

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION

Plaintiff,

vs.

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,
LYNN A. SMITH, DAVID M. WOJESKI, Trustee
of the David L. and Lynn A. Smith Irrevocable Trust
U/A 8/04/04, GEOFFREY R. SMITH, LAUREN
T. SMITH, and NANCY McGINN,

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

Defendants,

LYNN A. SMITH and NANCY McGINN,

Relief Defendants, and

DAVID M. WOJESKI, Trustee of the David L.
and Lynn a. Smith Irrevocable Trust U/A 8/04/04,

Intervenor.

**RELIEF DEFENDANT/DEFENDANT'S CROSS-MOTION SEEKING
ATTORNEYS FEES AND LIVING EXPENSES AND OPPOSITION TO
PLAINTIFF'S MOTION TO AMEND PRELIMINARY INJUNCTION ORDER**

Relief Defendant/Defendant Lynn Smith ("Mrs. Smith" or "Movant") respectfully cross-moves this Court to grant limited relief from the July 7, 2010 Order by releasing assets to pay living expenses and professional fees.

Mrs. Smith respectfully requests that the Court release \$16,431 per month from her assets the Government has frozen for her continued well-being. Given the on-going demands of defending this action, Movant respectfully requests that the Court approve the release of funds to allow for the payment of legal expenses as set forth in the declaration of Counsel in Exhibit A attached with this Cross-Motion. Next, Movant respectfully requests the release of \$13,466 for necessary expenses associated with her Florida residence. Finally, Movant respectfully requests that the Court enter an Order authorizing the sale of her Florida home, the proceeds of which will be placed in escrow pending the conclusion of these proceedings. In support of its Cross-Motion, Movant has filed a memorandum of law.

As it relates to Lynn Smith's opposition to plaintiff's motion to amend the Court's Preliminary Injunction Order, Plaintiff's request to restrict Lynn Smith's use of her personal credit cards should be rejected based on her capacity as a Relief Defendant and as a Defendant whose only alleged culpability arises from an unenforceable New York State statute.

Dated: October 4, 2010

Featherstonhaugh, Wiley & Clyne, LLP

By: 

James D. Featherstonhaugh, Esq.

Bar Roll No. 101616

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Intervenor.

MEMORANDUM OF LAW IN SUPPORT OF RELIEF
DEFENDANT/DEFENDANT'S CROSS-MOTION SEEKING ATTORNEYS FEES
AND LIVING EXPENSES AND IN OPPOSITION TO PLAINTIFF'S MOTION
TO AMEND THE PRELIMINARY INJUNCTION ORDER

The Preliminary Injunction blocks Movant's access to her assets, with substantial implications for her day-to-day living activities and well being during the pendency of this proceeding. Mrs. Smith has finite resources at her disposal and does not have any

meaningful source of income aside from the assets in her personal accounts that are subject to the freeze, and the Preliminary Injunction makes no provision for (1) Mrs. Smith to pay professional fees for her defense and representation in this matter; or (2) living expenses for day-to-day living activities.

To date, Mrs. Smith has provided a complete accounting – with a list of accounts, a statement of net assets, and detailed brokerage statements dating from 1999 to 2010 – to the Securities and Exchange Commission (“SEC” or “Commission”) in order to document the location and amount of all her personal assets and to demonstrate that those assets have been frozen in accordance with this Court’s TRO and subsequent July 7, 2010 Preliminary Injunction. As these records demonstrate, Mrs. Smith’s assets have been frozen – assets that are necessary for her to survive on a day to day basis and defend herself throughout the course of these proceedings. It is both inequitable and offensive to fundamental constitutional principals to: (1) deprive Mrs. Smith of necessary living expenses; and (2) deprive Mrs. Smith of the ability to fund her defense during the pendency of these proceedings.

Accordingly, Movant respectfully asks that the Court: (1) release \$16,431 per month for living expenses as set forth in Exhibit C; (2) approve the release of \$138,451.49 for attorneys’ fees and disbursements as set forth in Exhibit A, and such additional funds as referenced in Exhibit B for near-term anticipated legal expenses; (3) release \$13,466 for necessary expenses associated with the Florida residence as set forth in Exhibit D; and (4) enter an Order authorizing the sale of the Florida home, the proceeds of which will be placed in escrow pending the conclusion of this proceeding.

FACTUAL BACKGROUND

On April 20, 2010, the Court entered an Order to Show Cause, Temporary Restraining Order, and Order Freezing Assets and Granting Other Relief that, among other things, froze Mrs. Smith's personal assets. In its July 7, 2010 Order, this Court vacated the asset freeze concerning her camp on the Great Sacandaga Lake and preserved the freeze on all remaining personal assets belonging to Mrs. Smith, including the stock account she inherited over 40 years ago from her father. Pursuant to the terms of the July 7, 2010 Order, David Wojeski as Trustee for the David and Lynn A. Smith Irrevocable Trust and Mrs. Smith, in an arms length transaction, entered into a standard form purchase and sale contract with the Trust for the sale, at fair market value, of her real estate located on the Great Sacandaga Lake. Given the expansive nature of the SEC's action, all but \$96,700 of the funds Mrs. Smith received as a result of the sale of her camp have been expended on securing and making partial payments for professional services for both herself and her husband and for living expenses for herself and, in light of the broad nature of the freeze, for her family.

LEGAL ARGUMENT IN SUPPORT OF CROSS-MOTION

An asset freeze is a burdensome form of ancillary relief and the decision of whether to freeze a defendant's assets in a Securities and Exchange Commission enforcement action requires particularly careful consideration by the District Court. SEC v. Manor Nursing Centers, Inc., 458 F.2d 1082, 1105 (2nd Cir. 1972). Whether a defendant has other sources of income from which to pay living expenses or attorney fees is a factor in determining whether frozen assets should be released to pay these costs. United States SEC v. Petters, 2009 U.S. Dist LEXIS 98015 (D. Minn. 2009). Given that

the Court has the authority to freeze personal assets temporarily, it also has the “corollary authority to release frozen personal assets, or lower the frozen amount.” SEC v. Dowdell, 175 F. Supp 2d 850, 854 (W.D. Va. 2001), citing, SEC v. Gonzalez de Castilla, 170 F. Supp 2d 4427, 429 (S.D.N.Y. 2001). Accordingly, an asset freeze order should be narrowly tailored. Id. It should not prohibit a defendant from either supporting themselves up to and through trial or mounting a defense. See United States v. Noriega, 746 F. Supp 1541, 1545-46 (S.D. Fla. 1990). A district court may exercise its discretion to release frozen funds to pay living expenses or attorney fees, even in instances where the profit from the alleged wrongdoing exceeds the amount of the frozen funds. See Dowdell, 175 F. Supp 2d at 854; CFTC v. Noble Metals Int’l, 67 F.3d 766 (9th Cir. 1995).

Here, it is clear that Mrs. Smith has insufficient sources of income to pay living expenses and attorney fees during the pendency of these proceedings. Mrs. Smith’s assets have been frozen since April 20, 2010 and as a homemaker who independently holds title to a substantial amount of the assets in question and receives limited monthly payments from the Social Security Administration and the New York State Teachers Retirement System that are inadequate to pay necessary living expenses and attorney fees, she has no other sufficient sources of income other than those personal assets subject to the freeze order.

1. Mrs. Smith is Entitled to Reasonable Professional Fees.

Movant’s attorneys respectfully request reimbursement of attorneys’ fees and expenses from April 21, 2010 to September 30, 2010. These fees and expenses are significant and have been necessary given the amount of work needed in these

proceedings and related matters. The failure to consider these expenses in the Preliminary Injunction raises serious concerns of fundamental fairness.

To begin with, funds from Movant's personal accounts should be released to the extent that Mrs. Smith is able to reimburse her professionals for time and expenses spent defending this matter. The work performed primarily falls into three categories: (i) the civil case; (ii) compliance with the SEC's investigatory requests and this Court's Preliminary Injunction; and (iii) preparation for trial. Indeed, fundamental fairness dictates such a result. The hours spent by Movant's counsel are reasonable, particularly given the circumstances.

Where, as here, Movant's counsel has performed substantial work in the matter and the defendant challenges the Securities and Exchange Commission's allegations against her, courts have limited or modified asset freeze orders to permit the defendant to pay attorney's fees. See, e.g. SEC v. Gonzalez de Castilla, 170 F. Supp 2d 427 (S.D.N.Y.) (modifying asset freeze order to permit the payment of legal fees because no clear showing of wrongdoing had been necessary to sustain the preliminary injunction and asset freeze for violating the securities laws).

The central concern in this matter is the fairness of the proceedings. It is difficult to believe that the Court could achieve a fair result were it to deny Movant the ability to retain counsel. This is a complex legal matter, and lawyers are essential to the presentation of issues related to it. Not only is it fundamentally fair to afford Mrs. Smith reasonable funds to mount a defense, but her right to counsel of choice is an essential component of the Sixth Amendment – triggered here because of the parallel Department of Justice investigation.

Due process precludes the Securities and Exchange Commission from unilaterally denying Mrs. Smith the ability to defend herself in this action. To hinder such a fundamental interest here would work a permanent deprivation on Mrs. Smith, who certainly “needs the attorney *now* if the attorney is to do [her] any good.” United States v. Moya-Gomez, 860 F.2d 706, 726 (7th Cir. 1988)(emphasis in original).

Fairness and constitutional principals dictate that this Court should provide Mrs. Smith with access to her funds to pay her professionals’ fees while she is defending herself against these proceedings. Accordingly, Movant requests that the Court approve her request for attorneys fees submitted with this Cross-Motion and Memorandum. The Declaration of Movant’s attorney set forth in Exhibit A details to the Court: (i) the hours worked by Mrs. Smith’s attorneys; (ii) the disbursements and expenses charged; and (iii) the amount of unpaid fees, disbursements and expenses to date.

2. Mrs. Smith is Entitled to Reasonable Living Expenses

Mrs. Smith has no meaningful source of income other than that derived from the assets frozen by the Preliminary Injunction to sustain her throughout the pendency of these proceedings. Mrs. Smith presently receives \$133.01 per month from the Teachers Retirement System and \$790 per month from the Social Security Administration. As demonstrated in the attached Declarations and Exhibits, these funds and the remaining funds from the sale of her camp are insufficient to sustain Mrs. Smith during the pendency of these proceedings. The Preliminary Injunction makes no allowance for Mrs. Smith to purchase groceries, to purchase medical insurance, or even pay for basic housekeeping supplies and personal care. This certainly is not the kind of “narrowly tailored” asset freeze that the law favors.

Not only is the asset freeze overly broad, but the Securities and Exchange Commission has never indicated that it will negotiate narrowing the freeze to provide for living expenses for Mrs. Smith. Mrs. Smith has no meaningful source to pay for living expenses outside of her frozen assets during the pendency of these proceedings. (See Exhibit B, Declaration of Lynn A. Smith). Further, as described above, the Securities and Exchange Commission has not made any provisions for attorney's fees. Thus, the Securities and Exchange Commission is denying basic living expenses to Mrs. Smith. Such a result is patently unfair.

Ultimately, the limited, theoretical risk that assets might be dissipated must be weighed against the salient, detrimental effects of the wholesale freeze sought by the SEC. Courts have continuously acknowledged "the basic principle that burdensome forms of interim relief require correspondingly substantial justification." SEC v. Unifund SAL, 910 F.2d 1028, 1042 (2nd Cir. 1990). An order that prevents a defendant from supporting herself would likely work an injustice with constitutional implications. United States v. Jones, 160 F.3d 641, 646 (10th Cir. 1998). The asset freeze currently in place upon the personal assets of Lynn Smith is an enormous and devastating burden. Accordingly, Mrs. Smith should be entitled to make use of sufficient assets to provide for herself while she vindicates herself from the charges asserted against her.

**LEGAL ARGUMENT IN OPPOSITION TO THE SEC'S
MOTION TO AMEND THE PRELIMINARY INJUNCTION ORDER**

Mrs. Smith joins in the Defendants' David L. Smith and Timothy M. McGinn's October 4, 2010 Motion in Opposition to the Plaintiff's Motion to Amend the Preliminary Injunction Order to the extent that those arguments support Mrs. Smith's unfettered right to use her credit cards during the pendency of this proceeding. In addition to those

arguments, Mrs. Smith opposes the Motion in both her capacity as a Relief Defendant and as a Defendant who is not alleged to have violated any federal securities laws but rather a state statute that does not provide for the relief plaintiff now seeks to impose against Mrs. Smith.

As a non-culpable party to the action, only those assets that have been deemed “ill-gotten” can be the subject of any freeze order against her for the purposes of disgorgement. Mrs. Smith has not been alleged to have violated any federal securities laws. She has not invoked the protections of the Fifth Amendment nor can the SEC assume any inferences or presumptions against her. To the extent the use of a credit card can be even considered an asset that could be the subject of any freeze or restrictions pursuant to the existing Order, there is no basis in law to prevent her with the unfettered use of personal credit cards since disgorgement is the only equitable remedy available to the SEC as it relates to a relief defendant.

The SEC has also sought to include Mrs. Smith as part of this Motion based on the allegations in its Amended Complaint that she is alleged to have fraudulently conveyed an asset pursuant to the New York State Debtor and Creditor Law. Apart from the fact that it is doubtful this Court has supplemental jurisdiction over the state claim or that the SEC can somehow be deemed a “creditor” under the law or that the SEC has the statutory authority to assert a state law claim, the section of New York State law in which they seek relief does not provide creditors with the ability to restrict an alleged defendant from encumbering his or her assets except for the asset that is the subject of the alleged fraudulent conveyance. The SEC’s only remedy under §278 of the Debtor and Creditor Law is to either attach or levy on the property alleged to have been fraudulently conveyed

pursuant to the New York Civil Practice Law and Rules. Save Way Oil Co. v. 284 Eastern Parkway Corp. et al., 453 N.Y.S.2d 554 (Civil Ct. Kings County 1982). The SEC's attempt to boot strap alleged liability under this statute as a means to restrict Mrs. Smith's credit card use, which is completely unrelated to the conveyance upon which the SEC claims was fraudulent, is simply preposterous.

Accordingly, to the extent this Court deems that the future use of credit cards by the named defendants should be restricted, such Order should not extend to Mrs. Smith.

CONCLUSION

For the reasons set forth above, it is respectfully requested that this Court should grant Movant's Cross-Motion for limited relief from the Preliminary Injunction and award the Movant's reasonable attorneys' fees and living expenses.

Dated: October 4, 2010

Featherstonhaugh, Wiley & Clyne, LLP

By: 

James D. Featherstonhaugh, Esq.

Bar Roll No. 101616

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Exhibit A

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION

Plaintiff,

vs.

McGINN, SMITH & CO., INC.,
McGINN, SMITH ADVISORS, LLC,
McGINN, SMITH CAPITAL HOLDINGS CORP.,
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TIMOTHY M. McGINN, AND DAVID L. SMITH,
LYNN A. SMITH, DAVID M. WOJESKI, Trustee
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U/A 8/04/04, GEOFFREY R. SMITH, LAUREN
T. SMITH, and NANCY McGINN,

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

DECLARATION OF
JAMES D.
FEATHERSTONHAUGH
IN SUPPORT OF
RELIEF DEFENDANT/
DEFENDANT'S MOTION
FOR ATTORNEYS FEES
AND LIVING EXPENSES

Defendants,

LYNN A. SMITH and NANCY McGINN,

Relief Defendants, and

DAVID M. WOJESKI, Trustee of the David L.
and Lynn a. Smith Irrevocable Trust U/A 8/04/04,

Intervenor.

I, JAMES D. FEATHERSTONHAUGH, pursuant to 28 USC §1746, declare under penalty of perjury, the following facts:

1. I am an attorney duly admitted to practice before this Court and represent Lynn A. Smith in the instant proceeding. I make this declaration in support of Relief Defendant/Defendant's Motion seeking Attorneys' Fees and Living Expenses in this proceeding.

2. On April 29, 2010, I entered a Notice of Appearance as counsel of record for Lynn Smith.

3. As of September 30, 2010, the firm of Featherstonhaugh, Wiley & Clyne has performed 906.50 hours of legal representation on behalf of Mrs. Smith at a cost of \$227,205.00.

4. As of September 30, 2010, the firm of Featherstonhaugh, Wiley & Clyne has advanced disbursements and made expenses of \$26,246.49 associated with the Firm's legal representation of Mrs. Smith.

5. As of September 30, 2010, the total current work, disbursements and expenses for Featherstonhaugh, Wiley & Clyne totaled \$253,451.49 of which Ms Smith has paid \$115,000.

6. As of September 30, 2010, Mrs. Smith owes the firm of Featherstonhaugh, Wiley & Clyne \$138,451.49 for legal representation, disbursements and expenses associated with the Firm's representation of Mrs. Smith in these proceedings.

DATED: October 4, 2010

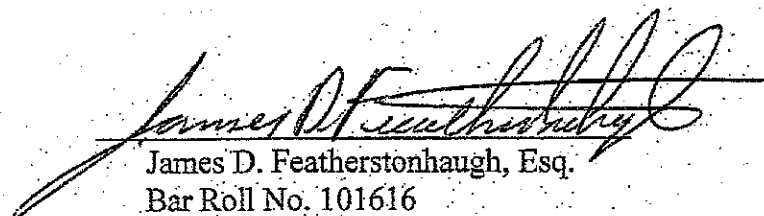

James D. Featherstonhaugh, Esq.
Bar Roll No. 101616

Exhibit B

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION

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TIMOTHY M. McGINN, AND DAVID L. SMITH,
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U/A 8/04/04, GEOFFREY R. SMITH, LAUREN
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**Case No.: 1:10-CV-457
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Relief Defendants, and

DAVID M. WOJESKI, Trustee of the David L.
and Lynn a. Smith Irrevocable Trust U/A 8/04/04,

Intervenor.

DECLARATION OF LYNN SMITH

I, Lynn Smith, pursuant to 28 USC §1746, declare under penalty of perjury, the following facts:

1. I am named as a Defendant and a Relief Defendant in the above-captioned matter.

2. I offer this declaration in support of this Cross-Motion seeking attorney's fees and living expenses.

3. The only income I receive is \$133.01 per month from the New York State Teachers Retirement System and \$790 per month from the Social Security Administration. As a result of the extensive nature of the SEC's action and the related freeze order I have \$96,700 remaining from the proceeds of the sale of my camp on the Great Sacandaga Lake.

4. The only other income I have comes from the assets currently frozen.

5. Accordingly, apart from the assets currently frozen, I have no meaningful income to support myself or defend myself throughout the pendency of these proceedings, which given the September 7, 2010 Uniform Pretrial Scheduling Order, are expected to progress well into 2011.

6. As of September 30, 2010, I currently owe the law firm of Featherstonhaugh, Wiley & Clyne, LLP the sum of \$138,451.49 for legal representation in this matter, and as the Court is well aware, the discovery proceedings, motion practice, and appellate practice are all on-going and I reasonably anticipate legal charges of approximately \$132,000 over the next three months.

7. It is my further request that the Court allow reasonable access to my funds to assist in the payment of my husband David Smith's legal defense.

8. I have prepared the proposed budget attached hereto as Exhibit C for my home at [REDACTED], Saratoga Springs, New York. The amounts reflected in Exhibit C accurately reflect the monthly amounts I require for the living expenses listed. I have no means to pay these expenses throughout the pendency of these proceedings but

it is my intention to maintain my home in Saratoga and with the Court's authorization I am prepared to pay all expenses necessary to maintain the property.

9. With regard to my home at [REDACTED], Vero Beach, Florida, I respectfully request an Order to be entered by the Court authorizing such property to be listed for sale with the understanding that the proceeds of the sale shall be placed in escrow pending the conclusion of these proceedings.

10. I have prepared the proposed budget attached hereto as Exhibit D for my home at [REDACTED] Vero Beach, Florida. The amounts reflected in Exhibit D accurately reflect the monthly amounts required for the expenses listed. I have no means to pay the expenses set forth in Exhibit D throughout the pendency of these proceedings.

11. My home at [REDACTED] Vero Beach, Florida is located in a gated community and subject to very strict association maintenance and membership rules. All assessments, maintenance standards and dues must be current otherwise the association has the right to lien the property and the membership equity. If the standards are not maintained, the association has the right to take it upon themselves to bring the property up to acceptable standards at the owners cost. The property is currently in arrears of \$19,183.27 on the mortgage. Property owners and the amount in arrears are posted publicly, and the existence of such arrears decreases the amount prospective buyers' offer when establishing a bid.

12. It is in the interest of the SEC that the equity in both the Saratoga Springs and Florida homes be maintained given the Commission is making a claim to the equity in both properties. Consequently, in order to maintain the Florida home, it is respectfully

requested that the Court authorize access to my funds to pay all expenses necessary to maintain the property throughout the pendency of these proceedings.

DATED: October 4, 2010



Lynn A. Smith

Exhibit C

The following are the minimal living expenses for the household at [REDACTED]
[REDACTED] Saratoga Springs, New York. 12866

<u>Expense Item:</u>	<u>Monthly Amount:</u>
Home mortgage	\$4667
Home taxes	\$1480
Home insurance	\$360
Telephone	\$400
Waste removal	\$43
Pharmacy	\$130
Cleaners	\$135
Food	\$1150
Gasoline	\$416
Cable/internet	\$240
Automobile payments	\$1170
Utilities	\$675
Pet care	\$160
Insurance (total)	\$2180
Medical	\$450
Automobile	\$390
Liability	\$60
Life	\$1280
Medical (co-payments)	\$115
Home maintenance	\$500
pest control, alarm, landscaping, repairs	
Entertainment	\$250
restaurants, movies, leisure	
Miscellaneous	\$475
hair care, newspapers/periodicals, EZ Pass, cash	
Clothes	\$235
General retail/household	\$400
Charitable pledge/ Empire State College	\$1250

<u>Total:</u>	\$16,431

Exhibit D

The following are the minimal expenses for the household at [REDACTED],
Vero Beach, Florida 32963

<u>Expense Item:</u>	<u>Monthly Amount:</u>
Mortgage	\$6188
Taxes	\$1875
Insurance	\$796
Utilities	\$530
Manager	\$165
Pool maintenance	\$86
Landscaping	\$475
Home maintenance	\$1150
Pest control	\$100
Dues:	
Annual	\$1375
Trail fee	\$100
Annual assessment	\$326
Vista Property assessment	\$300
Special assessment	\$200
Minimum food	\$100
Alarm	\$35

<u>Total:</u>	\$13,401