

UNITED STATES DISTRICT COURT  
NORTHERN DISTRICT OF NEW YORK

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SECURITIES AND EXCHANGE COMMISSION

*Plaintiff,*

vs.

Case No. 1:10-CV-457  
(GLS/CFH)

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, AND  
DAVID L. SMITH, GEOFFREY R. SMITH,  
Individually and as Trustee of the David L. and  
Lynn A. Smith Irrevocable Trust U/A 8/04/04,  
LAUREN T. SMITH, and NANCY MCGINN,

*Defendants,*

LYNN A. SMITH and  
NANCY MCGINN,

*Relief Defendants. and*

GEOFFREY R. SMITH, Trustee of the  
David L. and Lynn A. Smith Irrevocable  
Trust U/A 8/04/04,

*Intervenor.*

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**RECEIVER’S JOINDER TO PLAINTIFF’S BRIEF IN OPPOSITION TO  
DEFENDANT DAVID L. SMITH’S MOTION TO MODIFY THE ASSET  
FREEZE TO ALLOW THE RELEASE OF CERTAIN PROPERTY**

William J. Brown, as Receiver (“Receiver”) of McGinn, Smith & Co. (“MS & Co.”),  
by his counsel, Phillips Lytle LLP, respectfully submits this Joinder to the SEC’s Opposition  
(Docket No. 1049) to Defendant David L. Smith’s Motion to Modify Asset Freeze to Allow

the Release of Certain Property (Docket No. 1039) (“Motion”) by David L. Smith (“Smith”).

### **PRELIMINARY STATEMENT**

The Motion represents an attempt by Smith to avoid surrendering certain of his and Lynn Smith’s retirement accounts to the Receiver for distribution to defrauded investors, notwithstanding that Smith was ordered by this Court to disgorge to the Receiver \$99,101,350 and that L. Smith was ordered to return certain fraudulently transferred assets. Any additional amounts recovered from the Smiths will be distributed to the hundreds of investors who were wronged by Smith’s criminal conduct and who may recover, at most, between approximately 13.5% to 21.7% of their investments, pursuant to the Receiver’s Court-approved Plan of Distribution. Accordingly, the Receiver joins in the arguments of the Securities and Exchange Commission that the asset freeze should not be modified and that the assets in the Smiths’ retirement accounts should be turned over to the Receiver.

### **BACKGROUND**

On April 20, 2010, in connection with a Complaint filed by the Securities and Exchange Commission initiating the above-captioned action (Docket No. 1), this Court granted a Temporary Restraining Order (Docket No. 5), which, among other things, froze certain assets of, among others, Smith and his wife Lynn A. Smith (“L. Smith”), and appointed the Receiver as temporary receiver with respect to numerous entities controlled or owned by Defendants Timothy McGinn (“McGinn”) and Smith, including those listed on Exhibit A to the Preliminary Injunction Order entered in this action (Docket No. 96).

On July 26, 2010, following a hearing, the Court entered an order granting the SEC's Motion for a Preliminary Injunction and appointing the Receiver as receiver, pending a final disposition of the action ("Preliminary Injunction Order") (Docket No. 96).

On August 13, 2013, this Court entered a Judgment ("Criminal Judgment") against Smith in the criminal proceedings initiated against him by the United States Attorney's Office for the Northern District of New York. *See* Judgment, *United States of America v. David Smith*, 1:12-cr-00028-DNH (Aug. 13, 2013). The Criminal Judgment ordered Smith to pay restitution of \$5,748,722 ("Restitution").

On February 17, 2015, the Court issued its Memorandum-Decision and Order (Docket No. 807) ("MDO") granting the SEC's motion for summary judgment.

On June 25, 2015, the Court entered the Final Judgment as to Smith (Docket No. 835) ("D. Smith Judgment"). In the D. Smith Judgment, the Court ordered Smith to disgorge a total amount of \$99,101,350 ("Disgorgement") to the Receiver. D. Smith Judgment at 6.

The D. Smith Judgment provides that "[a]ny assets recovered by or under the control of the Receiver collected from the Defendant Smith pursuant to the prior orders of this Court are deemed to be assets of the Distribution Fund effective upon the entry of this Final Judgment." *Id.* at 9. The D. Smith Judgment also authorizes the Receiver to "liquidate and monetize any assets recovered from or on behalf of or in connection with Defendant Smith." *Id.*

On June 25, 2015, the Court entered the Final Judgment as to Lynn A. Smith, Lauren T. Smith, Geoffrey R. Smith, and Nancy McGinn (Docket No. 837) ("L. Smith Judgment" and collectively with the D. Smith Judgment, the "Final Judgments"). In the L.

Smith Judgment, the Court ordered that L. Smith be jointly and severally liable, together with Smith, for the return of certain fraudulently transferred assets or their equivalent value. *Id.* at 3. The L. Smith Judgment further provides that the Receiver shall apply all proceeds of all payments and transfers to him pursuant to the L. Smith Judgment to the Distribution Fund for investors. *Id.* at 4.

In December 2018, the Receiver was informed that Smith had a \$5,534.85 required minimum distribution (“RMD”) due from the McGinn Smith Incentive Savings Plan (“Plan”).

Accordingly, on December 27, 2018, the Receiver sent to Smith a letter (“Letter”) notifying Smith that the Receiver had been informed that Smith was due a \$5,534.85 required minimum distribution (“RMD”) from the McGinn Smith Incentive Savings Plan (“Plan”). By the Letter, the Receiver explained his intention to authorize a withdrawal of the RMD and cause it to be delivered to the Receiver, in accordance with the D. Smith Judgment. A copy of this Letter is attached to the Motion. The Receiver intended to place the proceeds of the RMD into an account for distribution to investors in accordance with the Plan of Distribution. The Receiver has not yet received the proceeds of the RMD.

On February 19, 2019, Smith filed the Motion, which seeks to modify the asset freeze imposed by the Preliminary Injunction Order with respect to Smith’s interest in the Plan, Smith’s Individual Retirement Account (“D. Smith IRA” and collectively with the Plan, the “Retirement Assets”) and Lynn A. Smith’s Individual Retirement Account (“L. Smith IRA”).

Smith raises several arguments in the Motion in support of the relief requested in the Motion. Smith argues that the amount of the Disgorgement is improper and that the

Retirement Assets and the L. Smith IRA are exempt from the Disgorgement pursuant to New York State law. Smith also argues that the Receiver does not control the Retirement Assets, and therefore may not monetize the Retirement Assets, because the exemption status of the Retirement Assets was not adjudicated before the D. Smith Judgment was entered. Smith also argues that the L. Smith IRA may not be turned over to the Receiver because it was not mentioned in the L. Smith Judgment or derived from “ill-gotten gains.” Finally, Smith argues that since the Restitution has been satisfied, the Retirement Assets are not needed to satisfy the Disgorgement.

On April 12, 2019, the Securities and Exchange Commission (“SEC”) filed its Brief in Opposition to Defendant David L. Smith’s Motion to Modify the Asset Freeze to Allow the Release of Certain Property (Docket No. 1049) (“Opposition”).

### **JOINDER AND OBJECTION**

The Receiver joins in the arguments submitted in the Opposition that (1) the Retirement Assets and the L. Smith IRA should be turned over to the Receiver for distribution to investors, (2) the Retirement Assets are not exempt under New York State law from the Disgorgement ordered by the D. Smith Judgment, (3) the Supreme Court’s holding in *Kokesh v. SEC*, 137 S. Ct. 1635 (2017) is not applicable to the Disgorgement, and (4) the L. Smith IRA, along with Lynn Smith’s non-IRA account, should be turned over to the Receiver in satisfaction of the L. Smith Judgment. Accordingly, the Receiver supports denial of the Motion for the reasons set forth in the Opposition.

In addition, Smith’s argument that the Final Judgments do not permit the Receiver to recover and liquidate the Retirement Assets or the L. Smith IRA is erroneous. For the reasons set forth in the Opposition, the Retirement Assets are not exempt from the

Disgorgement and therefore are not immune to recovery and distribution by the Receiver. Further, although Judge Sharpe did not explicitly include “exempt assets” when he granted the Receiver authority to liquidate and monetize any recovered assets for the Investor Distribution Fund, Smith offers nothing to support his assertion that Judge Sharpe intended to exclude assets if the exempt status of such assets under applicable state law had not been adjudicated prior to the entry of the D. Smith Judgment. Indeed, to insert such a broad limitation into the D. Smith Judgment would render many assets outside of the Receiver’s control, as the application of state law exemptions to many of Smith’s assets had not been litigated before the D. Smith Judgment was entered.

Further, the L. Smith Judgment provides that all proceeds of all payments and transfers to the Receiver pursuant to the L. Smith Judgment, which ordered L. Smith return certain fraudulently transferred assets or their equivalent value, shall be added to the Distribution Fund for distribution to investors. L. Smith remains a judgment debtor pursuant to the L. Smith Judgment for fraudulent transfers made in the aggregate amount of \$600,368, which amount remains unsatisfied. *See* L. Smith Judgment at 2-3.

Smith has already attempted to modify the asset freeze to access a retirement account by a motion filed November 3, 2010 (Docket No. 176). In the Memorandum Decision and Order entered by Judge Homer on December 15, 2010 (Docket No. 221), in which the Court declined to grant the relief requested by Smith, Judge Homer stated that the amount of money in Smith’s 401(k) retirement account “will be important in either facilitating repayment or determining whether he has an ability to pay the amount ordered disgorged.” *Id.* at 5. Thus, Judge Homer held that the freeze of the account “serves to maintain an asset

which may play an integral role in future proceedings” and declined the request to modify the asset freeze. *Id.*

Although Judge Homer’s Memorandum Decision and Order was entered before the D. Smith Judgment, it suggests that the Court was well aware that Smith’s retirement accounts, including the Retirement Assets, would be important in facilitating payment of the Disgorgement. Now that the D. Smith Judgment has been entered, and the Disgorgement remains unsatisfied, any amounts recovered from the Retirement Assets will facilitate repayment of the Disgorgement.

Finally, Smith may not rely on the fact that the Restitution ordered in the Criminal Judgment entered against Smith has been satisfied as a basis to avoid satisfaction of the Disgorgement ordered in the D. Smith Judgment. Smith has argued in the past that criminal restitution renders a civil disgorgement moot. *See* Defendant David L. Smith’s Response to Plaintiff’s Statement of Material Facts and Statement of Additional Facts in Opposition to Plaintiff’s Summary Judgment Motion (Docket No. 785). In response to Smith’s arguments, the Court noted in the MDO, “[r]estitution and disgorgement . . . are distinct.” MDO at 44. The Court went on to state that Smith’s arguments in this regard were “unpersuasive” and that “Smith has not cited, nor has the court found, a single case in which restitution in a criminal case limited or governed the disgorgement amount in a parallel civil case . . . .” *Id.*

Smith, along with McGinn, defrauded hundreds of investors out of millions of dollars. These innocent investors, many of whom were elderly retirees, trusted Smith with their investments and the Receiver estimates that those investors will receive, at most, a recovery ranging from 13.5% to 21.7%, depending upon the outcome of certain claim

objections. *See* Third Written Status Report of the Receiver (Docket No.925). Any and all amounts recovered from Smith's assets, including the Retirement Assets, and from the L. Smith IRA will increase the amounts available for distribution to innocent investors who were wronged by Smith and who stand to recover only a fraction of what they entrusted to Smith.

**CONCLUSION**

The Receiver respectfully requests that the Court deny the Motion as to the Retirement Assets, and grant such other and further relief as the Court may deem just and proper.

Dated: April 12, 2019

PHILLIPS LYTTLE LLP

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