UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

v. No. 10-CV-457 (GLS/CFH)

McGINN, SMITH & CO., INC., et al.,

Defendants.

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CHRISTIAN F. HUMMEL
U.S. MAGISTRATE JUDGE

MEMORANDUM-DECISION AND ORDER

Presently pending before the Court are two motions. The first is on behalf of defendant/intervenor, Geoffrey R. Smith, trustee for the David L. and Lynn A. Smith Irrevocable Trust U/A/ 8/04/04 ("the Trust") seeking to vacate the previous order of this

Court to sell the Trust's recently purchased camp on Sacandaga Lake. Dkt. No. 568. The second is a request from defendants David L. Smith and Lynn A. Smith seeking a modification of the preliminary injunction order issued on July 22, 2010, which froze various assets of the Smiths'. Dkt. No. 576. The plaintiff Securities and Exchange Commission ("SEC") opposes both motions (Dkt. Nos. 572 & 579) and the Receiver[1] opposes the motion to modify the asset freeze to pay the Smiths' tax liabilities (Dkt. No. 580). For the reasons which follow, both of the motions are denied in their entirety.

I. Background

For a more complete description of the background of this action, see S.E.C. v. McGinn, Smith & Co., 2011 WL 1770472 (N.D.N.Y. May 9, 2011) (district court's decision denying motions to dismiss of certain defendants); S.E.C. v. Wojeski, 752 F. Supp. 2d 220 (N.D.N.Y. 2010) (reconsidering prior asset freeze order and subsequently modifying said order to include the Trust) aff'd 422 Fed. App'x 10 (2d Cir. 2011).

A. Sale of the Sacandaga Property

In 2004, David and Lynn Smith created the Trust for the benefit of their two adult children. S.E.C. v. Smith, 798 F. Supp. 2d 412, 417 (N.D.N.Y. 2011) (hereinafter Smith I). On April 20, 2010, the SEC commenced the present action against Timothy McGinn, David

[1] The Receiver, who was appointed as permanent receiver with the consent of defendants David Smith and Timothy McGinn, has also been directed to oversee and perform various duties with respect to the Trust and Lynn Smith's assets. Dkt. Nos. 96, 263, 478. Defendants contend that the Receiver had no standing to participate in the pending motion. Def. Reply (Dkt. No. 583) at 5. As the Receiver's papers were unnecessary to consider when deciding the present motion, the issue of whether or not the Receiver had adequate standing need not be addressed as it is moot.

Smith, and their company alleging they had defrauded investors of more than $80 million in violation of various federal securities laws. Id. (citations omitted). To preserve the remaining assets, the SEC sought and received a temporary restraining order ("TRO") freezing a variety of assets, including the Trust, and appointing a receiver. Id. Following entry of the TRO, the Trust moved to intervene and lift the asset freeze as to the Trust. Id. at 418. An evidentiary hearing was conducted in June of 2010 whereupon a written decision was issued by the Court that determined that the Smiths held no interest in the Trust after its creation. Id.

Shortly thereafter, the SEC discovered that despite the purported irrevocable nature of the Trust, the Smiths had entered into a "Private Annuity Contract Between David L. Smith & Lynn A. Smith as Transferors and the David L. & Lynn A. Smith Irrevocable Trust UA dated August 31, 2004, Transferee" (hereinafter "the Annuity Agreement"). Smith I, 798 F. Supp. 2d at 418. The Annuity Agreement provided that beginning in September 2013, the Trust would pay the Smiths annual payments totaling $489,932.00 throughout the remainder of their lives or until the annuity was exhausted. Id. The SEC moved for reconsideration of the Court's prior order unfreezing the Trust's assets. Dkt. No. 103. The motion for reconsideration was granted, as was the SEC's motion for a preliminary injunction as to the Trust, and the assets were again frozen for the duration of the litigation. Dkt. No. 104. Specifically the Court found that

> it had become clear that a document existed which demonstrated . . . that David Smith possessed a continuing interest in the Trust by virtue of the Annuity Agreement . . .[and] individuals who had signed the Annuity Agreement . . failed to disclose [its] existence . . . despite obligations to do so or asserted contentions directly refuted by that agreement.

Smith I, 798 F. Supp. 2d at 420. Prior to the reinstatement of the asset freeze on August 3,

2010, the Trust disbursed over $1 million, resulting in a motion for sanctions being filed by the SEC. Id.

As relevant to the present motion, in determining that sanctions were appropriate, the Court held that:

> the SEC has demonstrated by clear and convincing evidence that Lynn Smith acted with subjective bad faith in failing to disclose the existence of the Annuity Agreement . . . The consequences of that conduct included the depletion of the Trust's assets by nearly $1 million, the unnecessary expenditure of court resources on the SEC's motion for reconsideration after discovery of the Annuity Agreement, and the expenditure of resources and costs by the SEC . . . Having demonstrated Lynn Smith's subjective bad faith in these regards, the SEC has met its burden of proof under both Rule 11(c)(3) and the Court's inherent power, and sanctions will be imposed . . . .

Smith I, 798 F. Supp. 2d at 426. As a direct and proximate result of Lynn Smith's concealment of the Annuity Agreement,

> the harm to the Trust and the SEC . . . total[ling] . . . $944,848.00 . . . shall be . . . disgorge[d] . . . to the Receiver on behalf of the Trust . . . [Specifically regarding] the Great Sacandaga Lake property, it appears that the Trust has taken title to that property . . . Therefore, if Lynn Smith fails to return to the Receiver by September 1, 2011 the full amount of the $600,000 sale price of the property plus closing costs, the Receiver may proceed in whatever manner he deems economically most feasible to maximize the return on this property. This may include the sale or rental of the property, or portions thereof, depending on the Receiver's determination of market condition . . . .

Id. at 437. This decision was appealed by inter alia the Trust. Dkt. Nos. 357, 380.

With respect to the Trust's appeal, it contended that the order to sell the Sacandaga Lake property "usurps the role of the trustee and forces the Trust to bear the costs of Lynn Smith's actions even though the Trust was not accused of wrongdoing." S.E.C. v. Smith, 710 F.3d 87, 98 (2d Cir. 2013) (hereinafter Smith II). The Second Circuit stated that "it [was] appropriate to allow the magistrate judge to consider the Trust's arguments in the first

instance." Id. at 99. However, the Second Circuit then stated that "[w]e in no way suggest that the district court should determine that its prior order with regard to the Trust [wa]s inappropriate . . . [h]owever, the court should provide additional guidance to the receiver concerning how to determine whether to dispose of the property, if at all." Id. According, the appeal was ultimately "remand[ed] to allow the Trust to contest the court's order regarding the disposition of Trust property and for the magistrate judge to give additional guidance to the receiver as to disposition of the Trust property." Id. at 90.

B. Tax Liability

On July 22, 2010, an order was entered granting the SEC's motion for a preliminary injunction freezing certain assets of the defendants for the benefit of the investors pending the outcome of this action. Dkt. No. 96. On February 6, 2013, defendant David Smith was convicted of fifteen counts of a superseding criminal indictment, including three counts of filing a false tax return. United States v. McGinn & Smith, No. 12-CR-28 (DNH), Counts 30-32, Dkt. No. 108. In conjunction with that conviction, the Smiths have accrued additional tax liabilities for the years 2006, 2007, 2008, and 2009. On April 25, 2013, defendants were provided with Revenue Agent Reports (Form 4549) indicating that the Smiths' joint taxes due and owing for that four year period were $257,601.00[2]. Dreyer Aff. (Dkt. No. 576-1) ¶ 3. These taxes remain outstanding. Id. ¶ 4. Furthermore, during sentencing, David Smith was directed to pay his tax liabilities. Dkt. No. 586. Defendants ask "that this Court . . . direct the Receiver to release from Mrs. Smith's stock account the sum of $257,601.00 and remit [the] same to the IRS upon further instructions of the Court." Dreyer Aff. ¶ 6.

[2] This total does not include any interests or penalties calculated thus far. Defs. Mem. of Law (Dkt. No. 576-2) at 3, n.1.

II. Discussion

A. Sale of the Sacandaga Property

In their present motion, the Trust does not renew any of the arguments that it previously asserted during its appeal to the Second Circuit. Instead, the Trust sought to vacate the prior Court's order because selling the Sacandaga Property would drastically change the status quo of the asset freeze and temper any attempts to diversify the assets which the Trust holds. Trust Mem. of Law (Dkt. No. 568-1). The SEC opposes the motion contending that the order was well within the Court's jurisdiction to enter, as was the determination to appoint the Receiver to manage the sale, and recommending that said sale be accomplished similarly to the previously court-ordered sale of the Smiths' Vero Beach vacation property. SEC Mem. of Law (Dkt. No. 572).

1. Appropriateness of Sale

i. Arguments Initially Raised on Appeal

While not renewed in the present request to vacate the Court's order, mindful of the Second Circuit's direction to consider the Trust's arguments proffered during its appeal, such arguments will be discussed. The Trust contends that ordering Lynn Smith to disgorge any amount of money was incorrect, as disgorgement is only an appropriate remedy after a party has been found guilty of a federal securities violation. Trust Mem. of Law at 11-12. The Trust also claims that its rights to Due Process were violated and that the Annuity Contract did not provide the Smiths with any control over the Trust's principle as their interest was only in future payments. Id. at 12. Lastly, the Trust contended that the Receiver had no rights to act over the Trust.

With regard to the second and third arguments, reference is made to prior decisions from this Court which were subsequently upheld on appeal. This Court concluded that "[t]he Annuity Agreement constituted conclusive evidence of David Smith's ongoing interest in the Trust . . . ." Smith I, 798 F. Supp. 2d at 418. Such findings were not appealed. Similar findings were determined with respect to Lynn Smith, also observing that "David and Lynn Smith took unusual steps to preserve the Trust's assets from its creation in 2004 . . . ," including the payment of its taxes and continued financial support of its beneficiaries even though they were both able to draw from the Trust, and it was created and intended for such purposes. Id. at 425. The Second Circuit upheld these conclusions, stating that "the record carrie[d] a circumstantial stench that only heroic credibility findings in [Lynn Smith's] favor would dissipate." Smith II, 710 F.3d at 98. Accordingly, while the paperwork completed to create the Trust and Annuity Agreement may assert that the Trust and Smith were separate and independent actors, their actions indicate otherwise. Thus, the Trust's claims that the Smiths did not have any control or ownership interest in the Trust is disingenuous at best.

Furthermore, any due process arguments should be resolved similarly to those asserted by Lynn Smith and dismissed by the Court when the sale of the Vero Beach property was contemplated in February 2011. S.E.C. v. Smith, No. 10-CV-457, 2011 WL 9528138, at *3 (N.D.N.Y. Feb. 1, 2011) (hereinafter Smith III). Moreover, any such concerns of notice and an opportunity to be heard are allayed by the Second Circuit's remand.

Lastly, the rejection of the Receiver having the ability to make decisions regarding the Trust corpus are also unfounded. The Receiver has already successfully sold a piece of property subject to the asset freeze. Smith III, 2011 WL 9528138, at *4-*5 aff'd 653 F.3d 121, 124 (2d Cir. 2011) (hereinafter Smith V). Moreover, any renewed arguments that

decisions about the diversification or investment in the Trust should lie with the Trustee have also already been decided by this Court. S.E.C. v. McGinn, No. 10-CV-457, 2012 WL 1142516, at *8 (N.D.N.Y. Apr. 4, 2012) (hereinafter Smith IV) (explaining that in the prior Court order, "the assets of the Trust were frozen under the terms of the preliminary injunction, which assigned responsibility for management of all such frozen assets to the Receiver . . . therefore, the Receiver, not the Trustee, . . . is responsible for, and has sole control over, the management of the Trust's assets . . . . "). Any additional citation to state law is again unpersuasive as the Trust has still failed to cite any "authority for it's proposition that state law supersedes the federal law which authorized the preliminary injunction." Id. Moreover, all of these conclusions still remain law of the case, as they have not been appealed or have been upheld on appeal. See Novella v. Westchester County, 661 F.3d 128, 138 (2d Cir. 2011) ("[t]he law of the case doctrine requires a court to adhere to its own decisions at an earlier stage of the litigation absent cogent or compelling reasons not to . . . .") (internal quotation marks, alterations, and citations omitted).

To the extent that Smith I ordered disgorgement, and whether the terminology of such order was incorrect, is irrelevant to the main purpose of the order. As has been stated numerous times throughout the course of this litigation, the asset freeze was put in place to protect the interest of the investors and "to insure the availability of those assets to compensate the alleged victims of defendants' conduct in the event the SEC prevails in this action." Smith IV, 2012 WL 1142516, at *2; see also S.E.C. v. Unifund SAL, 910 F.2d 1028, 1041 (2d Cir. 1990) (explaining that an asset freeze is "ancillary relief to facilitate enforcement of any disgorgement remedy that might be ordered in the event a violation is established at trial."); S.E.C. v. Infinity Group Co., 212 F.3d 180, 197 (3d Cir. 2000) ("A freeze of assets is designed to preserve the status quo by preventing the dissipation and

diversion of assets."). Lynn Smith's actions in concealing her and David Smith's interest in the Trust and allowing for disbursements from said Trust which resulted in the sale of a property which would never have otherwise been made was in direct contravention of the purpose of the asset freeze and the cause of direct harm to the Trust. The Trust was deprived of $600,000.00 which never should have been debited from the account. Despite the fact that the Trust received a piece of real estate from that transaction, it still does not relieve Lynn Smith of the fact that she was dishonest and misleading with the Court and the Trust or the conclusion that the subsequent sanction was properly administered.

The Trust now argues that it should not be harmed by the subsequent sale of the property. The fact is that it was already harmed by being an alleged unknowing party to a transaction with what it thought was its own money after a fraud was perpetrated on the Court. Accordingly, the Trust now stands in line with the many victims that have already been identified in this case. While the harm it suffered is distinguishable from those who were the victims of the defendant's securities fraud, the fact remains that they were still victims of a chain of fraudulent events culminating in an inappropriate lifting of the asset freeze and property sale which would never have occurred but for Lynn and David Smith's actions.

Moreover, the Trust is not to be harmed by the sale, the Trust is to be made whole as that $600,000 would be placed back into the asset freeze which, if the Trust ultimately prevails, will be returned to it. Further, acknowledging what the Trust proffers, that the piece of property is valuable, the Court's order directed that "the Receiver . . . proceed in whatever manner he deems economically most feasible to maximize the return on th[e] property . . . includ[ing] the sale or rental of the property, or portions thereof, depending on the Receiver's determination of market conditions." Smith I, 798 F. Supp. 2d at 437-38. This

seems to address the Trust's concerns of maintaining a diversified portfolio, as it gives the Receiver, who has ultimate authority, discretion to do what ensures the best financial fitness for the Trust. Therefore, the Trust's prior arguments do not compel changing the Court's determination in Smith I.

ii. Arguments Presently Raised on Appeal

To the extent that the Trust contends that its assets require diversification or a reevaluation of how they are invested, the Trust is reminded that the Receiver is responsible for such decisions for the reasons stated above. Moreover, throughout all the paperwork filed it appears that the Receiver has "worked on a transparent and bilateral basis with the Trustee," accordingly, any such concerns should be raised with the Receiver. Brown Decl. (Dkt. No. 571) ¶ 3.

Lastly, for the reasons stated above, to the extent that the Trust contends that the sale of the Sacandaga Lake property will upset the status quo, it is repeated that the status quo was upset by the fraudulent actions of the Smiths resulting from their fraudulent representations during discovery and the testimony from the July 2010 hearing. Accordingly, nothing proffered by the Trust persuades the Court to upset its prior determination in Smith I.

2. Direction to the Receiver

The Second Circuit's mandate specifically directed the Court to provide more direction to the Receiver. Consistent with the holding from Smith V, the Court recognizes that "certain findings" should be determined including (1) the market value of the property; (2) expectations that the market for the property will improve in the foreseeable future; (3)

whether the property is being maintained and whether additional debts are being incurred; (4) whether the equity in the property will be preserved; and (5) whether the value of the property will appreciate significantly to compensate for the expenses being incurred. 653 F.3d at 128-29. Given that information was not previously submitted to the Court to make such determinations, the Receiver is directed to evaluate these five topics, as well as any other areas of consideration he deems relevant given his expertise[3], and determine whether selling or renting the property, or a combination of both, will maximize its value. The Receiver should present his conclusions to the Court via a written report. The parties will then be afforded an opportunity to file written objections to the Receiver's report. The Court will then consider all submissions and make a finding consistent with maximizing the property's value, directing the Receiver to proceed with that plan.

Assuming Court approval of the aforementioned plan, while the ultimate discretion regarding the status of the property remains within the purview of the Receiver, it is clear that the Receiver has been available to address any questions or concerns proffered by the Trust. This is best evidenced by the Receiver's Declaration, filed in conjunction with the pending motion, stating that "[t]he Receiver has and will continue to receive proposed instructions from and consult with the Trustee of the Trust with respect to the Trust consistent with [his] prior practices with regard to maintenance, listing and sale of both the Smith Vero Beach property and the McGinn residence." Brown Decl. (Dkt. No. 571) ¶ 10.

B. Tax Liability

Defendants contend that money should be released from the frozen assets to relieve

[3] The Receiver has already outlined his expertise in real estate sales in conjunction with Smith III. 2011 WL 9528138, at *4 (citing Brown Decl. (Dkt. No. 222-3) ¶ 3).

the joint tax liability of Lynn and David Smith because the Internal Revenue Service ("IRS"), by virtue of filing the Revenue Agent Reports, has priority over any future judgments, the stock account is an asset of Lynn Smith's and therefore should be available to pay for her portion of the tax liability, and payment of the liability and mounting interest and fees is in the best interest of the investors. The SEC disagrees, contending that the IRS is not entitled to payment from the frozen assets, the stock account belongs to David Smith, and any modification of the asset freeze would harm the investors.

1. IRS Priority

The Internal Revenue Code provides that:

> [i]f any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, additional amount, addition to tax, or assessable penalty, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon **all property and rights to property**, whether real or personal, belonging to such person.

26 U.S.C. § 6321 (emphasis added). Pursuant to the following code section, "the lien imposed by section 6321 shall arise at the time the assessment is made and shall continue until the liability for the amount so assessed (or a judgment against the taxpayer arising out of such liability) is satisfied . . . ." Id. § 6322.[4]

Defendants rely on S.E.C. v. Levine, 881 F.2d 1165 (2d Cir. 1989), for the proposition that the IRS commands a priority lien which must be discharged. Further, defendants

[4] The priority that the IRS holds is, at this time, unclear. It does not appear that the IRS has recorded its lien, though its requirement to do so in order to hold priority is presently unknown. Compare 26 U.S.C. § 6322 with S.E.C. v. Haligiannis, 608 F. Supp. 2d 444, 454 (S.D.N.Y. 2009) (holding that despite the tax lien which IRS held on a defendant convicted of engineering a Ponzi scheme, "[s]ince th[at] lien was never recorded, . . . the SEC's lien takes priority.") (internal citations omitted).

contend that the funds from which such liabilities should be drawn are those which are frozen. In S.E.C. v. Levine, the plaintiffs entered into a consent judgment with the SEC which did not attribute guilt to the parties, settling on a disgorgement amount of $11.5 million dollars for "any and all claims against [Levine]" which the SEC could have brought. 881 F.2d at 1169. Further, the consent judgment only referenced one instance of several alleged securities violations. Id. at 1175. Levine subsequently pleaded guilty to using material nonpublic information to defraud investors, perjury, and income tax evasion and was sentenced to concurrent two-year prison terms. Id. at 1170. Conversely, in the present case, there has been no calculation of assets for disgorgement or agreement or finding of wrongdoing in the civil action. While defendant Smith has been found guilty and sentenced on criminal charges, the civil action is not close to any type of resolution. The present situation is seeking a modification of the asset freeze as opposed to the priority and distribution of already disgorged assets. Accordingly, the Levine case is distinguishable from the present procedural posture of the case at hand.

Moreover, unlike the Levine case, the IRS has not attempted to collect on any liens or intervened in the present case. The intentions of the IRS remain, at best, unclear at this time. The joint tax liability was created as a result of excess income generated pursuant to criminal activity on the behalf of David Smith. While this is termed a joint tax liability as the Smiths filed joint returns during those years, because the taxes resulted from David Smith's criminal activity it appears that "[t]he victims [arguably could] have priority over the IRS." Dkt. No. 584 (citing 18 U.S.C. § 3664(i) ("In any case in which the United States is a victim, the court shall ensure that all other victims receive full restitution before the United States receives any restitution.")). Therefore, the priority assumed by the IRS at this point is, at best, unclear. Thus the Smiths' arguments contending that the IRS priority requires

immediate payment of tax liabilities is less than compelling.

2. Ownership of the Stock Account

Defendants seek the unfreezing of a specific asset, namely the stock account of Lynn Smith. Defendants contend that these assets "should be released because the assets predate and are unrelated to any fraud alleged by the SEC." Defs. Mem. of Law (Dkt. No. 576-2) at 4. More specifically, defendants assert that Lynn Smith's stock account was hers and hers alone and that David Smith had a limited involvement "administering her stock account in accordance with her wishes and duties as her broker." Id. at 5. Defendants ultimately conclude that "[a]ny assertions by the SEC that [David] Smith controlled her stock account as his own is misplaced . . . ." Id.

Such contentions are vehemently opposed by the SEC. Moreover, such assertions are disingenuous as inconsistent with the law of the case. The ownership of the stock account was previously determined by this Court, holding that "David Smith had complete access to and control over the [stock] account and that such access and control were maintained for decades." S.E.C. v McGinn, Smith & Co., Inc., 752 F. Supp. 2d 194, 216 (N.D.N.Y. 2010). Moreover, this Court determined that "David Smith utilized the Stock Account as a personal line of credit . . . [and] treated . . . [it] as his own . . . mak[ing] bridge loans to keep his business going . . . [and] occasionally deposit[ing] his assets into the stock account." Id. The injunction was upheld on the Trust's appeal. Smith v. S.E.C., 432 Fed. Appx. 10 (2d Cir. 2011). Accordingly, this is now law of the case that joint ownership of the stock account is attributed to David Smith. See Novella v. Westchester County, 661 F.3d 128, 138 (2d Cir. 2011) ("[t]he law of the case doctrine requires a court to adhere to its own decisions at an earlier stage of the litigation absent cogent or compelling reasons not to . . . .") (internal

quotation marks, alterations, and citations omitted). As such, any contentions that Lynn Smith's joint tax liability should be taken from this frozen asset because it is hers and hers alone is a gross misstatement.

3. Modifying the Asset Freeze

As previously discussed by this court, "[t]he preliminary injunction freezing the defendants' assets was entered to insure the availability of those assets to compensate the alleged victims of defendants' conduct in the event the SEC prevails in this action." Smith IV, 2012 WL 1142516, at *2 (N.D.N.Y. Apr. 4, 2012); see also S.E.C. v. Unifund SAL, 910 F.2d 1028, 1041 (2d Cir. 1990) (explaining that an asset freeze is "ancillary relief to facilitate enforcement of any disgorgement remedy that might be ordered in the event a violation is established at trial."); S.E.C. v. Infinity Group Co., 212 F.3d 180, 197 (3d Cir. 2000) ("A freeze of assets is designed to preserve the status quo by preventing the dissipation and diversion of assets."). What defendants are asking the Court to again consider is, despite the stated purpose of the asset freeze, whether defendants have demonstrated that release of the assets to pay their tax liabilities, interests, and fees would be "in the best interests of the defrauded investors." S.E.C. v. Grossman, 887 F. Supp. 469, 661 (S.D.N.Y. 1995) aff'd 101 F.3d 109 (2d Cir. 1996).

District courts have a well established "authority to freeze personal assets temporarily and the corollary authority to release frozen personal assets, or lower the amount frozen." S.E.C. v. Duclaud Gonzalez de Castilla, 170 F. Supp. 2d 427, 429 (S.D.N.Y. 2001) (citations omitted). In considering whether to modify an asset freeze, "the disadvantages and possible deleterious effect of a freeze must be weighed against the considerations indicating the need for such relief." S.E.C. v. Manor Nursing Centers, Inc., 458 F.2d 1082,

1106 (2d Cir. 1972).

For multiple reasons, the balance of interests here weighs decidedly in favor of denying defendants' motion for payment of its tax liabilities. First, the total amount of investor funds obtained through defendants' alleged fraud far exceeds the value of assets frozen by the SEC for the benefit of those investors in the event the SEC prevails in this action. Compare Am. Compl. ¶¶ 1, 6 (alleging losses to over 900 investors of approximately $84 million) with e.g., Dkt. No. 580 ¶¶ 8-9 (explaining total claims asserted against the McGinn Smith Estate of approximately $125 million with objections of approximately $24 million leaving an excess of $100 million in investor claims with a cash on hand value of $14 million, with just under $3.4 million coming from frozen assets of the relief defendants). There still remains no likelihood that a surplus will exist from the frozen assets in the event the SEC prevails in this action. The investors, on whose behalf the assets were frozen, thus possess a heightened interest in having those assets maintained without further diminution pending the outcome of the action. While the Smiths contend that the accrual of penalties and interest will harm the investors as the investors will invariably be responsible for payment of such, they fail to cite to any authority for this proposition. Conversely, it appears that the investors' interest far outweighs that of the defendants in paying joint tax liabilities assessed to them in connection with David Smith's criminal conduct. See S.E.C. v. Lauer, No. 03-80612-CIV-MARRA, 2006 WL 2660752, at *5, n.8 (S.D.Fla Aug. 2, 2006) (modifying asset freeze to allow the IRS to foreclose upon defendant's house as it remained "the only asset [purchased before the alleged fraud and] appropriately available to satisfy the unpaid [tax and mortgage] debts," as withdrawal from his other accounts was not advised as such assets were "tainted by [defendant's] alleged fraud and, therefore, should remain available to the investors.").

Second, the Smiths maintain that the stock account, from which they have requested the asset modification, is under the sole control of Lynn Smith. As discussed supra, such contentions are disingenuous as the asset is owned by both David and Lynn Smith. The asset freeze over the account, therefore, should not be lifted absent a showing that the Smiths are unable to satisfy their tax obligations from other, unfrozen sources. The Smiths state that "as a result of the freeze, the Smiths no longer have control of their own finances [and d]espite possessing substantial assets prior to any allegations of wrongdoing, any funds that they could have used to satisfy their tax due and owing have been swept up in the freeze . . . ." Defs. Reply (Dkt. No. 583) at 4-5 (citing David L. Smith Decl. (Dkt. No. 456-1 at 2-3). These were the same facts relied upon by the Smiths in their previous motion seeking modification of the freeze order to pay the fees and costs of the Trust. Smith IV, 2012 WL 1142516, at *2, *11 (N.D.N.Y. Apr. 4, 2012). However, in that same order, the Court outlined that

> the SEC has proffered evidence, unrefuted by the Trust or Smith, that in 2011, the Smiths received $14,000 for the rental of their Saratoga Springs residence for the racing season and that in the summer of 2011, the Smiths paid $3,338.40 for an engagement party . . . indicat[ing] both that David Smith has other income and assets not presently subject to the asset freeze from which . . . fees and costs can be paid and that he continues to incur non-essential expenses the payment of which could have been made for . . . fees and costs.

Id., 2012 WL 1142516, at *11. There have been no similar allegations made in this motion that the Smiths have retained excess income or spent money on things which were non-essential; however, there has also been no additional proof to the contrary other than previous assertions which were deemed untrue.

The reality of the present situation is that the true financial picture of the Smiths and their possible availability of resources remains unclear. For example, the Smiths

represented that their principle residence was in foreclosure for nonpayment. Smith IV, 2012 WL 1142516, at *3, n.2. The status and proceeds from any foreclosure proceeding are unknown. However, the possibility may remain, given the ability of the IRS to acquire "a lien . . . upon **all property and rights to property**, whether real or personal, belonging to such person," that the foreclosure also represents a potential source of income for the pending tax liability. 26 U.S.C. § 6321 (emphasis added); see also S.E.C. v. Lauer, No. 03-80612-CIV-MARRA, 2006 WL 2660752, at *4 (S.D.Fla Aug. 2, 2006) (allowing modification of asset freeze to initiate a foreclosure proceeding on residence because it "was purchased prior to the commencement of the fraudulent conduct alleged . . . and is believed to be the sole asset undisputedly not acquired with the fruits of [defendant's] ill-gotten gains."). With such uncertainty surrounding the financial fitness of the Smiths, the intentions of the IRS, and the ability to acquire payment from other sources which were not previously considered as part of the asset freeze, the declared need for the release of funds is, at best, a neutral factor in this analysis.

Third, payment of the taxes and subsequent liabilities at the conclusion of this action remains possible if Lynn Smith prevails. If she prevails, the assets presently frozen attributable to the relief defendants are approximately $3.4 million, which far exceeds the present tax, interest, and fee liabilities.

Balancing these factors, the SEC, on behalf of investors, possesses a strong interest in maintaining the assets of the stock account, presently frozen, without diminution given the large sum of money which may potentially be owed by Smith. On the other hand, the Smiths' financial profile is uncertain given their conclusory and unsupported allegations which were previously deemed unfounded, the intentions of the IRS are unknown, and the ability of the IRS to collect from an alternate source, such as their foreclosed home, has yet

to be determined. Therefore, the interests of the defrauded investors in preserving the frozen assets substantially outweighs the interests of the Smiths in releasing assets to pay for tax liabilities. For these reasons, the Smiths' motions are denied.

III. Conclusion

For the reasons stated above, it is hereby

ORDERED that:

1. The Trust's motion to vacate the Court's previous order directing the Receiver to rent or sell the Sacandaga Lake property (Dkt. No. 568) is **DENIED** in all respects;
2. The Smiths' motion for release of assets from the preliminary injunction to pay tax liabilities (Dkt. No. 576) is **DENIED** in all respects.
3. The Receiver is directed to file with the Court, within thirty days of the entry of this order, a written report regarding whether selling or renting the property, or a combination of both, will maximize its value. The parties are directed to file any written objections within fourteen days of the filing of the Receiver's report.

SO ORDERED.

Dated: September 11, 2013
Albany, NY

Christian F. Hummel
U.S. Magistrate Judge