

Doc # 01-2414326.2

# **Exhibit A**

**William J. Brown**

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**From:** William J. Brown  
**Sent:** 2010-10-08 9:37 AM  
**To:** 'schultz@maynardoconnorlaw.com'  
**Cc:** 'hill@maynardoconnorlaw.com'  
**Subject:** FW: 74 State Street

Jim,

Thank you for having Ben forward the documents promptly to me yesterday. I promised to get back to you by the end of the week with a proposal on how to proceed on an agreed basis.

Subject to my reviewing promptly the hotel's operating performance and, for settlement purposes only under Federal Rule of Evidence 408, I am sending this e-mail to you.

In broad concept, as Receiver, I would consent to a lifting of the stay if we could implement a process, preferably with the borrower's cooperation, to list the hotel for sale while there is an orderly judicial foreclosure process. In my mind, at this point, there is a possibility that there is equity for the junior lien and investors. I would also envision that our agreement would contemplate a structure for the disposition of the hotel should that become possible. I am also open to the possibility of a deed in lieu of foreclosure under appropriate circumstances.

I believe we can memorialize this quickly, but a discussion with you and your client about what you have learned in your due diligence about the hotel property would be helpful in helping me reach a final conclusion and possibly concluding a prompt agreement with CIT.

I am in a meeting a good part of today, but can you suggest some times either on Monday or Tuesday when we might have that conversation either in person or by conference call.

Bill

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**From:** William J. Brown  
**Sent:** Thursday, October 07, 2010 10:03 AM  
**To:** 'schultz@maynardoconnorlaw.com'  
**Subject:** 74 State Street

Jim,

Following up our October 5 conversation regarding your client's intention to continue with the foreclosure action it commenced last February and the existence of the stay, as promised I intend to get back to you by the end of this week to likely propose a process by which to go forward which would call for a more typical sales marketing effort during the pendency of the foreclosure with an eye towards producing a market sale for the property.

As part of that, I'd appreciate receiving an electronic copy of CIT's loan and perfection documents.

Bill

William J Brown, Esq.  
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11/29/2010



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# Exhibit B

**William J. Brown**

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**From:** William J. Brown  
**Sent:** 2010-10-27 9:07 AM  
**To:** 'James R. Schultz'  
**Subject:** RE: CIT LSC vs. 74 State, et al/SEC

If you read the entire email to which you refer, I believe it is clear a reply was expected. It was a Rule 408 proposal.

I am leaving for a meeting in NYC right now, but I will be back this afternoon and will call you then.

Bill

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**From:** James R. Schultz [mailto:schultz@maynardoconnorlaw.com]  
**Sent:** Tuesday, October 26, 2010 6:16 PM  
**To:** William J. Brown  
**Subject:** RE: CIT LSC vs. 74 State, et al/SEC

I am unaware of any terms to which you asked a yes or no answer other than to hold a telephone conference call. You outlined a concept in your October 8 e-mail transmission, which I have copied below, but which did not request our reply:

In broad concept, as Receiver, I would consent to a lifting of the stay if we could implement a process, preferably with the borrower's cooperation, to list the hotel for sale while there is an orderly judicial foreclosure process. In my mind, at this point, there is a possibility that there is equity for the junior lien and investors. I would also envision that our agreement would contemplate a structure for the disposition of the hotel should that become possible. I am also open to the possibility of a deed in lieu of foreclosure under appropriate circumstances.

CIT has no objection to your entering into an agreement with the borrower to list the property for sale or doing whatever else you deem necessary during the foreclosure process as long as it doesn't impede CIT's ability to prosecute its action. Since the borrower continues to hold the right to redeem, there is no requirement to obtain CIT's consent.

If you are seeking something else from me or my client, feel free to call me tomorrow morning.

Jim

**James R. Schultz, Esq.**  
**Partner**  
**Maynard, O'Connor, Smith & Catalinotto, LLP**  
**6 Tower Place**  
**Albany, New York 12203**  
**(518) 465-3553**  
**(518) 465-5845 fax**  
[schultz@maynardoconnorlaw.com](mailto:schultz@maynardoconnorlaw.com)

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11/29/2010

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**From:** William J. Brown [mailto:WBrown@phillipslytle.com]  
**Sent:** Tuesday, October 26, 2010 5:44 PM  
**To:** James R. Schultz  
**Subject:** Re: CIT LSC vs. 74 State, et al/SEC

I had asked you to agree to certain terms as a condition to my consent to lifting the stay. I do not believe you have responded yes or no. Please give me your answer or we can discuss further in the morning since I am about to board a plane.

Bill

William J. Brown, Esq.  
Phillips Lytle LLP  
[wbrown@phillipslytle.com](mailto:wbrown@phillipslytle.com)  
Sent from my iPhone

On Oct 26, 2010, at 5:34 PM, "James R. Schultz" <[schultz@maynardoconnorlaw.com](mailto:schultz@maynardoconnorlaw.com)> wrote:

Bill, I had a conversation with Dennis Davis this date, who reported that he has not heard from you since our telephone conversation of Tuesday the 19th. We plan to go forward with our motion to lift the stay, but will not shut the door on any future discussions should you determine that they may be of benefit to everyone concerned.

Thank you.  
Jim Schultz

**James R. Schultz, Esq.**  
**Partner**  
**Maynard, O'Connor, Smith & Catalinotto, LLP**  
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11/29/2010

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SECURITIES AND EXCHANGE COMMISSION,

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the David L. and Lynn A. Smith Irrevocable  
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LAUREN T. SMITH, and NANCY MCGINN,

*Defendants, and*

LYNN A. SMITH, and  
NANCY MCGINN,

*Relief Defendants and:*

DAVID M. WOJESKI, Trustee of the  
David L. and Lynn A. Smith Irrevocable  
Trust U/A 0/04/04,

*Intervenor.*

**CERTIFICATE OF SERVICE**

I, Karen M. Hatch, being at all times over 18 years of age, hereby certify that on November 29, 2010, a true and correct copy of the Receiver's Response to CIT Lending Services Corporation Motion to Intervene and Vacate Stay (74 State Street Property) was caused to be served by e-mail upon all parties who receive electronic notice in this case pursuant to the Court's ECF filing system, and by First Class Mail to the parties indicated below:

Lynn A. Smith  
2 Rolling Brook  
Saratoga Springs, NY 12866

Charles C. Swanekamp  
Jaeckle, Fleischmann Law Firm  
12 Fountain Plaza  
700 Fleet Bank Building  
Buffalo, NY 14202

Dated: November 29, 201

/s/ Karen M. Hatch  
Karen M. Hatch