

UNITED STATES DISTRICT COURT  
NORTHERN DISTRICT OF NEW YORK

-----X  
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.*  
-----X

**NOTICE OF SIXTH CLAIMS MOTION OF WILLIAM J. BROWN, AS  
RECEIVER, FOR AN ORDER (A) APPLYING PREFERENTIAL  
PAYMENT OFFSET TO LESLEY LEVY CLAIMS AND (B) EQUITABLY  
SUBORDINATING LESLEY LEVY CLAIMS**

PLEASE TAKE NOTICE that upon the Sixth Claims Motion of William J. Brown, as Receiver, for an Order (A) Applying the Preferential Payment Offset to certain Lesley Levy Claims and (B) Equitably Subordinating Lesley Levy Claims (“Motion”), Phillips Lytle LLP will move before the Hon. Christian F. Hummel, United States Magistrate Judge, United States District Court for the Northern District of New York, James T. Foley - U.S. Courthouse, 445 Broadway, Albany, New York 12207-2924, on June

20, 2019 at 9:30 a.m., seeking an Order to be entered approving the Motion. No oral argument is requested.

PLEASE TAKE FURTHER NOTICE that objections, if any, to the relief requested in the Motion must be made in writing, and should be filed and served upon the undersigned at the address listed below in accordance with the Federal Rules of Civil Procedure and the Local Rules for the United States District Court for the Northern District of New York.

PLEASE TAKE FURTHER NOTICE that if no responses are timely filed and served with respect to the Motion, the Court may enter an Order granting the Motion, applying the Preferential Payment Offset and equitably subordinating the Lesley Levy Claims without further notice or opportunity to be heard offered to any party.

Dated: April 25, 2019

PHILLIPS LYTTLE LLP

By /s/ Catherine N. Eisenhut  
William J. Brown (Bar Roll #601330)  
Catherine N. Eisenhut (Bar Roll #520849)  
Attorneys for Receiver  
Omni Plaza  
30 South Pearl Street  
Albany, New York 12207  
Telephone No. (518) 472-1224

and

One Canalside  
125 Main Street  
Buffalo, New York 14203  
Telephone No.: (716) 847-8400

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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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**SIXTH CLAIMS MOTION OF WILLIAM J. BROWN, AS RECEIVER, FOR  
AN ORDER (A) APPLYING PREFERENTIAL  
PAYMENT OFFSET TO LESLEY LEVY CLAIMS AND (B) EQUITABLY  
SUBORDINATING LESLEY LEVY CLAIMS**

William J. Brown, as Receiver (“Receiver”), by his counsel, Phillips Lytle LLP,  
moves (the “Motion”) for an order (A) applying the Preferential Payment Offset (as defined

in the accompanying Declaration) to claims held by investor Lesley Levy<sup>1</sup> (“Levy”), as set forth on Exhibit A to the Motion and (B) equitably subordinating such claims, and respectfully represents as follows:

The Receiver files the Motion to request entry of an Order (A) applying the Preferential Payment Offset to the claims held by Levy (collectively, the “Levy Claims”) as shown on **Exhibit A** and (B) equitably subordinating such Levy Claims to the Investor B Claim (as defined in the accompanying Declaration), based on the accompanying Memorandum of Law and Declaration of William J. Brown, as Receiver (“Declaration”), each dated April 25, 2019.

**RELIEF REQUESTED**

The Receiver requests that the Court enter an Order substantially in the form attached as **Exhibit C** (“Order”) (A) applying the Preferential Payment Offset to the Levy Claims as shown on Exhibit A to the Motion and (B) equitably subordinating such Levy Claims, together with such other and further relief as the Court deems just and proper.

The Receiver reserves all rights to object on any other basis to the claims of all investors or claimants, including Levy and Investor B.

Doc #01-3663132.1

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<sup>1</sup> Lesley Levy voluntarily disclosed herself to the public as a McGinn Smith investor as evidenced by her letters to the Court filed at Docket Nos. 942 and 946 as well as Albany Times Union articles quoting her on September 19, 2011 and February 7, 2013 (copies of which are attached here as **Exhibit B**). Consequently, her name is not redacted in this Motion.

Dated: April 25, 2019

PHILLIPS LYTTLE LLP

By  /s/ Catherine N. Eisenhut  
William J. Brown (Bar Roll #601330)  
Catherine N. Eisenhut (Bar Roll #520849)  
Attorneys for Receiver  
Omni Plaza  
30 South Pearl Street  
Albany, New York 12207  
Telephone No. (518) 472-1224

and

One Canalside  
125 Main Street  
Buffalo, New York 14203  
Telephone No.: (716) 847-8400

# *Exhibit A*

## Application of Preferential Payment Offset to

## Levy Claims

Claim No.	Description	Claim Amount	Proposed First Distribution (10%)	Adjusted First Distribution
5540	FAIN 10.25% Secured Junior Notes	\$50,000	\$5,000.00	
5541	FAIN 10.25% Secured Junior Notes	\$100,000	\$10,000.00	
5542	FEIN 10.25% Secured Junior Notes	\$100,000	\$10,000.00	
5543	FAIN 10.25% Secured Junior Notes	\$100,000	\$10,000.00	
5544	TAIN Secured Junior Notes	\$60,000	\$6,000.00	
5545	TDM Cable Trust 06	\$100,000	\$10,000.00	
	<b>TOTAL</b>		<b>\$51,000.00</b>	<b>(\$39,000.00)</b>

# ***Exhibit B***



**timesunion** <https://www.timesunion.com/local/article/Investors-left-adrift-in-scam-case-2176656.php>

## Investors left adrift in scam case

**Alleged victims of former Albany brokerage grow desperate as proceedings lag to recover funds**



### IMAGE 1 OF 12

James and Celine Prior, of Greene County, said they lost their life's savings in what the U.S. Securities and Exchange Commission alleges was a massive fraud committed by a longtime Albany brokerage, McGinn ... [more](#)

ALBANY -- **Lesley Levy** was a Wall Street adviser. Through her years of hard work, she said, she hoped to spend her retirement comfortably nestled in her San Diego home.

Now, faced with the loss of up to \$2 million in investments she said she steered to an Albany brokerage, McGinn, Smith & Co., Levy, 61, fears she has lost everything. Levy said she's living off a credit card, shops at Dollar Tree and is unable to afford even routine medical visits. She has taken in boarders to try to cover her mortgage payments.



"You don't know what it's like to have strangers in your house," she said, recounting a tenant who would boil fish in her kitchen late at

night. "It's horrible."

Levy is among an estimated 900 individuals and organizations that placed investments with McGinn, Smith & Co., which was accused of fraud 17 months ago in a complaint filed by the U.S. Securities and Exchange Commission.

For several decades the firm's founders, **Timothy M. McGinn** and **David L. Smith**, were part of a country-club elite, rubbing elbows with the area's wealthiest residents while playing golf in exclusive destinations like Ireland and Palm Beach, Fla. They cultivated clients at the highest levels of society and built their brokerage into a lucrative firm that was once so connected their payroll included former state Senate Majority Leader Joseph L. Bruno.

But according to the SEC's civil complaint, McGinn, Smith and its various entities orchestrated what eventually became a Ponzi-type scheme that left hundreds of people financially devastated. The "house of cards" the SEC has accused the brokerage of building began to collapse three years ago. Even then, the SEC said, the brokerage's leaders began trying to hide their assets while raiding funds and luring money from more alleged victims.

Now, more than a year after the SEC stepped in, and as a federal criminal investigation remains pending, it's unclear whether investors who lost money will ever be repaid.

The SEC estimates the alleged fraud unfolded over at least a six-year period and involved up to \$136 million. The firm's largest investment account, called the Four Funds, has less than \$500,000 in cash despite owing investors at least \$84 million.

### **More Information**

Once-trusted broker's assets frozen

Some investors said they are frustrated by the efforts of federal authorities and have received misleading information regarding their options and chances of getting back their money.

In April 2010, U.S. Securities and Exchange Commission filed a civil complaint alleging massive fraud by Albany brokerage McGinn, Smith & Co.

SEC estimates the fraud has jeopardized more than 900 investors, \$136 million.

Largest account, Four Funds, owes investors \$84 million but has less than \$500,000.

Another 19 unregistered debt offerings have negative equity of \$18 million.

Life during scam case

James and Celine Prior of Greene County said they lost \$400,000 of their life savings to McGinn, Smith & Co. The couple, Irish immigrants and both in their 80s, saved the money to pay medical costs. Celine Prior is suffering from Alzheimer's disease and severe asthma. The couple have been forced to move in with their son and daughter-in-law in New Jersey. "They were intentionally sold investments which they purchased with blind trust from someone they believed to be reputable," said the couple's daughter-in-law, Wendy Prior. "They were not capable of researching them on a computer. They had fancy names that sounded like government securities ... and it was all a big scam."

Monica Check, 66, and her husband Peter, 65, said she has considered returning to work after losing \$100,000 in investments with McGinn, Smith & Co. The couple, who live on Florida's

The **Securities Investor Protection** Corp., established by Congress in 1970 to provide protection for investors who fall victim to bankrupt brokerages or fraud, said it has no role in the case and has not been contacted by the SEC or a federal receiver appointed to help recover money for investors.

**William J. Brown**, the federal receiver appointed in the McGinn, Smith case, said the SEC has had "direct discussions" with the SIPC and he has "not closed the book on that source."

The SIPC, with urging from Congress, was tapped to assist victims of convicted financier **Bernard Madoff**. But not all fraud cases involve high-profile victims or grab the attention of Congress.

"If any investors contacted SIPC, they would also be told that the matter has not been referred to SIPC by the SEC and they need to contact the SEC with questions. Mr. Brown has not been in contact with SIPC," said **Stephen Harbeck**, SIPC's president. "No facts have been presented to SIPC by either the SEC or the receiver with respect to this matter. ... Ordinarily, when, as, and if the SEC believes a SIPC proceeding is appropriate, SIPC is notified promptly."

west coast, are struggling financially while Peter Check battles prostate cancer. Monica Check, who worked in finance department for a pharmaceutical company, said she hoped to play golf in retirement but is now considering a job as a course ranger. "There's no work down here, per se, for anyone 65 years or older. ... We invested in June of 2009 and were supposed to receive this income monthly."

Stanley C. Rosenzweig, 81, said he and his wife, Betty, both of Hernando, Fla., invested more than \$1.1 million of their retirement assets with McGinn, Smith & Co.

"Apparently, the founders, Tim McGinn and David Smith, were using new investor's money to fund old investor's interest payments in a \$136 million Ponzi scheme, while pressuring agents to find new investment money, until caught by a bad economy," Rosenzweig wrote in a letter to a federal judge. "These people are still living a lavish life style, while we have serious financial problems, with an imposed frugal life style and a 12-year-old car that we cannot afford to replace."

Brown said the victims are not ready to hit a panic button.

"We've collected over \$8 million so far. That's been disclosed to certain parties ... and there's more to collect," he said. "I have talked to a significant number of investors recently and, save one instance, I believe they all understand the circumstances very well. I have not encountered any frustration or hostility."

Brown said his efforts have been slowed by inconsistent record-keeping at some 70 entities that entangled with McGinn, Smith's dealings. He added not all investors lost their money and he has to be careful that distributions are made only to those entitled to receive them.

In addition, McGinn and Smith, as well as Smith's wife, Lynn, whose assets are also being targeted by the SEC, have waged a costly and fierce legal battle with the SEC, which is seeking a court ruling allowing it to hunt down all remaining assets and help repay victims, who may only receive pennies on the dollars

lost.

The brokerage, formerly located at 99 Pine St. in Albany, closed five months before the SEC filed its complaint. According to the SEC, many investors were unaware their money was being placed in risky securities or that the firm had skimmed exorbitant fees and used

investors' money to make loans -- unlawfully -- to other troubled accounts and to top company officials.

"I've got nothing and I'll be maxed out in a couple of months," Levy said. "It's not right that these people are going to get away with this. What happens to us? Why is it always the victim that becomes the culprit. It's not right."

The investors were from a wide spectrum. To some, an investment of \$100,000 marked a life's savings. For others, the loss of \$1 million was a bad year.

**Eileen Cornacchia**, 64, said she lost "close to \$1 million" that she and her husband, Joseph, who died in June, had given to McGinn, who was their friend.

Joseph Cornacchia was president of the exclusive **Pine Tree Golf Club** in Boynton Beach, Fla., where McGinn had been a member. (The SEC said McGinn's living expenses, including membership fees at **Pine Tree and Schuyler Meadows Country Club** in Loudonville were paid from company accounts even as the bottom was falling out.)

"It certainly hurt and it was not our life's savings," Cornacchia said. "But on the other hand for my husband, who considered Tim a friend and had always trusted him, it was a severe blow, a severe shock."

Cornacchia said McGinn was always hunting investors. He hosted an annual golf tournament at Pine Tree and would bring about 20 golfers from New York to face off with golfers from Pine Tree.

"As Tim used to say: 'If I'm selling apples and they stop making apples, I'll sell oranges. I can sell anybody anything,'" she recounted. "He used us for our connections and he used us for our connections at Pine Tree. ... He actually tried to hire two of my nephews who wanted no part of it. ... I don't think Tim had any friends who were not also targets. We were marks."

James Prior, 83, a retired CitiCorp worker who lives in Greene County with his wife, Celine, said they invested \$400,000 -- his life's savings -- with McGinn, Smith & Co., after being told

the investments were safe and certain to return monthly dividends. The fallout has caused the couple to move in with their son and daughter-in-law in New Jersey.

**Celine Prior** is suffering from Alzheimer's disease and they cannot afford to stay in their Greenville residence while paying for her treatment, James Prior said.

"In the beginning everything worked out very well then around 2008 everything fell flat," said Prior, an Irish immigrant who used to reside in Queens. "We have a small savings but not much."

The Priors' daughter-in-law, Wendy Prior, said her in-laws were initially contacted by a McGinn broker through a telephone solicitation.

"They set up an appointment where they met at their home in Greenville and over the course of time were advised to purchase various investments promising lucrative returns," Wendy Prior said. "Eventually the truth was uncovered that the investments were extremely high risk, perhaps even fraudulent and were completely inappropriate to be sold to an elderly couple on a fixed income."

The SEC alleges the brokerage also used investors' money for payroll expenses and to pay back other investors.

The SEC has been aided in its case by federal prosecutors, who have given the SEC evidence seized in court-authorized, FBI-assisted searches of the businesses and homes of McGinn and Smith. Smith's wife, Lynn, was recently sanctioned by a federal judge for concealing the couple's interest in a \$4.5 million trust fund the Smiths said was set up exclusively for their two children. An attorney for the trust also was sanctioned for her role.

The long list of alleged victims, including institutional organizations and unsophisticated investors, has not been made public.

In 2008, according to the SEC, Smith wrote letters to investors blaming losses on the collapse of the sub-prime mortgage industry, which the SEC said was misleading and false.

Many of the firm's investments involved deals in which investors were promised high returns on the purchase of alarm company contracts. The investments involved the sale of long-term, alarm-monitoring contracts to customers who paid companies to monitor their residential alarm systems. But if a certain number of those customers defaulted on their contracts, the rate of return would drop, which happened.

Federal prosecutors are weighing whether the manner in which the accounts were sold, managed and eventually defaulted may constitute criminal activity. Another area of focus by a federal grand jury in Albany is whether the undisclosed and exorbitant fees gleaned from investors' accounts amounted to fraud.

Monica and Peter Check, both in their mid-60s, said they worked hard to secure a comfortable retirement in a small community along Florida's west coast. **Monica Check**, 66, who worked in a pharmaceutical company's finance office, invested most of her savings -- \$100,000 -- with McGinn, Smith & Co. in 2009, unaware the firm was privately crumbling.

Monica Check said her husband is battling serious health problems, including prostate cancer and the loss of a kidney. Now, on a fixed income and with no savings, she said, they can't afford basic needs.

"We didn't have a mortgage and we had to take an equity loan because of this (loss)," she said, adding they invested with the firm in 2009, when it was already facing collapse and federal authorities had been warned of its dealings. "Food-wise we eat leftovers beyond compare. I volunteer at a pantry and I'm afraid that I'm going to be one of my own clients and that's scary."

Reach Lyons at 454-5547 or by e-mail at [blyons@timesunion.com](mailto:blyons@timesunion.com).

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**H E A R S T**

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**timesunion** <https://www.timesunion.com/business/article/Trust-is-also-scam-victim-4257947.php>

## Trust is also scam victim

**McGinn, Smith investors were friends of firm's founders or were steered by other brokers**



### IMAGE 1 OF 15

Timothy McGinn, right, and David Smith leave the U.S. District Courthouse after their arraignment for fraud Friday Jan. 27, 2012 in Albany, N.Y. (Lori Van Buren / Times Union)

ALBANY — The guilty verdicts announced Wednesday by a federal jury against former Albany brokers **Timothy M. McGinn** and **David L. Smith** resonated swiftly through the ranks of the estimated hundreds of victims, many of whom were financially devastated by the region's largest fraud case on record.

Some were intimate friends of the embattled brokers, while others had been drawn to invest with the small Albany brokerage, McGinn, Smith & Co., through referrals, country club contacts

or brokers who sold investors on the private placement investments that were the firm's bread-and-butter business.

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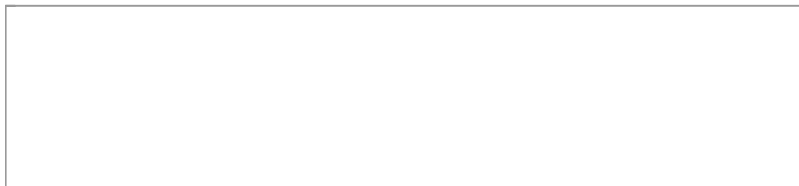
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While some investors said they were wealthy enough to absorb their losses without devastating impact, others said the fraud depleted their

savings and forced them to return to work. The U.S. Securities and Exchange Commission has said about 900 investors, including many institutional investors such as churches and corporations, may have lost up to \$136 million.

**Ron DeLeonardis**, who graduated with McGinn in 1966 from **Colonie Central High School**, lost several hundred thousand dollars of "hard-earned money" that DeLeonardis and his wife, Kathryn, had accumulated through years of devotion to their former business, Bob and Ron's Fish Fry in Albany.

The couple began investing with McGinn in 1981, not long after McGinn and Smith formed their partnership, and had done well for many years until the bottom began to fall out less than

10 years ago. In 2002, when DeLeonardis sold the business, he gave much of the money to McGinn to invest.

"Once the bottom leg came off, everything came tumbling down," said DeLeonardis, 64. "I worked very hard for 34 years ... it was a family business. My wife sacrificed her personal life. We put this trust into Tim and Dave, and it's a shame that it backfired."

Like many other victims, DeLeonardis said he hopes Smith and McGinn will plead guilty in the related civil case filed by the SEC, which is where hundreds of investors may stand their only chance of recouping at least a portion of their losses.

DeLeonardis, who testified at the criminal trial as a government witness, said it would be shameful for more assets to be expended on what many investors believe will be a fruitless civil defense for the fallen brokers.

**Lesley Levy**, a former Wall Street adviser who said she lost up to \$2 million with McGinn and Smith, credited U.S. Attorney **Richard Hartunian** and assistant U.S. Attorney **Elizabeth Coombe**, the lead prosecutor, for presenting the complex case in a way the jury could understand.

"The average person doesn't understand this ... you have to be someone with a Wall Street background," Levy said.

**Earl Seguire Jr.**, a 66-year-old retired state worker in Albany, lost about \$160,000 that he'd invested with McGinn and Smith. Seguire said he was lured to do business with the brokerage in 1992 when he attended a seminar McGinn gave. As did many other victims, he said the firm's offerings worked well for years, until the early to mid-2000s, when the federal government says McGinn and Smith began raiding investor accounts illegally.

"We've got to send a message in this country that you can't use investors' money for your own personal piggy bank," Seguire said.

**Monica Check**, who said she worked hard to secure a comfortable retirement in a small community on Florida's west coast, lost most of her savings, \$100,000, that she invested with McGinn and Smith in 2009. She was unaware at the time, she said, that the firm was crumbling and federal regulators were scrambling to shut it down.

### More Information

Check, who worked in a pharmaceutical company's finance office, said she was angry that McGinn and Smith were not taken into custody Wednesday after being convicted of multiple counts of fraud, conspiracy and tax evasion.

"It gives me satisfaction that they are convicted, but I'm unsatisfied that they are still out on bail," Check said.

DeLeonardis, meanwhile, said the experience has been a double-edged sword because McGinn was a longtime friend, someone the couple often socialized with, including outings at Saratoga Race Course and at cocktail parties.

"When you deal with somebody over 30 years ... you trust them," DeLeonardis said. "It's very emotional because of the personal side of it, because we were such good friends, but to lose everything you've worked for all your life has hurt us very bad."

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Times Union

### Wife of ex-Texas lawman pleads guilty in New York ho...

Times Union

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**HEARST**



# *Exhibit C*

UNITED STATES DISTRICT COURT  
NORTHERN DISTRICT OF NEW YORK

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*Relief Defendants. and*

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David L. and Lynn A. Smith Irrevocable  
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*Intervenor.*  
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**ORDER APPROVING SIXTH CLAIMS MOTION OF WILLIAM J. BROWN,  
AS RECEIVER, FOR AN ORDER (A) APPLYING PREFERENTIAL  
PAYMENT OFFSET TO LESLEY LEVY CLAIMS AND (B) EQUITABLY  
SUBORDINATING LESLEY LEVY CLAIMS**

Upon the Sixth Motion of William J. Brown, as Receiver, for an Order (a)  
Applying the Preferential Payment Offset to Lesley Levy Claims and (b) Equitably  
Subordinating Lesley Levy Claims (“Motion”); and notice of the Motion having been given  
to the Securities and Exchange Commission and Levy, by first class mail, and all parties  
who have filed a Notice of Appearance in this action by ECF, and all creditors of the  
McGinn, Smith entities and other parties in interest via the Receiver’s website, which notice

is deemed good and sufficient notice; and the Court having deemed that sufficient cause exists; it is therefore

ORDERED, that the Motion is approved, and it is further

ORDERED, that the application of the Preferential Payment Offset to reduce the distributions to Levy is approved as set forth on Exhibit A to the Motion, and it is further

ORDERED, that the remainder of the Levy Claims, after application of the Preferential Payment Offset, shall be equitably subordinated to the Investor B Claim, and the rights of the Receiver to object on any other basis to the claims of all investors or claimants, including Levy and Investor B, are expressly preserved.

Dated: \_\_\_\_\_, 2019

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HON. CHRISTIAN F. HUMMEL



UNITED STATES DISTRICT COURT  
NORTHERN DISTRICT OF NEW YORK

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LAUREN T. SMITH, and NANCY MCGINN,

*Defendants,*

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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.*

-----X  
**DECLARATION OF WILLIAM J. BROWN, AS RECEIVER, IN SUPPORT OF  
SIXTH CLAIMS MOTION FOR AN ORDER (A) APPLYING PREFERENTIAL  
PAYMENT OFFSET TO LESLEY LEVY CLAIMS AND (B) EQUITABLY  
SUBORDINATING LESLEY LEVY CLAIMS**

William J. Brown, as Receiver, declares, under the penalty of perjury, pursuant to 28

U.S.C. § 1746, as follows:

1. I am the Receiver of McGinn, Smith & Co. Inc., et al. (“MS & Co.”) appointed by the Court in this action pursuant to the Preliminary Injunction Order dated July 26, 2010 (Docket No. 96).

2. I make this Declaration in support of the Receiver’s Sixth Claims Motion (“Motion”) for an Order (A) applying the Preferential Payment Offset to claims held by investor Lesley Levy (“Levy”), as set forth on Exhibit A to the Motion, and (B) equitably subordinating the Levy Claims to the Investor B Claim (each as defined herein).

### **PROCEDURAL BACKGROUND**

3. MS & Co. was a broker-dealer registered with the Securities and Exchange Commission (“SEC”) with its headquarters in Albany, New York from 1981 to 2009. From 2003 through 2010, the broker-dealer was owned by David L. Smith (“Smith”), Timothy M. McGinn (“McGinn”), and Thomas E. Livingston.

4. On April 20, 2010, the SEC filed a Complaint initiating the above-captioned action (Docket No. 1). Also, on April 20, 2010, this Court granted a Temporary Restraining Order (Docket No. 5), which, among other things, froze certain assets of the above-captioned Defendants and Relief Defendants, and appointed the Receiver as temporary receiver with respect to numerous entities controlled or owned by Defendants McGinn and Smith including those listed on Exhibit A to the Preliminary Injunction Order entered in this action (Docket No. 96) (collectively, the “MS Entities”).

5. 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).

6. On August 3, 2010, the SEC filed an Amended Complaint (Docket No. 100). On June 8, 2011, the SEC filed a Second Amended Complaint (the “Complaint”) (Docket No. 334). On February 17, 2015, the Court issued its Memorandum-Decision and Order (Docket No. 807) (“MDO”) granting the SEC’s motion for summary judgment. The Court entered judgments in favor of the SEC in 2016 (Docket Nos. 835, 836, 837).

7. Generally, McGinn and Smith “orchestrated an elaborate Ponzi scheme, which spanned over several years, involved dozens of debt offerings, and bamboozled hundreds of investors out of millions of dollars.” MDO at 7. McGinn and Smith raised over \$136 million between 2003 and 2010 in over twenty unregistered debt offerings, including the Four Funds -- FAIN, FEIN, FIIN, and TAIN -- and various Trust Offerings, by representing that investor money would be “invested,” when instead it was “funneled” into various entities owned or controlled by McGinn and Smith. That money was then used to fund unauthorized investments and unsecured loans, make interest payments to investors in other entities and offerings, support McGinn’s and Smith’s “lifestyles,” and cover the payroll at MS & Co. MDO at 7.

#### **REDUCTION AND ELIMINATION OF PAYMENTS TO MS & CO. INVESTORS**

8. Investors were made aware of problems with their MS & Co. investments in January 2008, when Smith sent a letter to investors in the Four Funds notifying investors that interest payments on the junior tranches of Notes were being reduced to from 10.25% to 5%. *See* Exhibit A, attached here; *see also* MDO at 12. By April 2008, interest payments on the junior tranches of Notes were eliminated entirely. *See* Exhibit B, attached here; *see also* MDO at 12. In October 2008, David Smith sent a letter to all Note holders in the Four Funds outlining a restructuring plan which extended the maturity dates

of the Notes, reduced interest payments for all tranches, and forfeited all future fees due to MS & Co. *See* Exhibit C, attached here; *see also* MDO at 12-13. The issues were not limited to the Four Funds and interest and other payments owed to investors on account of investments in TDM Cable Trust 06, one of the Trust Offerings sold by MS & Co., had ceased by November 2009. On December 18, 2009, FINRA informed Smith that MS & Co. was in violation of FINRA's net capital rule and that MS & Co. was required to "cease conducting a securities business." MS & Co. ceased operations in December 2009. SEC Statement of Material Facts at 1 (Docket No. 711). On April 4, 2010, FINRA suspended MS & Co.'s membership. *Id.*

**PREFERENTIAL PAYMENT TO LEVY**

9. I have recovered evidence in the books and records of MS & Co. showing that on January 27, 2010, funds in the amount of \$90,000 were wired into an account at M&T Bank in the name of TDM Cable Funding LLC Trust 06 ("Account") by an MS & Co. investor ("Investor B") with the intent of purchasing \$100,000 worth of TDM Cable Trust 06 certificates. A redacted copy of the January 2010 statement for the Account ("Account Statement") is attached here as Exhibit D. A redacted copy of Investor B's direction to purchase TDM Cable Trust 06 certificates with the \$90,000 is attached here as Exhibit E.

10. The transaction was conducted by broker-dealer, Phillip Rabinovich ("Rabinovich"). In the administrative proceeding commenced by the SEC against Rabinovich and other brokers, Levy submitted an Affidavit in support of Rabinovich ("Affidavit"), attached here as Exhibit F. Levy's Affidavit stated that she had known Rabinovich for over 25 years and had been a client of Rabinovich for approximately 15

years. Affidavit ¶ 2. In the Affidavit, Levy stated that “[b]ased on our relationship and the 25 years I have known him, I find the very notion that he should be held responsible for the loss I suffered absolutely absurd.” *Id.* ¶ 5. Levy went on to attest that, “[i]n my estimation, Mr. Rabinovich continues to retain a stellar reputation among his clients . . . .” *Id.* ¶ 6.

11. Because FINRA had required MS & Co. to cease conducting a securities business in December 2009, Rabinovich made the trade through another brokerage firm, Dinosaur Securities LLC. Although Investor B’s wire payment was deposited into the Account, there was no investment in TDM Cable Trust 06 recorded in Investor B’s name in the books and records of MS & Co. Notwithstanding that an investment was not recorded on MS & Co.’s books and records in Investor B’s name, I intend to grant Investor B a claim in the amount of \$90,000 to account for Investor B’s transfer of funds into the Account (“Investor B Claim”).

12. The Account Statement further shows that, on January 28, 2010, the \$90,000 wired into the Account by Investor B was wired out of the Account to National Financial Services (“NFS”). I have recovered a wire transfer confirmation showing that the funds were wired from the Account to NFS for the benefit of Levy (“Preferential Payment”) as a redemption of Levy’s investment in TDM Cable Trust 06 9.25% 48 Months Contract Certificates in the principal amount of \$100,000. *See* Exhibit G, attached here. Although MS & Co. was not supposed to be operating as a securities business as of December 18, 2009, the Preferential Payment was authorized by either McGinn or Smith.

13. All of Levy’s claims (collectively, “Levy Claims”) were, in the Receiver’s original claims reconciliation process, adjusted for pre-Receivership distributions of principal and interest like all other investor claims, as shown on the Receiver’s Claims

Website (defined below). It was only thereafter when Investor B asserted their \$90,000 TDM Cable Trust 06 9.25% claim that I and my staff discovered the preferred Levy redemption. As a result, the Levy Claims have not been adjusted to account for the Preferential Payment. In connection with the distribution process, as described in greater detail in paragraph 22 below, Levy completed and signed the Questionnaire (as defined below) asserting her right to recover on a claim for which she had already been paid. A redacted copy of Levy's completed and executed Questionnaire is attached here as Exhibit H. Levy failed to report her receipt of the Preferential Payment on her Questionnaire. *See* Exhibit H, at 2.

#### **CLAIMS PROCEDURE**

14. On March 9, 2012, in my capacity as Receiver, I filed a Motion ("Claims Procedure Motion") (Docket No. 466) for entry of an Order approving, among other things, the Receiver's proposed procedure for the administration of claims against the MS Entities.

15. On March 27, 2012, the Court entered an Order granting the Claims Procedure Motion (Docket No. 475), which was subsequently amended by an Order dated April 17, 2012 ("Claims Procedure Order") (Docket No. 481). Each investor and known creditor of the MS Entities was mailed on May 1, 2012 an Access Notice describing the claims process and enclosing (i) Notice of the Claims Bar Date and Claims Procedure and (ii) a Claim Form. A confidential password providing access to the Receiver's Claims Website at [www.mcginnsmithreceiver.com](http://www.mcginnsmithreceiver.com) ("Claims Website") was also provided. If an investor or creditor agreed with the description and amount of their claim(s) as listed on the Claims Website and the claim(s) were not listed as disputed, contingent or unliquidated, the

investor or creditor did not need to take any further action. All other investors and creditors needed to timely file a paper claim before the bar date of June 19, 2012, as further described in detail on the Claim's Website.

16. The Claims Procedure Order established June 19, 2012 ("Bar Date") as deadline for creditors and investors to file claims against the MS Entities.

17. In accordance with the Claims Procedure Order, nearly six hundred creditors and investors timely filed paper claims prior to the Bar Date. In addition, more than 3,127 claims of investors and creditors were included on the schedules posted by the Receiver on the Claims Website in accordance with the Claims Procedure Order.

18. The Receiver conducted an initial review of the paper claims timely filed by creditors and investors in accordance with the Claims Procedure Order and determined it was necessary to establish a reserve as to investor claims totaling approximately \$23,617,190 since those claims have been listed by the Receiver as disputed, contingent or unliquidated.

#### **PLAN OF DISTRIBUTION PROCESS**

19. On December 30, 2015, the Receiver filed a Motion (Docket No. 847) ("Plan Distribution Motion") to seek approval of (i) a plan of distribution of assets of the MS Entities to investors ("Plan of Distribution"); and (ii) interim distributions to investors with allowed claims scheduled or timely filed in accordance with the Claim Procedure Order.

20. On October 31, 2016, the Court entered a Memorandum-Decision and Order (Docket No. 904) ("Plan Distribution Order") granting the Plan Distribution Motion,

overruling objections, approving the Plan of Distribution, and allowing the Receiver to make interim distributions as set forth in the Plan Distribution Motion.

21. Among other things, the Plan of Distribution provides for a reserve for disputed claims to allow the Receiver to make initial distributions, but to also provide for funds to be reserved until any objections to disputed claims can be heard and decided by final order of the Court. As of April 15, 2019, \$6,578,150 has been distributed to investors with allowed claims as a First Distribution. I estimate that 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).

22. In accordance with the Plan of Distribution, in February 2017, I distributed questionnaires to all of the investors (“Questionnaires”), which, among other things, required investors to report under penalty of perjury whether they received, or were pursuing a recovery from, any other source related to MS & Co. The Questionnaires also included a description of the investors’ investment and the amount of their claim pursuant to the books and records of MS & Co. Although Levy’s claim amount as set forth on the Questionnaire did not reflect the receipt of the Preferential Payment, Levy certified under penalty of perjury that she did not receive any payment related to her TDM Cable Trust 06 investment; *see also* Exhibit H.

23. The Plan of Distribution provides that all investor claims would be calculated by using the “Net Investment” methodology, i.e., the claim amount is equal to the amount of the initial investment made less any distributions received prior to the appointment of the Receiver, including any distributions of principal or interest. Plan of Distribution, Art. IV. The Plan of Distribution further provides for a collateral recovery



offset (“Collateral Recovery Offset”), where distributions made on account of investor claims will be reduced on a dollar-for-dollar basis to the extent the investor has received a recovery from a source other than the Receivership in connection with their claimed loss.

*Id.* Art. II.

### **CLAIMS MOTIONS**

24. On September 21, 2017, in my capacity as Receiver, I filed a Motion (Docket No. 937) (“First Claims Motion”) to seek disallowance of certain filed paper claims that were duplicative of the corresponding claims granted by the Receiver. On November 9, 2017, I filed a Statement (Docket No. 957) in furtherance of the First Claims Motion, adjourning the First Claims Motion with respect to those duplicative investor paper claims filed by investors whose Receiver-granted claims have been disputed by the Receiver. On December 28, 2017, the Court entered an Order granting the First Claims Motion and disallowing the duplicative paper claims other than with respect to those filed by investors with disputed claims (Docket No. 966).

25. On February 15, 2018, in my capacity as Receiver, I filed a Motion (Docket No. 974) (“Second Claims Motion”) to seek disallowance of certain filed paper claims for which there is no basis for payment in the books and records of MS & Co. On April 13, 2018, the Court entered an Order granting the Second Claims Motion and disallowing the paper claims.

26. On March 19, 2018, in my capacity as Receiver, I filed a Motion (Docket No. 984) (“Third Claims Motion”) to seek disallowance of certain claims of former MS & Co. brokers. On May 4, 2018, I filed a Reply (Docket No. 1002) to the Response of Frank Chiappone (Docket No. 995) to the Third Claims Motion. On March 6, 2019, the

Court entered an Order granting the Third Claims Motion and disallowing the brokers' claims.

27. On July 6, 2018, in my capacity as Receiver, I filed a Motion (Docket No. 1009) ("Fourth Claims Motion") to seek disallowance of paper claims filed by certain preferred investors and to apply a preferential payment offset to the distributions to be made to the preferred investors. On August 27, 2018, I filed a Reply (Docket No. 1020) ("Reply") to the Opposition filed by certain preferred investors (Docket No. 1019) to the Fourth Claims Motion.

28. On October 16, 2018, in my capacity as Receiver, I filed a Motion (Docket No. 1025) ("Fifth Claims Motion") to seek to apply a preferential payment offset to the distributions to be made to preferred investors One City Center Associates and Burton Fisher.

29. On March 6, 2019, the Court entered an Order granting the Fourth Claims Motion and the Fifth Claims Motion, disallowing the preferred investors' paper claims and applying the preferential payment offset (Docket No. 1042) ("Preferential Offset Order").

### **NOTICE**

30. In connection with service of the Motion and all accompanying papers, including this Declaration, I will cause to be mailed to Levy a copy of the Motion and related pleadings.

Dated: April 25, 2019

/s/ William J. Brown  
William J. Brown

# *Exhibit A*

January 15, 2008

\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

Re: \$ \_\_\_\_\_ Third Albany Income Notes, LLC – Internal Investment # \_\_\_\_\_  
Registration: \_\_\_\_\_

Dear: \_\_\_\_\_

As an investor in one of the following mezzanine debt funds (FUNDS) managed by McGinn, Smith Advisors (MSA), we thought that it was important to communicate with you the general status of the funds, our view on the current credit markets and their impact on your fund, how MSA views the markets going forward, and steps that we are considering to address the present credit conditions.

The FUNDS include:

- First Independent Income Notes, LLC
- First Excelsior Income Notes, LLC
- Third Albany Income Notes, LLC
- First Advisory Income Notes, LLC

Each of the LLC's has three series of notes that have been issued: Senior Notes, Senior Subordinated Notes, and Junior Notes, all with varying interest rate coupons and maturities. In each of the LLC's, the notes starting with the Senior down through the Junior have a primary call on the assets and cash flow of the various investments in each of the LLC's. Thus, the Senior Notes receive all of the income and asset value of the entire LLC until satisfied, followed by the Senior Subordinate Notes, and finally the Junior Notes are entitled to asset coverage and cash flow only after the Senior and Senior Subordinate Notes are satisfied. You are an investor in the Junior Notes.

MSA is the sole equity member of all the FUNDS, and therefore as the managing member is responsible for all the decisions impacting the business of the FUNDS. MSA has a fiduciary responsibility to manage the FUNDS in a manner consistent with the investment goals and to best preserve the assets of the FUNDS.

Over the last several months, a number of investors have inquired as to the impact on the FUNDS due to the turmoil, and in some cases collapse, of the various debt and credit markets, as a result of the sub-prime mortgage debt crises that started to boil over in July of 2007. As the impact has grown, and in our judgment the crisis shows less and less probability of being resolved quickly and easily, MSA has begun an effort to get

ahead of events and formulate strategies that will protect the value of the LLC's and your investment in them.

While the media, including newspapers and financial publications, have provided a daily accounting of the credit market crisis and the subsequent financial impact, I realize some of you may not be in a position or have the interest to follow what has been taking place, so I have provided a brief summary. First, it should be understood that the credit crisis is primarily a result of the major Wall Street investment banks and the largest commercial banks in the country developing and marketing a variety of investment instruments built on a shaky foundation of sub prime mortgages. Sub prime mortgages can be defined as those mortgages offered to borrowers with spotty credit, mortgages that required too little equity, mortgages on properties in less desirable areas or where the supply of housing was growing beyond the demand, and where the terms of the mortgage often emphasized "teaser rates" or interest only requirements early in the amortization schedule. While these types of mortgages carry a high risk of default, the early years of the recent housing boom produced unusually low rates of default and created a false sense of security for the mortgage lenders.

In pure destructive power, the sub prime mess has become Wall Street's version of Hurricane Katrina. It has reeked havoc on the nation's largest brokerage firm, Merrill Lynch, and biggest bank, Citigroup, which have announced billions of dollars in losses and have fired their celebrated CEOs. Dozens of similar companies in the mortgage business have folded completely. As stunning as today's losses are, more carnage lies ahead. Wall Street banks are holding tens of billions in risky securities on their books, and no one seems to have any idea what they are worth. The follow on crisis is that confidence in the value of all securities, but mostly the smaller and more illiquid securities, is destroyed. Investors are reluctant to pay any price because they are not sure what the real value is, and if they are forced to sell them in the future they may do so only by slashing prices. Thus, investors go on strike and refuse to bid any price. In addition, many of these securities were purchased with debt. As prices go down, lenders require more security through increased equity. To get equity and raise cash, investors have to sell the illiquid securities. With no real markets, prices are driven forever lower, and a vicious cycle is started. In a high number of cases, there is simply no price that investors are willing to pay, and the value of the securities must be further marked down, generally based on some theoretical model put together by the investment bankers. That is why Merrill Lynch predicted a \$4.5 billion sub prime loss for the third quarter, then jolted investors and analysts three weeks later by announcing that its real default was \$7.9 billion, or 76% more than the initial estimate. And just last week, Merrill Lynch again announced an increase in their losses to over \$15 billion dollars, approximately 3 ½ times their original estimate. And Merrill is not alone. Losses on CDO's, asset backed securities, and other structured products include announced losses by Citigroup (\$9.8 billion, followed by an additional \$24 billion dollars as of January 14<sup>th</sup>). UBS (\$4.4 billion), and Morgan Stanley (\$3.7 billion). These conditions, aside from producing real and enormous losses for the holders of these debt instruments are creating a far more difficult problem for the capital markets in general. The aforementioned lack of liquidity, or the inability to sell ones investments, causes enormous difficulty throughout the investment cycle. For example, companies who are looking to raise equity either in the private or public markets often borrow capital in the form of short term debt in order to



“bridge” the time between the present and when they can complete their equity offering, a time that can easily take up to one year. This type of credit has become increasingly scarce as lenders are withdrawing from the markets until they have a better level of comfort regarding risk and their own financial condition. Merger and acquisition activity that is often financed with debt has dramatically decreased. The last six months has seen daily announcements of the withdrawal of financings for these types of transactions. Meanwhile, the funds at the heart of the situation known as structured investment vehicles or SIV’s – need to find investors for billions of dollars coming due in the next six to twelve months. However, as ratings firms come out with reports that lower the ratings of these type of securities, this causes a further depression in the value of those investments and a large number of buyers are now precluded from investing because their corporate indenture prevents them from investing in lower rated securities. Holders of the SIV notes are bearing the brunt of this fallout because they face two options: they risk losing money if the SIV sells assets at a loss in order to meet their capital needs, including the payment of maturing notes, or try to provide liquidity for the SIV’s by buying more of its debt. The FUNDS in which you are invested have some of those similar problems.

The impact on the FUNDS from the aforementioned credit crisis has primarily been on liquidity and the upcoming need to sell assets in the next year to pay off maturing notes. While there have been losses in the FUND’s investments, we have a limited and manageable exposure to the real estate markets, including the mortgage market. Our real concern is the present and future ability to sell our present investments at a value that is needed to meet the FUND’s obligations. When managing the FUND’s assets, MSA always had to be mindful of meeting the future liquidity needs. It was always anticipated that those needs would be able to be met through a combination of having some of the assets mature at approximately the same time as its liabilities, that some of the assets would be invested in public securities with a ready market, that the FUNDS would have the ability to raise new capital from either present or new investors, and that some of the assets would be able to be sold to other investors. The credit crisis has impacted all of those strategies, and unless the markets dramatically improve over the next year, we will face the same challenges that we do today.

As mentioned previously, there presently is no market at fair prices that exist for non-public debt securities. Investors are now looking for the safest most liquid securities until the crisis is better understood or is resolved. In addition, many of the investments in these companies are dependent on new financings to have the capital to pay off their existing debt to the FUNDS. Several of our investments fall into this category. For example, we have an investment in several of the FUNDS in a company that provides print and advertising financing for the independent film industry. For the last nine months they have had a commitment from an investment bank to raise approximately \$10 mm in equity, contingent on the company’s ability to secure a credit line of \$10-15 mm. That capital is to be used to retire their obligation to the FUNDS. To date, the company has been unable to procure the credit line, and thus the equity raise has been put on hold. They have no source of funds to repay us until that capital raise is completed. Thus, we have no choice but to extend their debt, probably past the time when our obligations to our debt holders are due. Another example is a company that we have financed that is in the business of evaluating and providing capital to companies based on the worth of the

company's intellectual property. A major investment bank has given the company a term sheet that will provide \$750 million of financing over the next five years. However, the original structure called for a substantial portion of that capital to be provided up front and that would be used to repay our debt. The investment bank is now only willing to provide the capital on a staggered basis over the next five years, with the result that while we are confident of being repaid in full, it is not likely that we will be paid out until the fourth and fifth year of their commitment. Again, a decision that will impact our liquidity for next year.

MSA has determined that we need to be very proactive over the next year to be in a position to overcome these credit market conditions and the lack of liquidity now present. If we have learned anything in being in the business for over 30 years, it is that a financial crisis is never solved in a short time or without substantial pain to investors. We don't believe that this one will be any different. We believe that the credit markets are likely to continue to be under very severe pressure and that a two to three year time horizon is the minimum for a return to normality.

MSA has spent the last several months reviewing a variety of strategies that will address the present problems and give our investors liquidity within a reasonable time frame from what they had originally expected.

First, any strategic approach has to recognize the capital structure of the FUNDS that calls for assets and cash flow to be pledged in their entirety to the most senior class of securities. Thus, as notes mature next year we need to be in a position to first retire the senior one year notes. We are confident that we will be in a position to maintain the current level of interest, and as long as conditions do not materially worsen; we will be able to retire the debt on a timely basis. The second class of securities issued by the LLCs is the Senior Subordinated Notes. Here too, as long as present conditions remain relatively stable, we believe that the current rate of interest will be maintained. However, the ability to retire the entire issue at the same time as the Senior notes is most unlikely. Our present thinking is that these notes will have to be extended for two-three years in order to establish the capital resources to pay off the debt. The third class of securities, the junior notes, present the biggest challenge because they are subordinate to the claims on assets and cash flow of the senior securities. In order to meet the obligations of the Senior securities, the FUNDS have to pledge all of their cash flow to them, **thus at the present time the rate of interest is being reduced to 5% on the Junior notes until such time as some of our investments return to a timely cash flow or we can refinance our debt or raise additional capital.** MSA is presently working on plans to provide the needed liquidity and help some of our investments restructure their debt in order to meet their obligations.

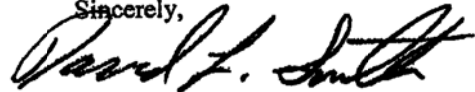
**MSA is making a significant contribution to increasing the cash flow for all of the Funds by suspending the commissions due to McGinn, Smith & Co., the advisory fee due to MSA, and the administrative fee due to McGinn, Smith Capital Holdings. These fees for the combined Funds amount to \$2,827,500, annually.**

Over the next year we will hopefully be able to get a better handle on how to evaluate our investments. This difficulty to evaluate remains the number one problem for credit markets today. During this summer's credit crunch, more than 80% of investors in bonds tied to the mortgage market said they had trouble obtaining price quotes from their bond dealers. "Michael Vranos, recently told investors in his large hedge-fund company, Ellington Management Group, that he was suspending investor redemptions because he couldn't figure out values for some of the fund's investments". "There is no way to determine values that would be simultaneously fair both to investors redeeming from the funds and to investors remaining in the funds", he wrote in a September 30<sup>th</sup> letter. Recently the Federal Reserve, in a move to make credit markets more liquid, announced a plan that is designed to enable banks to borrow money directly from the Fed at below-market rates. However, there can be no assurances that this plan will ease the current credit and liquidity crisis.

In conclusion, MSA believes that by trying to get out in front of the problem of having sufficient liquidity by next year when the FUNDS notes become due, they are both doing the right thing and will lesson the anticipated challenges a year from now. **The Senior and Senior Subordinated note holders will maintain current interest payments, while Junior note holders will have their interest reduced to 5%.** Over the course of the year we will communicate with you regarding the progress and plans that we are making to address the liquidity needs for next December. Our obvious goal is first preservation of your investment and second to maximize cash flow to the FUNDS in order to have sufficient cash to meet the interest payments.

If there are any questions concerning this communication, please contact your McGinn, Smith & Co. representative.

Sincerely,



David L. Smith  
Managing Member  
McGinn, Smith Advisors



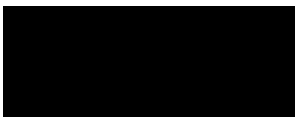
# ***Exhibit B***

*McGinn Smith  
& Company, Inc.*

Investment Bankers • Investment Brokers

6 Executive Park Dr.  
Clifton Park, NY 12065  
518-348-0060  
Fax 518-348-0107  
www.mcginnsmith.com

April 11, 2008



Re: \$25000 First Independent Income Notes, LLC – Internal Investment # 1800  
Registration:

Dear

In our communication of January 15, 2008 we outlined for you the negative impact that the present credit crisis resulting from the sub-prime mortgage collapse was having on First Independent Income Notes (FIIN), LLC. We provided the background leading to the crisis and reasons why we felt it was likely to worsen before the markets were able to stabilize. We cited the tremendous losses that the major commercial and investment banks were being forced to take and that these losses were spreading to institutions worldwide and to credit markets far beyond the mortgage business. We mentioned that the major impact was on market liquidity and that debt holders were being forced to sell securities and investments at prices below fair market value in an effort to deleverage their balance sheets and to meet forced margin calls. Unfortunately, all the problems that we cited have become more acute, and by now the daily news brings repeated announcements of the adverse effects the crisis is having on the general economy and of major financial institutional failures such as the collapse of Bear Stearns, Inc.

The central theme for all fixed income investments and managed funds of such investments has been the inability to refinance their investments and thus be forced to cease or eliminate interest payments and distributions. Leading the way in this category has been the area of Auction Rate Securities (ARS) which are long term municipal bonds, corporate bonds, and preferred stocks that are traded at auctions that set the instrument's interest rate and ultimately the price of the security. The market in total is somewhere around \$320 billion and it is estimated that \$80 billion or 25% of the market has recently failed. These investments were often marketed as substitutes for money market accounts with a higher yield. Many businesses invested their excess cash in these instruments and now find themselves not only not receiving interest, but with no access to their cash as well. The good news is that the majority of the underlying investments are still paying interest, but the funds just are not able to refinance them at rates that allow them to pay investors their principal.

Since our last communication with you, two of our investments have been forced to eliminate their dividend or cease distributions. One was a result of their loss of refinancing from a bank that was a major lender to Countrywide Credit, the country's largest sub-prime mortgage lender and who suffered major losses from that relationship and had to withdraw their commitment. The other was a holder of only AAA mortgages and who in November assured us that they were at limited risk and the dividend was safe. In February, they were forced to sell most of their portfolio to meet margin calls and suffered losses that have wiped out their earnings

GOVERNMENT  
EXHIBIT

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and their ability to pay their dividend. This in turn has put increased pressure on our cash flow and our ability to meet our obligations. Consequently, we are being forced to eliminate the interest payment to the Junior Subordinated debt holders for this quarter.

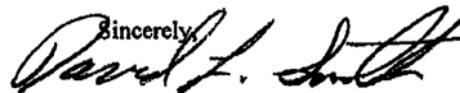
In keeping with our goal to solve the longer term problem of capital preservation we have been working on two fronts. First, we are working with individual companies within our portfolio to help them gain access to capital that would allow them to operate during this crisis. I am pleased to report, that in two of our investments we have been successful and that I am confident that later in the year both of these companies will be successful in obtaining permanent financing that will bring liquidity back to our investment.

The second area is to restructure the Funds, or at least the Junior Subordinated debt, in order to have a plan that will provide investors with an eventual exit. The issues here are complex because of the need to preserve the rights of the Senior and Senior Subordinated Noteholders. We have engaged securities counsel to assist us with the restructuring, but they have not yet been willing to provide a legal opinion as to a particular course of action. One of the ideas that we are pursuing is that instead of a total restructuring that will carry the risk that the Senior Noteholders might find objectionable we will keep the structure intact, but offer Junior Subordinated Noteholders an opportunity to receive equity in other investments that will provide them an additional source of return for their investment in the FUNDS.

In addition to having the cash flow in the FUNDS recently reduced and therefore causing us to suspend the quarterly interest for the Junior Subordinated Noteholders, we have also been advised by counsel that distributions at this time quite probably reflect a return of capital and not interest, and therefore distributions might be considered an invasion of the principal due to the Senior and Senior Subordinated Noteholders. This is a result of not knowing how and where to price our investments in these very illiquid markets. We have also heard from several Junior Subordinated Noteholders that until market conditions become clearer, they would rather suspend their distributions which are taxable interest in order to preserve future distributions of return of capital which of course are not taxable.

We do expect to have a better picture by next quarter as to a specific plan of action available to us going forward and of course the hope that markets will at least stabilize and stop retreating. However, we repeat, we do not view this crisis to be easily settled or to exhaust itself anytime soon. There has been severe and long lasting damage to the U.S. and world financial markets that will require patience to work through.

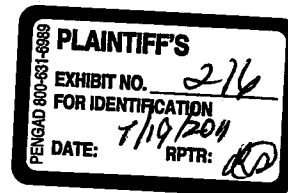
As always, if there are any questions regarding your account or this memorandum, please contact your McGinn, Smith & Company representative.

Sincerely,  


David L. Smith  
Managing Member  
MS Advisors, LLC

DLS/gbg

# *Exhibit C*



**First Independent Income Notes, LLC**

99 Pine Street  
Albany, NY 12207  
Phone 518-449-5131  
Fax 518-449-4894

October 13, 2008

RE [Redacted]

Re: \$5,000 First Independent Income Notes 7% due 12/15/08  
Internal Investment # [Redacted]  
Registration: [Redacted]

Dear Mr. & Mrs. [Redacted]

*copy*

This communication is being sent to investors of First Independent Income Notes, LLC (the FUND) in each of the three classes of Notes, Senior, Senior Subordinated, and Junior maturing on December 15, 2008. The purpose of the communication is to apprise you of the status of your investment and also inform you of the restructuring plan that has been presented to the FUND's Trustee, McGinn, Smith Capital Holdings Corp. by the FUND's managing member, McGinn, Smith Advisors, LLC.

McGinn, Smith Advisors, LLC (MSA) has determined that as a result of losses incurred in the FUND's investments and the total illiquidity for the vast majority of the FUND's investments it is not possible to redeem the Notes on the due date of December 15, 2008 and will require a restructuring of all classes of Notes. In restructuring the notes, MSA has taken into account the responsibility of the Trustee to address both the principal and interest payments due to the Senior noteholders and therefore must reschedule future interest and principal payments for all three classes of noteholders, giving priority to the Senior noteholders. Based on best estimates of current cash flow and present liquidity, MSA has developed a plan that alters scheduled interest and principal payments for all three classes. All three classes are having their maturities extended and their interest payments reduced. MSA has the responsibility to manage the FUND consistent with the provisions of the note's indenture and in a manner that best protects the assets of the FUND. Accordingly, MSA will be presenting a plan outlined later in this communication that in its sole judgment provides for an orderly liquidation of assets, payment of reasonably expected cash flows, and gives priority to the Senior Noteholders over the Senior Subordinated Noteholders and the Junior Noteholders. The plan takes into account that current conditions in financial credit markets presently offer



no liquidity for almost any financial instrument other than U.S. Treasury Notes and Bonds. The investments in the FUND are primarily non public securities that presently have no secondary market for resale and in fact do not have the ability to even establish a fair market value. The plan makes assumptions that cannot be relied upon with any certainty. Events in the US and world financial markets have been changing with a degree of volatility never before experienced at any time in history. The Credit market crisis that started approximately 18 months ago with the troubles in the sub prime mortgage market has accelerated to the point that threatens to impair the entire world's financial foundations and has spread from Wall Street to Main Street. Under these conditions, any planning has to be subject to changing events. We have assumed that markets will continue to be unstable and primarily illiquid for at least two years. The damage to the world's banking system and investment markets is very severe and in our judgment will dramatically change the nature of markets for years to come. While governments, worldwide are rushing to shore up the system with liquidity and taking steps to restore confidence the fact is that no one knows what the ultimate impact of their actions and the reaction of markets will be. What was initially a financial crisis is now a full blown worldwide economic crisis with unknown consequences. MSA is fully confident that financial markets will eventually stabilize and that investor confidence and liquidity will be restored. Anything less is just not acceptable, and therefore the allocation of resources, new efforts of governmental oversight and regulation, and cooperation on a global scale of financial markets is expected to ultimately resolve the present crisis. But the aforementioned intervention in markets will certainly change the way markets work and with any change comes the need for patience and time for investors to first understand and then accept those changes.

As I write this memo the US Stock Market has just finished the day with the Dow Jones Industrial average down over 500 points and down almost 900 points for the last two days. This of course is subsequent to the "rescue bill" or formally the "Emergency Economic Stabilization Act of 2008" signed into law last Friday after several weeks of Congressional wrangling. While in my opinion this was a necessary first step, the idea in some circles that its ultimate passage would bring instant cure to what was ailing the credit markets was ill founded. The stock market's decline is just a symptom of the credit crisis, and while I am in total sympathy for all of us suffering market losses, the real issue is the total lack of liquidity in the credit markets. This is the major issue that impacts your investment in the FUND. Lack of liquidity simply means that there are no efficient markets to buy and sell investments because investors have lost confidence that they can fairly judge what those investments are worth. As the events of the mortgage markets and eventually all fixed income markets played out over the last 18 months, investors repeatedly got burned on making a decision to invest. A sophisticated hedge fund investor made a \$1.8 billion investment last April in Washington Mutual, the country's largest saving bank, only to see it reduced to zero after being taken over by the FDIC last month. National political leaders assured us this summer that Fannie Mae and Freddie Mac, our two leading GSE (Government Sponsored Enterprises) mortgage lenders, were financially sound only to be declared bankrupt and taken over by the FDIC in mid September. Three of the five largest investment banks, Bear Stearns, Merrill Lynch, and Lehman Brothers no longer exist. AIG, the world's largest insurance

COM

company required an \$85 billion cash infusion and equity investors were wiped out. Hundreds of banks and mortgage companies have been closed including the forced sales of Wachovia to Wells Fargo and Citi Corp. Virtually all financial institutions have had to either cut or eliminate dividends in order to strengthen their balance sheets. Other evidence of the cessation of liquidity in the credit markets include:

- 1.) billion dollar hedge funds such as D.B. Zwirn and Pardus Capital Management refused to allow investors to redeem because they were unable to sell assets to raise cash
- 2.) last week \$120 billion of commercial paper not marketable, causing companies to lose liquidity for normal operating functions like payroll
- 3.) despite a lowering of interest rates, banks refusing to lend overnight to other banks from fear of not knowing the financial soundness of the borrower
- 4.) Reserve Money Market Fund assets fall below the one dollar redemption price and overnight withdrawal of \$40 billion of the \$60 billion in assets forces the fund to cease redemptions
- 5.) The College Fund, who manages assets for 1500 college endowments and their operating funds restrict access to their money market fund to 38% of their deposits and state that 100% of your capital won't be available until 2010

There are hundreds of other examples that have occurred and demonstrate the liquidity crisis. Most of you are aware of this because the media has been giving this story full attention for months. The reason that it is important for you to be aware of the freezing of the credit markets is because it impacts the investments in the FUND in a variety of ways. First, if the most liquid and strongest investment assets such as money market funds, commercial paper, and mortgages are having difficulty in finding buyers, than the ability for almost all other assets to have liquidity is impossible. Second, if forced to sell these assets in order to redeem the notes, the market price would be far below fair market value. As an example, Merrill Lynch in July, in an effort to get some of these assets off their balance sheet and receive cash, sold \$30 billion worth for just 22 cents on the dollar. And even then, the buyer forced Merrill Lynch to finance 75% of the purchase with a non-recourse loan which meant the true cost of the purchase was just 6 cents on the dollar. Third, many of the assets, including loans of the companies in our portfolio, were dependent on subsequent financing in order to repay us. Often, our loans were bridge loans to companies until they could get permanent financing through stock or bond offerings. The initial public offerings (IPO's) hit a 5 year low in July and included only some of the most visible companies in the world such as Visa International. Of the 25 billion dollars in offerings through July, Visa accounted for 18 billion dollars, leaving just 6 billion dollars for the other 23 companies taken public. Thus, the companies in our portfolio have been totally shut out, and in several instances the capital raises included money to satisfy their debts to us or to provide us with liquidity for our investments. When these offerings will once again be available is not determinable, but it is not likely to be anytime soon.

*CM*

So what is next for what former Chairman of the Federal Reserve, Alan Greenspan, has identified as the once in a century financial crisis? First, the Federal Government continues to be active through all of its agencies. As mentioned earlier, Congress recently passed a bill that is to provide \$700 billion dollars to help purchase some of these distressed assets and restore liquidity to the banks so that they can begin to make the loans and provide the credit that allows our economy to begin to function normally. The SEC has decreed that short selling in financial stocks is no longer permitted until further notice. The FDIC has instituted an insurance program for money market funds. They have raised FDIC insurance on bank deposits from \$100,000 per account to \$250,000. This week they have opened the discount window, normally reserved only for banks, to allow for the purchase of commercial paper. Those actions are designed to both restore a semblance of confidence and provide sufficient liquidity for the most critical markets of our economy. However, time is what ultimately is required for banks and financial institutions to deleverage their balance sheets and restore sufficient liquidity that will allow them to once again start lending to businesses and consumers. J.P. Morgan, one of our leading financial institutions, believes that credit losses will eventually exceed 4 trillion dollars and that the housing price decline will bottom out down 30% from 2006 levels and last until 2010.

MSA has tried to evaluate and model the impact of the current crisis on its own investments and put forth a plan that provides for all classes of note holders to first get their principal back and second provide them with some return on their investment in the interim. We have communicated with some of you earlier in the year indicating that MS was working on a plan to meet those objectives, mindful of the Senior notes and the subordination issues of the other two classes. Anything that we would have proposed earlier this year certainly would have already proven to be too optimistic. Thus, our current plan we believe to be very achievable, and we are hopeful that as markets and liquidity are restored to a more normal operational mode, we in fact may be able to accelerate the repayment. However, we must emphasize that we are in uncharted waters and what we have learned from the last 18 months is to expect the unexpected.

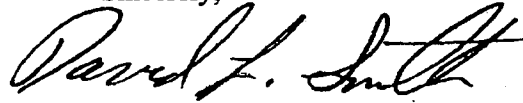
*CMH*

The plan calls for immediate implementation on the next interest payment due date. We have taken great care, and with consultation with our attorneys, to present a plan that we believe to be fair, protect all classes, and still give priority to the rule of seniority. We understand that many of you have personal liquidity issues due to retirement or other financial needs and this plan may put a personal hardship on you. MSA and its affiliate McGinn, Smith & Co. will be making its own sacrifice. Management fees, commissions, and administrative fees aggregate approximately \$2,750,000 per year for all of our FUNDS that are part of this reorganization. In an effort to improve liquidity we have agreed to forfeit all such future fees while this reorganization plan is in effect. Legal fees attributed to defense of our actions and fees incurred in the pursuit of recovering any of our investments will be the responsibility of the FUNDS. The plan will be implemented for the benefit of all investors. Obviously, to be fair and acceptable to all investors, we cannot entertain a different approach for individual investors. If circumstances change in the future, hopefully for the better, we reserve the right to restructure and implement a new plan.



In conclusion, we thank you in advance for your patience and understanding of the very difficult position that we are in. If there are any questions regarding your accounts or this memorandum, please contact your McGinn, Smith & Company representative.

Sincerely,

A handwritten signature in black ink, appearing to read "David L. Smith". The signature is fluid and cursive, with a large initial "D" and "S".

David L. Smith  
Managing Partner  
McGinn, Smith Advisors

DLS/gg

COPY

The attached is the restructuring plan for First Independent Income Notes, LLC (FIIN) for the Senior, Senior Subordinated, and Junior Noteholders. This Schedule makes no attempt to configure the benefit of asset sales beyond approximately 8% per year of the capital base for the first 6 years due to the manager's inability to predict the timing and price received for asset sales. While we believe that the market environment will remain difficult for the first 2-3 years for asset sales, we remain optimistic that the market should improve subsequent to that period. Fifty percent of the proceeds of those sales will be a return of principal to the Senior noteholders until they are paid in full. Subsequently, the same 50% of asset sales will be returned as principal to the Senior Subordinated noteholders. When both Senior and Senior Subordinated noteholders are paid out in full, distribution of future sales to the Junior noteholders will be at the discretion of MSA, deemed to be consistent with successfully being able to return full principal to those Junior noteholders.

Copy

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COH

**First Independent Income Notes, LLC  
Restructuring Plan of October 2008**

**I. Senior Notes 7%, due December 15, 2008**

Payments: October 15<sup>th</sup>  
January 15<sup>th</sup>  
April 15<sup>th</sup>  
July 15<sup>th</sup>

1. Starting October 15, 2008 through July 15, 2009  
Annual rate of 5%, interest only
2. Starting October 15, 2009 through October 15, 2014  
Annual rate of 5%  
10 year amortization
3. Maturity – October 15, 2014

Example of \$100,000 note:

1<sup>st</sup> year: 5% interest  
4 quarterly payments of \$1,250

2<sup>nd</sup> – 6<sup>th</sup> year - 5% interest, 10 year amortization  
20 quarterly payments of \$3,192.14

Maturity payment - \$56,179.51

*Note: 50% of all liquidated investment proceeds will be applied immediately to principal.*

**II. Senior Subordinated Notes 7.5%, due December 15, 2008**

Payments: October 15<sup>th</sup>  
January 15<sup>th</sup>  
April 15<sup>th</sup>  
July 15<sup>th</sup>

*Copy*

1. 1<sup>st</sup> payment October 15, 2010 through July 15, 2013  
Annual rate of 3%,  
10 year amortization
2. Starting October 15, 2013 through July 15, 2020  
Annual rate of 6%  
7 year amortization

Final payment July 15, 2020

Example of \$100,000 note:

Year 1-2	no payments
Year 3-5	3% interest, 10 year amortization 12 quarterly payments of \$2,903.02
Year 6-12	6% interest, 7 years amortization 28 quarterly payments of \$3,215.20

*Note: Starting in year 7, 50% of all liquidated investment proceeds will be applied immediately to principal.*

III. Junior Subordinated Notes 10.25%, due December 15, 2008

Payments: October 15<sup>th</sup>  
January 15<sup>th</sup>  
April 15<sup>th</sup>  
July 15<sup>th</sup>

1. 1<sup>st</sup> payment October 15, 2010 through July 15, 2014  
5% principal only
2. Starting October 15, 2014 through July 15, 2023  
Annual rate of 5%,  
15 year amortization
3. Maturity July 15, 2003

Example of \$100,000 note:

Year 1-2	no payments
Year 3-6	5% principal only 16 quarterly payments of \$1,250
Year 7-15	5% cpn, 15 year amortization 36 payments of \$1,903.19

Maturity payment - \$39,251.93

**C101**

# *Exhibit D*



FOR INQUIRIES CALL: ALBANY MIDDLE MARKET  
(518) 464-6118

00 0 02179M NM 017

ACCOUNT TYPE
CORPORATE CHECKING

ACCOUNT NUMBER	STATEMENT PERIOD
[REDACTED]	1/01/10 - 1/31/10

TDM CABLE FUNDING LLC  
TRUST 06 ACCOUNT  
99 PINE ST # 5  
ALBANY NY 12207-2776

BEGINNING BALANCE	\$140.33
DEPOSITS & CREDITS	90,000.00
LESS CHECKS & DEBITS	90,000.00
LESS SERVICE CHARGES	0.00
ENDING BALANCE	\$140.33

ACCOUNT ACTIVITY				
DATE	TRANSACTION DESCRIPTION	DEPOSITS & CREDITS	CHECKS & DEBITS	BALANCE
1/01	BEGINNING BALANCE			\$140.33
1/27	INCOMING FEDWIRE FUNDS TRANSFER [REDACTED]	\$90,000.00		90,140.33
1/28	OUTGOING FEDWIRE TRANSFER AUTO NON REP NFS		\$90,000.00	140.33
NUMBER OF DEPOSITS/CHECKS PAID		1	0	

M&T IS EXTENDING ITS PARTICIPATION IN THE FDIC'S TRANSACTION ACCOUNT GUARANTEE PROGRAM (TAG), UNDER WHICH ALL BALANCES IN NON-INTEREST BEARING TRANSACTION ACCOUNTS ARE FULLY GUARANTEED BY THE FDIC THROUGH JUNE 30, 2010. NOW ACCOUNTS (OTHER THAN CERTAIN MUNICIPAL NOW'S) ARE ALSO ELIGIBLE FOR COVERAGE UNDER TAG PROVIDED THAT THE INTEREST RATE ON SUCH ACCOUNT IS NO HIGHER THEN 0.50% PER YEAR THROUGH JUNE 30, 2010. TAG COVERAGE IS IN ADDITION TO AND SEPERATE FROM THE COVERAGE AVAILABLE UNDER THE GENERAL FDIC DEPOSIT INSURANCE RULES.

# ***Exhibit E***



Wired  
1/27/2010

McGinn, Smith & Co., Inc.  
99 Pine St.  
Albany, NY 12207

To Whom It May Concern:

Please accept this letter as authorization to wire \$90,000 from our account  
[REDACTED] to purchase \$100,000 TDM Cable 06 Contract Certificates 9.25% due 11/15/10.

RMS

**Wire Instructions:**

M&T Bank  
ABA# [REDACTED]  
Acct Name: TDM Cable 06  
A/c #: [REDACTED]

Sincerely,

[REDACTED]

# *Exhibit F*



Rabinovich would call to further review, ensuring my overall understanding of risks. I was an accredited investor and completed and submitted the subscription documents as such.


4. I do not believe Mr. Rabinovich made any material misrepresentation or omission about any McGinn Smith security in which I invested. I further do not believe Mr. Rabinovich had anything at all to do with the losses that I incurred in any McGinn Smith security.

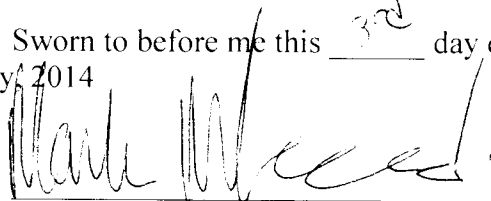
5. Based on our relationship and the 25 years I have known him, I find the very notion that he should be held responsible for any loss I suffered absolutely absurd. The true culprits and thieves, Messrs. McGinn & Smith, have already been found guilty earlier this year of innumerable counts of fraud and secret misappropriation of funds!

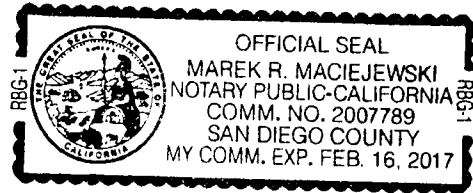
6. There was absolutely nothing that Mr. Rabinovich said or did not say relating to the McGinn Smith securities which could have prevented my losses.

7. In my estimation, Mr. Rabinovich continues to retain a stellar reputation among his clients, even with the stigma of his association to the two criminals McGinn and Smith.

8. I invested well over \$500,000 in principal amount of McGinn Smith securities (specifically, in the First Excelsior Income Notes, Third Albany Income Notes, First Advisory Income Notes and TDM Cable Trust 06 private placement transactions) during 2004, 2005 and 2006.

  
\_\_\_\_\_  
Lesley Levy

Sworn to before me this 3<sup>rd</sup> day of  
January, 2014  
  
\_\_\_\_\_  
Notary Public



# *Exhibit G*

Brian Shea

From: Sadhak, Nisch [NSADHAK@mtb.com]  
Sent: Monday, June 10, 2013 8:41 AM  
To: Brian Shea  
Subject: FW: Wire research

Here is the copy w/all details. Thanks

ICN : MT 100128 003564 000

PAYMENT INFORMATION :

VALUE DATE : 100128 CURR : USD AMOUNT : 90,000.00

MOR : IFN

MOP : 000 SI MOP : OVERRIDE SI MOP : Y

REF : RELATED REF :

PARTY INFORMATION :

PARTY ACCOUNT ID NAME CITY  
RCVD FROM [REDACTED] FT TDM CABLE FUNDING LLC ALBANY NY

BENEFICRY [REDACTED] OV NFS  
ORDER CUST [REDACTED] ALBANY NY 12207 USA

ORDER BANK  
ACCT WITH 021000021 JPMCHASE NY

INTERMED  
SEND CORR  
RCVR CORR

CORR TYP (I/O) : ADJ ICN : COVR ICN :

DETAILS OF PAYMENT : FBO: LESLEY LEVY FFC ACCT #RMR [REDACTED]

BANK TO BANK INFO :

REF : B2Q8921CF0006932 SEND DATE : 01/28/10 TIME : 12:14

\*\*\*\*\*

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# *Exhibit H*





## Securities and Exchange Commission vs. McGinn, Smith & Co. Inc. Investor Questionnaire Pursuant to Receiver's Plan of Distribution

This two-sided form is individualized for each investment you hold or claim per the Receiver's records. A Questionnaire will be mailed to you for each investment. Each form must be completed, properly signed, and returned to the Receiver in the enclosed envelope along with the completed W-9 Form.

No distribution checks will be paid to an Investor with an Allowed Claim until a Questionnaire has been properly completed for each investment and received by the Receiver.

\*\*\*\*\*

Name of Investor(s)	Description of Investment	Amount of Investment
Lesley Levy	TDM CABLE TRUST 06 9.25% 48 MONTHS CONTRACT CERTIFICATES 11/15/10	\$100,000.00
<b>Claim No. 5545 A</b>		

Social Security Number(s) (for each owner) [REDACTED]

Mailing Address:

Street: [REDACTED] Apt. #: \_\_\_\_\_

City: [REDACTED] State: [REDACTED] Zip Code: [REDACTED]

Telephone Number (\_\_\_\_\_) \_\_\_\_\_  
Area Code

E-Mail Address [REDACTED]

Is this investment held in an IRA? Yes \_\_\_/No . If so, provide name and address of Trustee where payment should be sent.

IRA Trustee Name \_\_\_\_\_

Trustee Address:

Street: \_\_\_\_\_

City: \_\_\_\_\_ State: \_\_\_\_\_ Zip Code: \_\_\_\_\_

IRA Account No. \_\_\_\_\_

**Collateral Recoveries**

Did you receive, or are you pursuing or intend to pursue, a recovery from any other source related to McGinn Smith? For example, a recovery through FINRA, other lawsuit, or other type of recovery including insurance.

\_\_\_\_\_ Yes       No

If so, how much? (List separately for each Collateral Recovery)

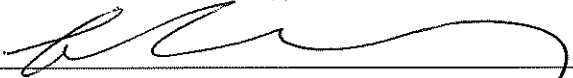
	<u>Net Amount Received by Investor**</u>	<u>Source</u>
1.	\$ _____	_____ Name _____ Address _____ City                      State                      Zip Code
2.	\$ _____	_____ Name _____ Address _____ City                      State                      Zip Code
3.	\$ _____	_____ Name _____ Address _____ City                      State                      Zip Code

\*\* The net amount is the amount received by Investor after all fees are applied. Do not pro-rate among investments.

The undersigned certifies under penalty of perjury pursuant to 28 U.S.C. § 1746 that the information contained in this Questionnaire is true and correct.

Dated: 2-9-~~16~~ 17, 2017.

LESLIE LEVY  
(Printed Name of Investor 1)

  
(Signature of Investor 1)

\_\_\_\_\_  
(Printed Name of Investor 2)

\_\_\_\_\_  
(Signature of Investor 2)

UNITED STATES DISTRICT COURT  
NORTHERN DISTRICT OF NEW YORK

-----X  
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.* :

-----X

**MEMORANDUM OF LAW IN SUPPORT OF SIXTH CLAIMS  
MOTION OF WILLIAM J. BROWN, AS RECEIVER, FOR AN ORDER  
(A) APPLYING PREFERENTIAL PAYMENT OFFSET TO LESLEY LEVY  
CLAIMS AND (B) EQUITABLY SUBORDINATING LESLEY LEVY CLAIMS**

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William J. Brown, as Receiver (“Receiver”) of McGinn, Smith & Co., Inc., et al. (“MS & Co.”), respectfully submits this Memorandum of Law in support of his Sixth Claims Motion (“Motion”) for an Order (A) applying the Preferential Payment Offset to claims held by investor Lesley Levy<sup>1</sup> (“Levy”), as set forth on Exhibit A to the Motion, and (B) equitably subordinating the Levy Claims to the Investor B Claim (each as defined herein).

### **PRELIMINARY STATEMENT**

From 2003 to 2010, David L. Smith and Timothy M. McGinn orchestrated an elaborate Ponzi scheme through which more than 900 investors were defrauded. In late 2009, FINRA ordered MS & Co. to cease conducting operations as a securities business. MS & Co. ceased operations in December 2009.

By that time, investors in TDM Cable Trust 06 ceased receiving any payments on account of their investments. Nevertheless, the Receiver’s due diligence has revealed that a certain preferred investor, Levy, received a material redemption of her TDM Cable Trust 06 investment in January 2010. For no legitimate reason, Levy was elevated to a “preferred” status and was provided with a payment of ninety percent of her principal investment while other similarly situated investors received nothing. Further, Levy acted inequitably by accepting this material payment at a time when it was generally known that other investors were not receiving any payments and MS & Co. was not permitted to operate, resulting in harm to other investors. Thereafter, Levy returned an Investor Questionnaire to the Receiver signed under penalty of perjury pursuant to 28 U.S.C. § 1746

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<sup>1</sup> Lesley Levy voluntarily disclosed herself to the public as a McGinn Smith investor as evidenced by her letters to the Court filed at Docket Nos. 942 and 946 as well as Albany Times Union articles quoting her on September 19, 2011 and February 7, 2013 (copies of which are attached to the Motion as Exhibit B). Consequently, her name is not redacted in the Motion.

claiming payment on this same instrument for which she had already been paid. Levy has a background in securities, as indicated in the Albany Times Union September 19, 2011 news article, where Levy is described as having worked as a Wall Street advisor. It would be inequitable to permit Levy to retain those funds. Accordingly, the Receiver seeks to reduce the distributions on account of all of Levy's other investments by the amount of the Preferential Payment received on a dollar-for-dollar basis and equitably subordinate the balance of Levy's claims due to Levy's inequitable conduct.

### **STATEMENT OF FACTS**

MS & Co. was a broker-dealer registered with the Securities and Exchange Commission ("SEC") with its headquarters in Albany, New York from 1981 to 2009. From 2003 through 2010, the broker-dealer was owned by David L. Smith ("Smith"), Timothy M. McGinn ("McGinn"), and Thomas E. Livingston. Brown Dec'l. ¶ 3.<sup>2</sup>

On April 20, 2010, the SEC filed a Complaint initiating the above-captioned action (Docket No. 1). Also, on April 20, 2010, this Court granted a Temporary Restraining Order (Docket No. 5), which, among other things, froze certain assets of the above-captioned Defendants and Relief Defendants, and appointed the Receiver as temporary receiver with respect to numerous entities controlled or owned by Defendants McGinn and Smith, including those listed on Exhibit A to the Preliminary Injunction Order entered in this action (Docket No. 96) (collectively, the "MS Entities"). Brown Dec'l. ¶4.

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).

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<sup>2</sup> "Brown Dec'l. ¶ \_\_" refers to the Declaration of William J. Brown dated April 25, 2019 filed in support of the Motion.



On August 3, 2010, the SEC filed an Amended Complaint (Docket No. 100).

On June 8, 2011, the SEC filed a Second Amended Complaint (the “Complaint”) (Docket No. 334). On February 17, 2015, the Court issued its Memorandum-Decision and Order (Docket No. 807) (“MDO”) granting the SEC’s motion for summary judgment. The Court entered judgments in favor of the SEC in 2016 (Docket Nos. 835, 836, 837).

Generally, McGinn and Smith “orchestrated an elaborate Ponzi scheme, which spanned over several years, involved dozens of debt offerings, and bamboozled hundreds of investors out of millions of dollars.” MDO at 7. McGinn and Smith raised over \$136 million between 2003 and 2010 in over twenty unregistered debt offerings, including the Four Funds -- FAIN, FEIN, FIIN, and TAIN -- and various Trust Offerings, by representing that investor money would be “invested,” when instead it was “funneled” into various entities owned or controlled by McGinn and Smith. That money was then used to fund unauthorized investments and unsecured loans, make interest payments to investors in other entities and offerings, support McGinn’s and Smith’s “lifestyles,” and cover the payroll at MS & Co. MDO at 7.

**A. Reduction and Elimination of Payments to MS & Co. Investors**

Investors were made aware of problems with their MS & Co. investments in January 2008, when Smith sent a letter to investors in the Four Funds notifying investors that interest payments on the junior tranches of Notes were being reduced to from 10.25% to 5%. *See* Exhibit A to Brown Dec’1; *see also* MDO at 12. By April 2008, interest payments on the junior tranches of Notes were eliminated entirely. *See* Exhibit B to Brown Dec’1; *see also* MDO at 12. In October 2008, David Smith sent a letter to all Note holders in the Four

Funds outlining a restructuring plan which extended the maturity dates of the Notes, reduced interest payments for all tranches, and forfeited all future fees due to MS & Co. *See* Exhibit C to Brown Dec'l; *see also* MDO at 12-13. The issues were not limited to the Four Funds and interest and other payments owed to investors on account of investments in TDM Cable Trust 06, one of the Trust Offerings sold by MS & Co., had ceased by November 2009. Brown Dec'l. ¶ 8. On December 18, 2009, FINRA informed Smith that MS & Co. was in violation of FINRA's net capital rule and that MS & Co. was required to "cease conducting a securities business." MS & Co. ceased operations in December 2009. SEC Statement of Material Facts at 1 (Docket No. 711). On April 4, 2010, FINRA suspended MS & Co.'s membership. *Id.*

**B. Preferential Payment to Levy**

The Receiver has recovered evidence in the books and records of MS & Co. showing that on January 27, 2010, funds in the amount of \$90,000 were wired into an account at M&T Bank in the name of TDM Cable Funding LLC Trust 06 ("Account") by an MS & Co. investor ("Investor B") with the intent of purchasing \$100,000 worth of TDM Cable Trust 06 certificates. Brown Dec'l. ¶ 9. A redacted copy of the January 2010 statement for the Account ("Account Statement") is attached to the Brown Dec'l. as Exhibit D. A redacted copy of Investor B's direction to purchase TDM Cable Trust 06 certificates with the \$90,000 is attached to the Brown Dec'l. as Exhibit E.

The transaction was conducted by broker-dealer, Phillip Rabinovich (“Rabinovich”).<sup>3</sup> Brown Dec’l. ¶ 10. In the administrative proceeding commenced by the SEC against Rabinovich and other brokers, Levy submitted an Affidavit in support of Rabinovich (“Affidavit”), attached to the Brown Dec’l. as Exhibit F. Levy’s Affidavit stated that she had known Rabinovich for over 25 years and had been a client of Rabinovich for approximately 15 years. Affidavit ¶ 2. In the Affidavit, Levy stated that “[b]ased on our relationship and the 25 years I have known him, I find the very notion that he should be held responsible for the loss I suffered absolutely absurd.” *Id.* ¶ 5. Levy went on to attest that, “[i]n my estimation, Mr. Rabinovich continues to retain a stellar reputation among his clients . . . .” *Id.* ¶ 6.

Because FINRA had required MS & Co. to cease conducting a securities business in December 2009, Rabinovich made the trade through another brokerage firm, Dinosaur Securities LLC. Brown Dec’l. ¶ 11. Although Investor B’s wire payment was deposited into the Account, there was no investment in TDM Cable Trust 06 recorded in Investor B’s name in the books and records of MS & Co. *Id.* Notwithstanding that an investment was not recorded on MS & Co.’s books and records in Investor B’s name, the Receiver intends to grant Investor B a claim in the amount of \$90,000 to account for Investor B’s transfer of funds into the Account (“Investor B Claim”).

The Account Statement further shows that, on January 28, 2010, the \$90,000 wired into the Account by Investor B was wired out of the Account to National Financial Services (“NFS”). Brown Dec’l. ¶ 12. The Receiver has recovered a wire transfer

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<sup>3</sup> On December 21, 2018, the SEC entered an Order Making Findings and Imposing Remedial Sanctions, finding that Rabinovich, among other broker-dealers, violated section 17(a)(2) and (a)(3) of the Securities Act of 1933 by selling MS & Co. investments. On March 6, 2019, the Court entered a Summary Order disallowing Rabinovich’s claims, along with those of certain other brokers, based on Rabinovich’s misconduct in negligently selling MS & Co. investments. *See* Summary Order (Docket No. 1043).

confirmation showing that the funds were wired from the Account to NFS for the benefit of Levy (“Preferential Payment”) as a redemption of Levy’s investment in TDM Cable Trust 06 9.25% 48 Months Contract Certificates in the principal amount of \$100,000. *See* Exhibit G to Brown Dec’l. Although MS & Co. was not supposed to be operating as a securities business as of December 18, 2009, the Preferential Payment was authorized by either McGinn or Smith. *Id.*

All of Levy’s claims (collectively, “Levy Claims”) were, in the Receiver’s original claims reconciliation process, adjusted for pre-Receivership distributions of principal and interest like all other investor claims, as shown on the Receiver’s Claims Website (defined below). It was only thereafter when Investor B asserted their \$90,000 TDM Cable Trust 06 9.25% claim that the Receiver and his staff discovered the preferred Levy redemption. As a result, the Levy Claims have not been adjusted to account for the Preferential Payment. Brown Dec’l. ¶ 13. In connection with the distribution process, as described in greater detail in paragraph D below, Levy completed and signed the Questionnaire (as defined below) asserting her right to recover on a claim for which she had already been paid. A redacted copy of Levy’s completed and executed Questionnaire is attached to the Brown Dec’l. as Exhibit H. Levy failed to report her receipt of the Preferential Payment on her Questionnaire. *See* Exhibit H to Brown Dec’l, at 2.

**C. Claims Procedure**

On March 9, 2012, the Receiver filed a Motion (“Claims Procedure Motion”) (Docket No. 466) for entry of an Order approving, among other things, the Receiver’s proposed procedure for the administration of claims against the MS Entities.

On March 27, 2012, the Court entered an Order granting the Claims Procedure Motion (Docket No. 475), which was subsequently amended by an Order dated April 17, 2012 (“Claims Procedure Order”) (Docket No. 481). Each investor and known creditor of the MS Entities was mailed on May 1, 2012 an Access Notice describing the claims process and enclosing (i) Notice of the Claims Bar Date and Claims Procedure and (ii) a Claim Form. Brown Dec’1. ¶15. A confidential password providing access to the Receiver’s Claims Website at [www.mcginnsmithreceiver.com](http://www.mcginnsmithreceiver.com) (“Claims Website”) was also provided. *Id.* If an investor or creditor agreed with the description and amount of their claim(s) as listed on the Claims Website and the claim(s) were not listed as disputed, contingent or unliquidated, the investor or creditor did not need to take any further action. *Id.* All other investors and creditors needed to timely file a paper claim before the bar date of June 19, 2012, as further described in detail on the Claim’s Website. *Id.*

The Claims Procedure Order established June 19, 2012 (“Bar Date”) as deadline for creditors and investors to file claims against the MS Entities. Brown Dec’1. ¶16.

In accordance with the Claims Procedure Order, nearly six hundred creditors and investors timely filed paper claims prior to the Bar Date. Brown Dec’1. ¶17. In addition, more than 3,127 claims of investors and creditors were included on the schedules posted by the Receiver on the Claims Website in accordance with the Claims Procedure Order. *Id.*

The Receiver conducted an initial review of the paper claims timely filed by creditors and investors in accordance with the Claims Procedure Order and determined it was necessary to establish a reserve as to investor claims totaling approximately \$23,617,190

since those claims have been listed by the Receiver as disputed, contingent or unliquidated. Brown Dec'1. ¶18.

**D. Plan of Distribution Process**

On December 30, 2015, the Receiver filed a Motion (Docket No. 847) (“Plan Distribution Motion”) to seek approval of (i) a plan of distribution of assets of the MS Entities to investors (“Plan of Distribution”); and (ii) interim distributions to investors with allowed claims scheduled or timely filed in accordance with the Claim Procedure Order. On October 31, 2016, the Court entered a Memorandum-Decision and Order (Docket No. 904) (“Plan Distribution Order”) granting the Plan Distribution Motion, overruling objections, approving the Plan of Distribution, and allowing the Receiver to make interim distributions as set forth in the Plan Distribution Motion.

Among other things, the Plan of Distribution provides for a reserve for disputed claims to allow the Receiver to make initial distributions, but to also provide for funds to be reserved until any objections to disputed claims can be heard and decided by final order of the Court. As of April 15, 2019, \$6,578,150 has been distributed to investors with allowed claims as a First Distribution. Brown Dec'1. ¶21. The Receiver estimates that 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).

In accordance with the Plan of Distribution, in February 2017, the Receiver distributed questionnaires to all of the investors (“Questionnaires”), which, among other things, required investors to report under penalty of perjury whether they received, or were pursuing a recovery from, any other source related to MS & Co. Brown Dec'1. ¶22. The

Questionnaires also included a description of the investors' investment and the amount of their claim pursuant to the books and records of MS & Co. *Id.* Although Levy's claim amount as set forth on the Questionnaire did not reflect the receipt of the Preferential Payment, Levy certified under penalty of perjury that she did not receive any payment related to her TDM Cable Trust 06 investment. *Id.*; *see also* Exhibit H to Brown Dec'l.

The Plan of Distribution provides that all investor claims would be calculated by using the "Net Investment" methodology, i.e., the claim amount is equal to the amount of the initial investment made less any distributions received prior to the appointment of the Receiver, including any distributions of principal or interest. Plan of Distribution, Art. IV. The Plan of Distribution further provides for a collateral recovery offset ("Collateral Recovery Offset"), where distributions made on account of investor claims will be reduced on a dollar-for-dollar basis to the extent the investor has received a recovery from a source other than the Receivership in connection with their claimed loss. *Id.* Art. II.

#### **E. Claims Motions**

On September 21, 2017, the Receiver filed a Motion (Docket No. 937) ("First Claims Motion") to seek disallowance of certain filed paper claims that were duplicative of the corresponding claims granted by the Receiver. On November 9, 2017, the Receiver filed a Statement (Docket No. 957) in furtherance of the First Claims Motion, adjourning the First Claims Motion with respect to those duplicative investor paper claims filed by investors whose Receiver-granted claims have been disputed by the Receiver. On December 28, 2017, the Court entered an Order granting the First Claims Motion and disallowing the duplicative paper claims other than with respect to those filed by investors with disputed claims (Docket No. 966).

On February 15, 2018, the Receiver filed a Motion (Docket No. 974) (“Second Claims Motion”) to seek disallowance of certain filed paper claims for which there is no basis for payment in the books and records of MS & Co. On April 13, 2018, the Court entered an Order granting the Second Claims Motion and disallowing the paper claims.

On March 19, 2018, the Receiver filed a Motion (Docket No. 984) (“Third Claims Motion”) to seek disallowance of certain claims of former MS & Co. brokers. On May 4, 2018, the Receiver filed a Reply (Docket No. 1002) to the Response of Frank Chiappone (Docket No. 995) to the Third Claims Motion. On March 6, 2019, the Court entered an Order granting the Third Claims Motion and disallowing the brokers’ claims.

On July 6, 2018, the Receiver filed a Motion (Docket No. 1009) (“Fourth Claims Motion”) to seek disallowance of paper claims filed by certain preferred investors and to apply a preferential payment offset to the distributions to be made to the preferred investors. On August 27, 2018, the Receiver filed a Reply (Docket No. 1020) (“Reply”) to the Opposition filed by certain preferred investors (Docket No. 1019) to the Fourth Claims Motion.

On October 16, 2018, the Receiver filed a Motion (Docket No. 1025) (“Fifth Claims Motion”) to seek to apply a preferential payment offset to the distributions to be made to preferred investors One City Center Associates and Burton Fisher.

On March 6, 2019, the Court entered an Order granting the Fourth Claims Motion and the Fifth Claims Motion, disallowing the preferred investors’ paper claims and applying the preferential payment offset (Docket No. 1042) (“Preferential Offset Order”).



## ARGUMENT

### **A. Rising Tide Accounting Methodology Should be Applied to Promote Equality Among Investors**

The district court has broad power and discretion to determine relief in an equity receivership. *See S.E.C. v. Elliott*, 953 F.2d 1560, 1566 (11th Cir. 1992); *S.E.C. v. Basic Energy & Affiliated Res., Inc.*, 273 F.3d 657, 668 (6th Cir. 2001). “In equity receiverships resulting from SEC enforcement actions, district courts have very broad powers and wide discretion to fashion remedies and determine to whom and how the assets of the Receivership Estate will be distributed.” *S.E.C. v. Detroit Mem’l Partners, LLC*, No. 1:13-cv-1817-WSD, 2016 WL 6595942 at \*5 (N.D. Ga. Nov. 8, 2016) (internal quotation omitted). A receiver’s choice among allocation schemes in the course of administering a receivership is within the discretion of the district court to approve or disapprove. *S.E.C. v. Huber*, 702 F.3d 903, 908 (7th Cir. 2012).

The Rising Tide method is a common methodology used for determining the distribution of assets in a Receivership. In the Preferential Offset Order, the Court approved the application of an offset calculated using the Rising Tide methodology to reduce the distributions made by the Receiver to certain investors who received preferential interest payments and supplemental payments in the Preferential Offset Order. *See* Preferential Offset Order at 6-7. The Court has also approved the use of the Rising Tide methodology in the calculation of the Collateral Recovery Offset. *See* Plan Distribution Order at 12-13.

The Rising Tide method subtracts pre-receivership payments received by an investor from the investor’s pro rata distribution, reducing that investor’s pro rata distribution on a dollar-for-dollar basis. *U.S. Commodity Futures Trading Comm’n v. Lake Shore Asset Mgmt. Ltd.*, No. 07 C 3598, 2010 WL 960362 at \*7 (N.D. Ill. Mar. 15, 2010).

The Rising Tide methodology “brings the recovery of claimants who received no payments during the course of the Ponzi Scheme equal to those claimants who did receive payments during the course of the Ponzi Scheme.” *In re Receiver*, No. 3:10-3141-MBS, 2011 WL 2601849 at \*2 (D.S.C. July 1, 2011). Otherwise, a straight pro rata distribution of funds, irrespective of pre-receivership payments, “would be inequitable because it would unfairly elevate investors who received those pre-receivership payments.” *Lake Shore*, No. 07 C 3598, 2010 WL 960362 at \*9.

Courts have not approved the use of the Rising Tide methodology where a significant amount of investors would not recover any distribution as a result of applying that methodology. *S.E.C. v. Huber*, 702 F.3d 903, 907 (7th Cir. 2012) (approving Rising Tide where only 18% of investors would receive no recovery); *U.S. Commodity Futures Trading Comm’n v. Barki, LLC*, No. 3:09 CV 106-MU, 2009 WL 3839389 (W.D.N.C. Nov. 12, 2009) (refusing to approve Rising Tide where 55% of investors would receive no recovery); *see also S.E.C. v. Byers*, 637 F. Supp. 2d 166, 182 (S.D.N.Y. 2009) (approving the Net Investment methodology after receiver did not recommend using Rising Tide because 45% of investors would not receive a recovery). In this Receivership, the Receiver is making distributions to all investors with allowed claims. *See* Third Written Status Report of the Receiver, at 6 (Docket No. 925).

**B. Levy’s Distributions Should be Adjusted Using the Rising Tide Methodology**

Distributions made on account of all of the Levy Claims should be adjusted to account for Levy’s receipt of the Preferential Payment using the Rising Tide methodology (“Preferential Payment Offset”). In January 2010, after investors had stopped receiving payments from MS & Co. on account of their investments, Levy received a significant

\$90,000 payment on her principal investment in TDM Cable Trust 06. Levy was, thus, elevated to a preferred position by MS & Co. over the other similarly situated investors.

Although the Preferential Payment was received in connection with Levy's TDM Cable Trust 06 investment, the Preferential Payment Offset should be applied to all of the Levy Claims, as set forth on Exhibit A to the Motion. The Preferential Payment was material redemption of an investment at a time when other investors in TDM Cable Trust 06 and other MS & Co. entities had ceased receiving any payments from MS & Co. In order to return Levy back to the position she would have been in without the Preferential Payment, the Preferential Payment Offset should be applied to all Levy Claims. In this way, the Preferential Payment Offset will act like the Collateral Recovery Offset, reducing the aggregate amounts to be distributed to Levy by the amount of the Preferential Payment on a dollar-for-dollar basis and promoting the equitable treatment of all investors. Indeed, had Levy disclosed the Preferential Payment on the Questionnaire, the Preferential Payment would likely have been treated as a Collateral Recovery.

Had the Receiver not discovered Levy's failure to disclose the Preferential Payment on the Questionnaire, Levy would have received Receivership distributions from the Receivership for her TDM Cable Trust 06 investment *in addition to* the \$90,000 Preferential Payment she had already received. By application of the Preferential Payment Offset, Levy will not receive distributions in excess of what she would have received had she not received the Preferential Payment or had she disclosed the receipt of the Preferential Payment on the Questionnaire.

The Net Investment method was applied to all investor claims, including the Levy Claims, to account for pre-receivership payments of principal and/or interest made to

all investors, as approved by the Plan Distribution Order. *See* Plan Distribution Order at 15. Unlike the rest of the investors, however, Levy received the Preferential Payment in January 2010, after MS & Co. had ceased operations and while ordinary investors ceased receiving anything on account of their MS & Co. investments, including TDM Cable Trust 06. The Preferential Payment thus reduced amounts available for distribution to all investors defrauded by McGinn and Smith and unfairly increased total recoveries of Levy.

Although courts have not approved the use of the Rising Tide methodology where a large percentage of investors would not receive a recovery as a result of the application of Rising Tide, this is not the case here. After application of the Preferential Payment Offset, Levy will not receive an interim first distribution and will have a credit against future distributions in the amount of the excess of the Preferential Payment over the amount of the interim first distribution. Levy, however, represents less than 1% of all MS & Co. investors.

To permit Levy to retain the Preferential Payment, without a corresponding dollar-for-dollar reduction in the amount of her pro rata distribution, would result in the Levy retaining excess amounts for no reason other than that Levy was arbitrarily selected to receive a material redemption while other MS & Co. investors had stopped receiving any payments in connection with their investments. The Preferential Payment Offset promotes equality among all investors by accounting for the arbitrary treatment of Levy and will increase the pool of proceeds available for pro rata distribution to *all* investors.

**C. The Balance of Levy's Claims Should be Equitably Subordinated to the Investor B Claim**

To the extent that Levy is entitled to receive any future distributions in excess of the Preferential Payment Offset, such claims should be equitably subordinated to the Investor B Claim due to Levy's misconduct which resulted in harm to Investor B.

A district court also has "the authority to subordinate the claims of certain investors to ensure equal treatment." *S.E.C. v. Wealth Mgmt. LLC*, 628 F.3d 323, 333 (7th Cir. 2010). While equitable subordination is a concept that derives from bankruptcy case law, the district court has "the equitable power to subordinate one claim to another if it finds that the creditor's claim, while not lacking a lawful basis nonetheless results from inequitable behavior on the part of that creditor." *S.E.C. v. Am. Bd. of Trade*, 719 F.Supp. 186, 196 (S.D.N.Y. 1986) (internal quotation omitted). To equitably subordinate a claim, (1) the claimant must have engaged in some type of inequitable conduct and (2) the misconduct must have caused injury to the other creditors. *S.E.C. v. Spongetech Delivery Sys., Inc.*, 98 F. Supp. 3d 530, 551 (E.D.N.Y. 2014). "Inequitable conduct" may include "conduct that may be lawful but is nevertheless contrary to equity and good conscience. It includes a secret or open fraud . . . ." *Id.* at 553. Equitable subordination is a remedial remedy and "should be applied only to the extent necessary to offset specific harm suffered by creditors on account of the inequitable conduct." *See In re SubMicron Sys. Corp.*, 432 F.3d 448, 462 (3d Cir. 2006) (internal quotation omitted).

Levy has acted inequitably resulting in harm to creditors, specifically to Investor B. Levy accepted a material partial redemption of ninety percent of her investment at a time that Levy should have known that MS & Co. should not have been making any redemptions, due to (a) the problems arising in connection with the Four Funds, which

Levy would have been aware of as an investor in the Four Funds, (b) the fact that payments to investors in connection with the Trust Offerings had ceased by November 2009, and (c) the fact that FINRA had demanded that MS & Co. cease operations. By accepting the Preferential Payment, Levy caused direct economic harm to Investor B, whose funds were used to make a material redemption of Levy's investments instead of being invested. As a result, Investor B now stands to recover from the Receivership, at most, a recovery ranging between 13.5% to 21.7% of the funds wired into the Account, funds which Investor B believed were being invested but instead were being used to redeem Levy. Accordingly, the Levy Claims should be equitably subordinated to the Investor B Claim unless and until such time as Investor B receives payment in full of the Investor B Claim.

**D. Summary Proceedings are Appropriate**

The Receiver has sought to provide Levy with appropriate notice and sufficient time to respond to the Motion. Accordingly, the Receiver has complied with the claim objection and notice procedures set forth in the Federal Rules of Bankruptcy Procedure ("Bankruptcy Rules") as a form of best expression of law. Bankruptcy Rule 3007 requires that a claim objection must be filed and served at least thirty days before any scheduled hearing and that the objection must be served on the claimant by first class mail. Fed. R. Bankr. P. 3007(a)(1), (2).

In accordance with Rule 7.1 of the Local Rules of Practice for the United States District Court for the Northern District of New York, the Receiver has filed and will serve the Motion on Levy at least thirty-one days in advance of the scheduled return date of June 20, 2019. The Receiver will give notice of the Motion to the Securities and Exchange Commission, all parties who have filed a Notice of Appearance in this action by ECF, and

all creditors and parties in interest via the Receiver's website (www.mcginnsmithreceiver.com), as well as posting at the top of the Receiver's website an explanation of the Motion. Additionally, notice by first class mail will be given to Levy. Brown Dec'l. ¶30.

The Receiver requests that the Court enter an order granting the relief requested in this Motion without a hearing with respect to those claims for which an objection is not timely interposed. Disallowance or adjustment of a claim without a hearing where there is no factual dispute is an appropriate and preferred procedure in federal receivership cases. *See S.E.C. v. Elliott*, 953 F.2d 1560, 1566 (11th Cir. 1992) (holding that summary proceedings are favored in federal receivership cases because a summary proceeding "reduces the time necessary to settle disputes, decreases litigation costs, and prevents further dissipation of receivership assets"); *United States v. Fairway Capital Corp.*, 433 F. Supp. 2d 226, 241 (D. R.I. 2006) ("Receivership courts can employ summary procedures in allowing, disallowing and subordinating claims of creditors").

**CONCLUSION**

The Receiver requests that the Court enter an Order substantially in the form attached to the Motion as Exhibit C (a) applying the Preferential Payment Offset to the Levy Claims and (b) equitably subordinating the balance of the Levy Claims to the Investor B Claim, together with such other and further relief as the Court deems just and proper.

Dated: April 25, 2019

PHILLIPS LYTTLE LLP

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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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**CERTIFICATE OF SERVICE**

I, Karen M. Ludlow, being at all times over 18 years of age, hereby certify that on April 25, 2019, a true and correct copy of the (i) Notice of Motion and Sixth Claims Motion of William J. Brown, as Receiver, for an Order (A) Applying Preferential Payment Offset to Lesley Levy Claims and (B) Equitably Subordinating Lesley Levy Claims (“Sixth Claims Motion”), (ii) Declaration of William J. Brown, as Receiver, in Support of Sixth Claims Motion, and (iii) Memorandum of Law in Support of Sixth Claims Motion (collectively, “Sixth Claims Motion Documents”) were 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:

- **William J. Brown** wbrown@phillipslytle.com,khatch@phillipslytle.com
- **Roland M. Cavalier** rcavalier@tcglegal.com
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And, I hereby certify that on April 25, 2019, I mailed, via first class mail using the United States Postal Service, copies of the Sixth Claims Motion Documents to the individuals listed below:

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/s/ Karen M. Ludlow  
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