UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION,	:	
Plaintiff,	:	
v.	:	**10 Civ. 457 (GLS/CFH)**
McGINN, SMITH & CO., INC., et al.,	:	
Defendants.	:	

PLAINTIFF'S STATEMENT OF MATERIAL FACTS IN SUPPORT OF MOTION FOR SUMMARY JUDGMENT

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July 8, 2014

Pursuant to Rule 56 of the Federal Rules of Civil Procedure, and Rule 7.1(a)(3) of the Local Rules of Practice for the United States District Court for the Northern District of New York, plaintiff Securities and Exchange Commission (the "SEC") respectfully submits this statement of undisputed material facts in support of its motion for summary judgment against Timothy M. McGinn, David L. Smith, Lynn A. Smith, Geoffrey R. Smith, Lauren T. Smith, and Nancy McGinn.

I. PARTIES AND RELEVANT ENTITIES

A. McGinn and Smith

1. Defendants Timothy M. McGinn ("McGinn"), age 66, and David L. Smith ("Smith"), age 69, founded defendant McGinn, Smith & Co., Inc. ("MS & Co.") in 1980, a registered broker-dealer with its headquarters at 99 Pine Street, Albany, New York. App. Ex. 336.

2. McGinn also served as CEO of Integrated Alarm Services Group, Inc. ("IASG"), a public company which also had its headquarters at 99 Pine Street in Albany, from July 2003 to May 2006. App. Ex. 332 at 12.

B. Entities Owned and Controlled by Smith and McGinn

3. MS & Co. was owned by Smith (50%), and McGinn (50%), until January 2004, when Thomas E. Livingston ("Livingston"), a registered representative at MS & Co., acquired a 20% interest. App. Ex. 351

4. MS & Co. sold securities to its customers through approximately 35 registered representatives who operated from MS & Co. offices in New York, NY, Clifton Park, NY, and King of Prussia, PA. 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." App. Ex. 333. *See also* App Ex. 331 (memorandum to MS & Co. employees dated December 21, 2009 stating "McGinn Smith was ordered by FINRA to cease business as a result of being in violation of its net capital requirement").

5. FINRA suspended MS & Co.'s membership on August 4, 2010. App. Ex. 336.

6. Defendant McGinn, Smith Advisors, LLC ("MS Advisors") is a New York limited liability company formed in September 2003. It was owned by McGinn Smith Holdings, LLC, and was registered with the Commission as an investment advisor from January 3, 2006 to April 24, 2009.

7. McGinn, Smith Holdings, LLC ("MS Holdings") is a New York limited liability company formed in September 2003, and was owned by Smith (50%), McGinn (30%), and Livingston (20%).

8. Defendant McGinn, Smith Capital Holdings Corp. ("MS Capital") is a New York corporation formed in January 1989, and was owned by MS Holdings (52%), Smith (24%) and McGinn (24%).

C. <u>The Four Funds, Trust and MSTF Offerings</u>

9. Defendants First Independent Incomes Notes, LLC ("FIIN"), First Excelsior Income Notes LLC ("FEIN"), Third Albany Income Notes LLC ("TAIN"), and First Advisory Income Notes LLC ("FAIN") (collectively the "Four Funds") were single purpose, New York limited liability companies formed in September 2003, January 2004, November 2004 and October 2005, respectively. App. Ex. 86-89.

10. MS Advisors was the sole managing member of each of the Four Funds, MS & Co. was their placement agent, and MS Capital was the trustee. *Id.*

11. The Four Funds each had substantively identical private placement memoranda (PPMs). *Id.* Each offered $20,000,000 worth of notes, except for TAIN, which offered $30 million, which were sold through their placement agent, MS & Co. Each offering had three tranches of notes paying quarterly interest of 5% through 10.25%, and promised a return of principal at maturity, in one, three or five years. *Id.*

12. Beginning in October 2006, MS & Co. was the sales agent for the following unregistered offerings, which sold trust certificates (the "Trust Offerings"):

a) TDM Cable Trust 06, 7.75%/9.25% ($3,550,000) (11/13/06), App. Ex. 64;
b) TDM Verifier Trust 07, 8.25%/9% ($3,475,000) (2/23/07), App. Ex. 66;
c) Firstline Senior Trust 07, 9.25% ($1,850,000) (5/19/07), App. Ex. 68;
d) Firstline Trust 07, 11% ($1,867,000) (5/19/07), App. Ex. 67;
e) TDM Luxury Cruise Trust 07, 10% ($3,630,000 (7/16/07), App. Ex. 69;
f) Firstline Senior Trust 07 Series B, 9.5% ($1,435,000) (10/19/07), App. Ex. 71;
g) Firstline Trust 07 Series B, 11% ($2,115,000) (10/19/07), App. Ex. 70;
h) TDM Verifier Trust 08, 8.50%/10% ($3,850,000) (12/17/07), App. Ex. 72;
i) Cruise Charter Ventures Trust 08, 13% ($3,250,000) (2/14/08), App. Ex. 83;
j) Integrated Excellence Sr. Trust 08, 9% ($900,000) (5/30/08), App. Ex. 74;
k) Integrated Excellence Jr. Trust 08, 10% ($580,000) (5/30/08), App. Ex. 73;
l) Fortress Trust 08, 13% ($3,060,000) (9/24/08), App. Ex. 75;
m) TDM Cable Trust 06, 10% ($1,380,000) (11/17/08), App. Ex. 65;
n) TDM Verifier Trust 09, 10% ($1,300,000) (12/15/08), App. Ex. 76;
o) TDMM Cable Jr Trust 09, 11% ($1,325,000) (1/19/09), App. Ex. 77;
p) TDMM Cable Sr. Trust 09, 9% ($1,550,000) (1/19/09), App. Ex. 78;
q) TDM Verifier Trust 07R, 9% ($2,100,000) (2/2/09), App. Ex. 79;
r) TDM Verifier Trust 08R, 9% ($2,005,000) (7/6/09), App. Ex. 80;
s) TDMM Benchmark Trust 09, 8%, 9%, 10%, 11%, 12% ($3,000,000) (8/20/09), App. Ex. 81; and
t) TDM Verifier Trust 11, 9% ($1,550,000) (9/3/09), App. Ex. 82.

13. The Trust Offerings investors were offered monthly interest payments ranging from 7.75% to 13% per year, and a return of principal at maturity, 15 months to 5 years. App. Ex. 64-83.

14. McGinn, Smith Transaction Funding Corporation ("MSTF") is a New York corporation formed in 2008. On April 22, 2008 MSTF offered $10,000,000 worth of notes sold through its sales agent MS & Co. App. Ex. 85 at 1.

15. Cruise Charter Ventures, LLC ("CCV LLC"), is a Florida limited liability company. On September 25, 2009, CCV LLC, offered $400,000 worth of 12% notes due to mature on May 31, 2010. CCV LLC was to use the net proceeds of the offering to charter a 3 day cruise departing from Miami, Florida on October 29, 2010. According to the PPM, CCV LLC operates in the trade as YOLO Cruises ("YOLO"). "YOLO believes it was the first to charter an entire ship for a "Lifestyle Cruise" in April 2009. App. Ex. 84. Timothy McGinn was the managing member of CCV LLC. App. Ex. 84 at 26.

D. Lynn, Geoffrey and Lauren Smith; Nancy McGinn

16. Defendant and Relief Defendant Lynn A. Smith ("L. Smith"), age 67, is the wife of Smith and is a resident of Saratoga Springs, New York.

17. Defendant Geoffrey R. Smith ("G. Smith"), age 34, is a resident of Aspen, Colorado. G. Smith is the son of Smith and L. Smith. G. Smith is a beneficiary of the David L. and Lynn A. Smith Irrevocable Trust (the "Smith Trust"). G. Smith became the trustee of the Smith Trust on February 14, 2011, following the resignation of the prior trustee, David M. Wojeski.

18. Lauren T. Smith ("L.T. Smith"), age 31, is a resident of Aspen, Colorado. Lauren Smith is the daughter of Smith and L. Smith. Lauren Smith is a beneficiary of the Smith Trust.

19. Nancy McGinn, age 53, is the wife of McGinn and is a resident of Troy, New York.

II. JURISDICTION AND VENUE

20. This Court has jurisdiction over this action pursuant to Sections 20(b) and 22(a) of the Securities Act [15 U.S.C. §§ 77t(b) and 77v(a)], Sections 21(e) and 27 of the Exchange Act [15 U.S.C. §§ 78u(e) and 78aa], Sections 42 and 44 of the Company Act [15 U.S.C. §§ 80a-41 and 80a-43], and Sections 209 and 214 of the Advisers Act [15 U.S.C. §§ 80b-9 and 80b-14].

21. This Court has jurisdiction over the fraudulent conveyance claim – the Eighth Claim for Relief – pursuant to 28 U.S.C. § 1345 and the Court's ancillary and/or supplemental jurisdiction.

22. Venue lies in the Northern District of New York pursuant to Section 22(a) of the Securities Act [15 U.S.C. § 77v(a)], Section 27 of the Exchange Act [15 U.S.C. § 78aa], Section 44 of the Company Act [15 U.S.C. § 80a-43], and Section 214 of the Advisers Act [15 U.S.C. § 80b-14].

III. PROCEDURAL HISTORY

A. Overview

23. On April 20, 2010, in order to halt the ongoing fraud, maintain the status quo and preserve assets for injured investors, the SEC filed a Complaint and Order to Show Cause seeking emergency relief. Dkt.[1] 1-4. Later that day, the Court granted the Commission's application and entered an Order temporarily freezing assets of the defendants and the relief defendant, L. Smith. Dkt. 5.

24. Following a hearing the Court entered the Preliminary Injunction Order on July 22, 2010. Among other things, the Preliminary Injunction Order confirmed the appointment as Receiver of William J. Brown, Esq., who had been appointed temporarily on April 20, 2010,

[1] "Dkt." refers to docket entry numbers in *SEC v. McGinn, Smith & Co., Inc. et al.*, 10-cv-457 (N.D.N.Y.).

pending the final disposition of this action, over the assets of approximately 80 entities that Smith and McGinn controlled, including MS & Co., MS Advisors, MS Holdings, and MS Capital, and the Four Funds. Dkt. 96 at 5-9, Ex. A.

25. The Court entered a Scheduling Order on September 7, 2010, Dkt. 136, and the parties conducted deposition and document discovery through December 2011.

26. On February 13, 2012, the Court set a schedule for the filing of dispositive motions. Dkt. 442. On March 27, 2012, however, upon a motion filed by the US Attorney's Office for the Northern District of New York, the Court stayed all dispositive motions and the trial pending completion of the parallel criminal proceedings. Dkt. 474.

27. On September 5, 2013, the Court lifted the stay, and further ordered that a briefing schedule on dispositive motions would be "reserved until the SEC is informed of when it can expect a copy of the transcript from the criminal proceedings." Dkt. 589. On January 23, 2014, the Court ordered that dispositive motions shall be filed by July 1, 2014. Dkt. 672. *See also* Dkt. 695 (adjusting briefing schedule).

B. <u>The Court's July 7, 2010 Decision</u>

28. L. Smith opposed the entry of the Preliminary Injunction, and moved to vacate the Court's freeze over certain assets held in her name: a checking account, a brokerage account (the "Stock Account"), the Sacandaga Lake property, and a vacation home in Vero Beach, FL.

29. On May 26, 2010, the Trustee for the David L. and Lynn A. Smith Irrevocable Trust U/A dated August 4, 2004 (the "Smith Trust") intervened in order to challenge the freeze over its only asset: a brokerage account. Dkt. 31-35.

30. Following a three-day evidentiary hearing on June 8, 9 and 10, 2010, the Court ruled that the Stock Account should remain frozen because "the SEC has shown a substantial

likelihood of success in proving that [the] . . . Stock Account includes ill-gotten gains to which [Lynn Smith] has no legitimate claim of ownership"; and "David Smith had complete access to and control over the account and that such access and control were maintained for decades." Dkt. 86 at 30-35; *SEC v. McGinn, Smith & Co., Inc., et al.*, 752 F. Supp. 2d 194, 216-217 (N.DN.Y 2010).

31. For "essentially the same" reasons, this Court also continued the asset freeze as to the Vero Beach vacation home and the checking account. Dkt. 86 at 35-36; 752 F. Supp. 2d at 217.

32. As to the Trust Account and the Sacandaga Lake property, however, the Court found that the SEC had not established a likelihood that it could prove that David Smith was their beneficial owner, and therefore vacated the freeze as to those assets. Dkt. 86 at 37-41; 752 F. Supp. 2d at 218-219.

33. The Court also vacated the freeze as to McGinn's residence in Niskayuna, NY, because in 2009 McGinn had transferred title to the house to his wife, Nancy McGinn, who was not a party to the initial Complaint. Dkt. 86 at 41-42; 752 F. Supp. 2d at 219-220.

34. Between July 7, 2010 and August 3, 2010, a total of $944,848 was transferred out of the Smith Trust's brokerage account to, among other things, pay attorney fees and purchase the Sacandaga Lake property from L. Smith.

C. <u>The SEC's Motion for Reconsideration Based on Newly Discovered Evidence</u>

35. On August 3, 2010 – after the SEC discovered a previously undisclosed "Private Annuity Agreement" between David and Lynn Smith and the Smith Trust – the SEC filed an Amended Complaint, motion for reconsideration of the July 7, 2010 decision, and an application

for emergency relief requesting that the Court, among other relief, again freeze the Smith Trust's brokerage account. Dkt. 100, 103.

36. On November 22, 2010, following an evidentiary hearing, the Court issued a decision granting the Commission's motion for reconsideration , and vacated that portion of the July 7, 2010 decision lifting the asset freeze as to the Smith Trust. Dkt. 194 at 23; *SEC v. Wojeski, et al.*, 752 F.Supp.2d 220, 233 (N.D.N.Y. 2010). The Court found that the SEC had shown "a substantial likelihood of success as to the Trust" based on, among other things, evidence that "David Smith maintained control of Trust assets after the Trust was created . . . to ensure that the annuity payments required by the Annuity Agreement could be made beginning in 2015." *Id.*

37. The November 22, 2010 decision also found evidence of "fraud, misrepresentation, and misconduct" by L. Smith and others in concealing the existence of the Annuity Agreement, and granted the SEC "leave to move for sanctions against the Trust, [Trusteee David] Wojeski, [former Trustee Thomas] Urbelis, [Trust attorney Jill] Dunn, Lynn Smith and Lynn Smith's counsel for the conduct described herein." Dkt. 194 at 20 n.17, 24; 752 F.Supp.2d at 231 n.17, 233.

38. On July 20, 2011, this Court issued a decision granting the SEC's motion for sanctions, finding "that Lynn Smith, Dunn and Wojeski acted with subjective bad faith." Dkt. 342 at 37; *SEC v. Lynn Smith, et al.,* 798 F.Supp.2d 412, 436 (N.D.N.Y. 2011).

39. Among other sanctions, the July 20, 2011 decision held L. Smith liable for disgorgement of the $944,848 transferred out of the Smith Trust's account; Dunn and Wojeski were ordered to disgorge the fees they received. L. Smith was also ordered to pay the SEC's attorneys' fees of $51,232 incurred in connection with the Annuity Agreement. Should L. Smith

fail to pay such amounts, the "SEC may have judgment against L. Smith for any amount which remains unpaid," and the Receiver was granted leave "to take whatever action he deems in his judgment to be financially appropriate to obtain the maximum possible return on the [Sacandaga Lake property], including the sale or rental of that property[.]" Dkt. 342 at 50-51; 798 F. Supp. 2d at 442.

40. On October 6, 2011, this Court entered a Judgment in favor of the SEC stating that "L. Smith is liable for attorney's fees and costs in the amount of $51,232." Dkt. 399 at 2.

D. <u>The Second Circuit Opinions Affirming this Court's Orders</u>

41. The Smith Trust, L. Smith, Dunn and Wojeski filed appeals (Dkt. 128, 279, 296, 379, 380, 381) with the United States Court of Appeals for the Second Circuit. In three opinions, the Second Circuit affirmed all of this Court's orders.

42. First, Second Circuit affirmed the orders freezing the Stock Account and the Trust. *Smith v. SEC,* 432 Fed. Appx. 10 (2d Cir. 2011).

43. Second, the Second Circuit affirmed the order allowing the Receiver to sell the Smiths' Vero Beach house. *Smith v. SEC,* 653 F.3d 121 (2d Cir. 2011).

44. Finally, the Second Circuit affirmed the sanctions against L. Smith; and found no jurisdiction to hear the appeals by Dunn and Wojeski. *SEC v. Smith,* 710 F.3d 87, 98 (2d Cir. 2013) ("The court's finding that Lynn Smith acted in bad faith in not revealing her interest in the Trust is amply supported by the record.").

45. As to the order authorizing the Receiver to dispose of the Sacandaga Lake property if L. Smith failed to pay the disgorgement order, the Second Circuit remanded "to allow the magistrate judge to consider the Trust's arguments in the first instance." 710 F.3dd. at 99.

46. On remand, and after further briefing, this Court ordered that the Receiver could proceed with the sale of the Sacandaga Lake property. Dkt. 647 at 7.

E. This Court Found McGinn in Contempt of the Preliminary Injunction Order

47. On December 1, 2010, following the filing of another emergency motion by the SEC, the Court found that, after the entry of the Preliminary Injunction, McGinn engaged in a fraudulent securities offering and that "McGinn has recklessly and willfully initiated and participated in violations of the anti-fraud provisions of the securities laws." Dkt. 207 at 8. The Court, therefore, found McGinn in contempt of the Preliminary Injunction Order, and enjoined him from proceeding with any offering without prior Court approval. Dkt. 207 at 14.

IV. THE PARALLEL CRIMINAL CASE

A. McGinn and Smith

48. On January 26, 2012, a grand jury returned an Indictment against McGinn and Smith. *United States v. Timothy M. McGinn and David L. Smith*, 12-cr-00028 (DNH) ("MS Criminal Case"), Dkt. 1.

49. On October 11, 2012, a grand jury returned a Superseding Indictment against McGinn and Smith, which charged them with conspiracy to commit mail and wire fraud (Count 1); mail fraud (Counts 2-10); wire fraud (Counts 11-20); securities fraud (Counts 21-26); and filing false tax returns (Counts 27-32). App. Ex. 6; MS Criminal Case, Dkt. 25.

50. A four-week jury trial took place from January 7 through February 1, 2013, in Utica, NY, before Judge Hurd.

51. On February 6, 2013, after 23 hours of deliberation over four days, the jury returned verdicts. Both Smith and McGinn were found guilty of conspiracy to commit mail and wire fraud (Count 1). McGinn was found guilty of seven counts of mail fraud (Counts 4-10), all

ten counts of wire fraud (Counts 11-20), all six counts of securities fraud (Courts 21-26), and all three counts of filing false tax returns (Counts 27-29). Smith was found guilty on three counts of mail fraud (Counts 8-10), two counts of wire fraud (Counts 14 and 17), all six counts of securities fraud (Counts 21-26), and all three counts filing false tax returns (Counts 30-32). App. Ex. 23, 24 (MS Criminal Case, Dkt. 104, 108).

52. Judgments of acquittal were entered as to McGinn (on Counts 2 and 3) and Smith (on Counts 2-7, 11-13, 15, 16 and 18-20). MS Criminal Case, Dkt. 109, 110.

53. On April 26, 2013, the Court denied McGinn's and Smith's motions for acquittal or, in the alternative, for a new trial. MS Criminal Case, Dkt. 135*; United States v. Timothy M. McGinn and David L. Smith*, 941 F. Supp. 2d 260 (N.D.N.Y. 2013).

54. On August 7, 2013, the Court sentenced Smith to 10 years' imprisonment and ordered him to pay a $50,000 fine, and sentenced McGinn to 15 years' imprisonment and ordered him to pay a $100,000 fine. The District Court also ordered that Smith and McGinn be jointly and severally liable for payment of $5,748,722 in restitution payable to the victims of their fraud. In addition, Smith and McGinn were ordered to pay $241,014 and $244,078, respectively, to the Internal Revenue Service. App. Ex. 25, 26.

55. Judgments against McGinn and Smith were entered on August 13, 2013. App. Ex. 10, 11 (MS Criminal Case, Dkt. 231, 232).

56. Notices of appeal were filed by Smith and McGinn, on their convictions and sentences, and by the United States, on the sentence only. MS Criminal Case, Dkt. 237, 238, 249, 250,

B. Guilty Pleas of Shea, Rogers and Simons

57. On July 24, 2012, Brian Shea, the chief financial officer for MS & Co. from April 2009 through April 20, 2010, pled guilty to one count of corruptly interfering with the administration of the internal revenue laws. In his plea agreement, Shea admitted to, at Smith and McGinn's direction, making false accounting entries and backdating promissory notes to disguise improper transfers of investor funds. App. Ex. 12 at 3-8, 13.

58. On March 7, 2013, Shea was sentenced to two years' probation, ordered to perform 100 hours of community service, and ordered to pay a $5,000 fine. App. Ex. 14.

59. On November 29, 2011, Matthew Rogers, a former senior managing director at MS & Co., pled guilty to one count of filing a false tax return. In his plea agreement, Rogers admitted that he failed to declare as income $948,000 he received from certain McGinn Smith entities from 2008 through 2009 and, at McGinn's insistence, signed backdated promissory notes in November 2009. App. Ex. 15 at 4-8.

60. On April 12, 2013, Rogers was sentenced to one year probation and ordered to pay a $10,000 fine. App. Ex. 16.

61. On November 11, 2011, Ronald Simons, a certified public accountant and partner at the accounting firm of Piaker & Lyons, who prepared tax returns for Smith, McGinn and MS & Co., pled guilty to one count of delivering and disclosing a false federal income tax return. In his plea agreement, Simons admitted to preparing Smiths' 2006 tax return, which did not report $407,000 distributed to Smith from TDM Cable Funding LLC. App. Ex. 17 at 3-4, 21.

62. On March 14, 2013, Simons was sentenced to one year probation and ordered to pay a $5,000 fine. App. Ex. 18.

V. OTHER PROCEEDINGS AGAINST MCGINN AND SMITH

63. On April 5, 2010, FINRA charged Smith, McGinn and MS & Co. with violating Section 10(b) of the Securities Act and Rule 10b-5 thereunder, and various FINRA rules. App. Ex. 19.

64. On September 14, 2011, FINRA issued a *Default Decision as to Respondents Smith and McGinn*, which barred Smith and McGinn from association with any FINRA member firm. App. Ex. 20.

65. On February 20, 2014, an Administrative Law Judge issued an *Initial Decision Making Findings and Imposing Sanctions by Default as to Timothy M. McGinn* which permanently barred McGinn from, among other things, associating with any broker, dealer, or investment adviser. App. Ex. 59 (Initial Decision). *See also* App. Ex. 60 (Notice That Initial Decision Has Become Final).

66. On April 23, 2014, the Commission issued, on consent, an *Order Making Findings and Imposing Remedial Sanctions Pursuant to Section 15(b) of the Securities Exchange Act of 1934 and Section 203(f) of the Investment Advisers Act of 1940 as to David L. Smith*, which permanently barred Smith from, among other things, association with any broker, dealer, and investment adviser. App. Ex. 61.

VI. UNDISPUTED FACTS SHOWING VIOLATIONS OF THE FEDERAL SECURITIES LAWS

A. Evidence of McGinn's and Smith's Violations

1. Structure of the Four Funds and the PPM Disclosures

67. The PPMs for the Four Funds did not authorize use of offering proceeds to invest in affiliates of MS & Co.; to redeem investors in earlier MS & Co. offerings; to purchase an investment from an affiliate for more than the affiliate paid; or to redeem investors in the Trust

Offerings. App. Ex. 86-89. Nevertheless, Smith used Four Funds proceeds for all these prohibited purposes, starting almost immediately after the launch of FIIN in September 2003.

68. Smith approved the content of the Four Funds PPMs.

69. The PPMs for the Four Funds all include a subsection titled "Use of Proceeds." App. Ex. 86 at 15, 87 at 15, 88 at 15, 89 at 15.

70. The "Use of Proceeds" subsection states that net proceeds will be used "to acquire various public and/or private investments." App. Ex. 86 at 15, 87 at 15, 88 at 15, 89 at 15.

71. The PPMs does not state that the proceeds of the Four Funds may be used to invest in affiliates of MS & Co.

72. The PPMs for the Four Funds which state that the Four Funds "may acquire such investments directly or from… an affiliate or managing member," and that if any of the Funds "purchase[s]" an investment from a managing member or affiliate, that Fund will pay the same price it would have paid had it directly purchased the investment. App. Ex. 86 at 15, 87 at 15, 88 at 15, 89 at 15.

73. The PPMs disclose that MS & Co. as placement agent would receive a one-time 2% commission. App. Ex. 86 at 1, 87 at 1, 88 at 1, 89 at 1.

74. Each of the Four Funds' PPMs made clear that the investors' risk arose from the investments made by the Funds: "[o]ur cash flow is wholly dependent on our ability to find and acquire suitable investments. If we are unable to generate a sufficient cash flow, our results of operations and financial condition would be materially and adversely affected and we may be unable to make payments on the notes." See, e.g., App. Ex. 86 at 13. The PPMs also stated that "[o]ur profitability is largely determined by the difference, or 'spread,' between the effective rate

we pay on the Investments we acquire and the full rate of return received on such Investments." See, e.g., App. Ex. 86 at 13.

2. Payments of Four Funds Proceeds to Redeem pre-2003 Offerings

75. Contrary to the PPMs and at Smith's direction, investor proceeds from the Four Funds offerings were used to pay investor redemptions or interest to investors of pre-2003 MS & Co. offerings and to make loans to entities controlled by McGinn and Smith. App. Ex. 1 at ¶¶ 8-29, 32-34 and 36.

76. Between the early 1990s and 2003, MS & Co. raised approximately $185 million from investors in dozens of trusts formed to invest in pools of security alarm contracts (the "Pre-2003 Trust Offerings"). App. Ex. 352; App. Ex. 334 at 1. These Pre-2003 Trust Offerings had fixed interest rates and maturity dates. See, e.g., App. Ex. 314 (RTC Trust PPM), 29, 31, 33, 338 (SPT Trust PPMs).

77. Most of the alarm contracts owned by the Pre-2003 Trust Offerings were rolled into the $200 million IPO of IASG and the Trust investors were redeemed from IPO proceeds. App. Ex. 332 at 15. However, several Pre-2003 Trust Offerings were not rolled into the IASG IPO and relied on $12.8 million in financial support from the Four Funds offerings. App. Ex. 1 at ¶ 8; at 44 (Palen Ex. 8).

78. Under the Pre-2003 Trust Offering PPMs, the noteholders were supposed to be paid from the cash flow generated by the pool of contracts. See, e.g., App. Ex. 29 at 13.

79. Smith's 1999 letter to McGinn acknowledged the failure of the Pre-2003 Trust Offerings. App. Ex. 54, and 55 Smith stressed the need to "develop[] a course of action that will stave off our immediate financial crisis" because "if our trusts go into default, everything else will come apart." App. Ex. 55 at 3, 5. MS & Co. had "become addicted to the cash flow from

the trust business, and without them will have a difficult time surviving." App. Ex. 55 at 5. Smith characterized the use of new dollars to "fulfill the investment promise to earlier investors" as a "Ponzi scheme." App. Ex. 55 at 7. Smith stated that the "default of the trusts will drastically reduce revenues, . . . bring on crushing litigation . . and prosecution by regulators or worse." Id.; see also id. at 6, 10 (Smith feared criminal prosecution). Smith suggested that MS & Co. "restructure debt and reduce present financing costs." App. Ex. 55 at 20.

80. The "restructure" that Smith wrote of came in the form of the IASG IPO: MS & Co. solved its Pre-2003 Trust Offering cash flow shortfall by using approximately $35 million raised through the IASG IPO to redeem Pre-2003 Trust Offering investors. App. Ex. 332 at 16; App. Ex. 55 at 20. As Shea testified, "a big part of the IPO was to relieve all the high interest rate payments."

81. Smith used Four Funds proceeds to either: (1) purchase alarm contracts from Pre-2003 Trust Offerings for more that their initial cost; or (2) make loans to these trusts for the purpose of redeeming or making interest payments to investors. App. Ex. 1, ¶¶ 8-29. This was contrary to the investment mandate in the Four Funds PPMs, which stated that investments were acquired from affiliates "we will not pay above the price paid by our managing member or such affiliate for the Investment." App. Ex. 86 at 15, 87 at 15, 88 at 15, 89 at 15).

82. The Four Funds purchased alarm contracts from four of the Pre-2003 Trust Offerings, Security Participation Trust I ("SPT I"), Security Participation Trust II ("SPT II"), Security Participation Trust III ("SPT III"), and Security Participation Trust IV ("SPT IV") for an amount equal to the amount these trusts needed to redeem SPT investors. The amount the Four Funds paid for the alarm contracts exceeded the amount that the SPTs initially paid for them years earlier, despite the fact that the income from those same contracts had, in Smith's

words, "been substantially reduced due to attrition." App. Ex. 1, at ¶¶ 8-29; at 45 (Palen Ex. 9) App. Ex. 27 at 3, App. Ex. 47at 3.

83. These purchases were negotiated and signed by and between Smith for the Four Funds, as the "buyer," and McGinn for the Pre-2003 Trusts, as the "seller." App. Ex. 1 at ¶ 40. App. Ex. 28, 30, 32. Smith instructed his staff to create purchasing agreements retroactively in April 2009. App. Ex. 35. In September 2007, MS & Co.'s accounting staff determined that the Four Funds paid a total premium of around $5.5 million for the SPT Trust alarm contracts. App. Ex. 49 at 6.

84. FIIN, FEIN, and TAIN funds were used to redeem a customer invested in Pacific Trust. App. Ex. 1, ¶¶ 22-23. Letters of credit between the Funds and Pacific Trust were backdated for this transaction as well. Id. at ¶ 23. Similarly, FEIN and FAIN loaned over $750,000 to pay RTC Trust interest after that trust failed to generate sufficient income. Id. at ¶¶ 24-27. FAIN made a $1 million "investment" in SAI Trust in connection with an investor redemption. Id. at ¶¶ 28-29.

85. Smith acknowledged the use of Four Funds money to support the Pre-2003 MS Trusts in an internal memorandum dated November 25, 2007: "A substantial amount of investment dollar went to refinance alarm contracts that were due in 2003. The income from these contracts had been substantially reduced due to attrition . . . we felt that other investment returns would make up for the shortfall in cash flow from the alarm contracts. This proved not to be the case." App. Ex. 47, 27.

86. The SPT notes were three-year notes due on or about November 1, 2003 at maturity. App. Ex29 (SPT PPM).

87. FIIN entered a purchase agreement with SPT in the amount of 2,090,000, dated November 1, 2003 ("SPT I"). App. Ex. 1, ¶ 12, App. Ex. 28, 339 Smith Dep. 210:11-16, 203:24 – 205:8.

88. The SPT I purchase agreement was signed by Smith on behalf of FIIN as managing director and McGinn on behalf of SPT I. App. Ex. 1, ¶ 20; App. Ex. 28; App. Ex. 339.

89. Smith and McGinn jointly decided on behalf of MS Advisors to pay $2,090,000 for the assets acquired pursuant to SPT I. App. Ex. 289; 290 (Smith Dep. 211:16-24, December 13, 2011; Smith Dep. 238:6-13, December 14, 2011.)

90. MS & Co. as trustee of SPT made the decision on behalf of SPT to accept $2,090,000 for the assets in question in SPT I. App. Ex. 28; App. Ex. 289 (Smith Dep. 212:6-11, December 13, 2011.)

91. Smith and McGinn, as principals of MS Advisors, had a fiduciary responsibility to FIIN note holders to pay the least possible price for the SPT I assets. App. Ex. 289 (Smith Dep. 216:20 – 217:22, December 13, 2011.)

92. As principals of MS & Co., Smith and McGinn had a fiduciary responsibility to the SPT note holders to receive the highest possible price for the SPT I assets. App. Ex. 289 (Smith Dep. 216:20 – 217:22, December 13, 2011.)

93. No third party was brought in to conduct an independent evaluation of the SPT I assets. App. Ex. 289 (Smith Dep. 218:3 – 219:16, December 13, 2011.)

94. The Four Funds subsequently acquired other SPT assets, in purchase agreements SPT II, III, and IV. App. Ex. 1, ¶ 14-19; App. Ex. 290; (Smith Dep. 267:17 – 268:5, December 14, 2011; McGinn Dep. 110:13 – 112:21, December 15, 2011.)

95. The sales of SPT I, II, III, and IV assets to the Four Funds all coincided with the maturation of the SPTs. (McGinn Dep. 112:22-25, December 15, 2011.)

96. If the SPT I, II, III, and IV assets had not been sold to the Four Funds, McGinn, representing the trustee for the SPT, would have had to seek the consent of SPT note holders to extend the maturity dates. (McGinn Dep. 113:6 – 114:10, December 15, 2011.)

97. Overall, MS & Co. overpaid for the SPT contracts by at least $5.5 million. (See App. Ex. 49 at 6)

3. The Four Funds' Unauthorized Investments in Affiliates

98. The Four Funds PPMs did not disclose that the Funds would directly invest in affiliates of McGinn and Smith. See, e.g. App. Ex. 86 at 15. In November of 2007, Smith recognized that

> [O]ne of the more troubling aspects of the [Four Funds] investments has been my willingness to make substantial investments in affiliated entities, both because they were available and in some cases, such as Coventry, new investments were needed to support past investments. Thus, in the case of Coventry, alseT, EXBV the pattern was often the same; invest more money to support the original investment. In all cases this has proved to be a poor decision and has not only aggravated our cash flow problems, but puts us in some legal jeopardy as well. App. Ex. 47 at 3, 27 at 3.

99. By December 31, 2007, investments in affiliates accounted for over half of the investments made by the Four Funds – a total of approximately $40.3 million. App. Ex. 1, ¶ 30; see also id. at 46-52 (Palen Ex. 10-14). With the exception of an investment in Pine Street Capital Partners ("Pine Street"), most the affiliated investments provided no cash flow to the Four Funds, however, the investment plus accrued interest remained on the Four Funds balance sheet at cost. App. Ex. 1 at ¶ 30.

100. Joseph Carr was General Counsel at MS & Co. Smith and McGinn never asked Carr whether the Four Funds could make loans to affiliated companies. App. Ex. 354 at 33. In

early 2010, Carr read the PPMs for the Four Funds, and testified at his deposition that "I formed an opinion that they [loans to affiliates] were not appropriate . . . it couldn't loan money to an affiliated company. That was my reading of the PPMs." Id. At 33-34.

101. The Four Funds invested approximately $8.8 million – 10% of the money raised from Four Funds investors – in an affiliated start-up company, alseT IP Management ("alseT"). App. Ex. 1, ¶ 31; at 67 (Palen Ex. 23).

102. Newton Advisors, which was owned by Smith (30%) and Livingston (70%), was a managing member of alseT and owned a 24.1% interest. App. Ex. 306 at 2. App. Ex.323 at 27. App. Ex. 53 at 41. Livingston was also an officer of alseT.

103. alseT had no revenues. App. Ex. 1 ¶ 31. To make its quarterly interest payments due on loans from FIIN, TAIN, and FAIN, alseT had to borrow additional money. App. Ex. 1 ¶ 31; id. at 67 (Palen Ex. 23); App. Ex. 318.

104. In a memorandum to Smith and McGinn in December 2007, Livingston recognized "the obvious conflicts of interest that existed between [alseT as] borrower and [MS & Co. as] lender." App. Ex. 50 at 4. As of December 2, 2007, MS & Co. considered its investment in alseT to be worthless. App. Ex. 1 ¶ 31 (citing App. Ex. 47 and 48).

105. Livingston was paid $40,000 per month from alseT beginning in January 2006 through April 2007, for a total of $640,000. App. Ex. 324.

106. Another example of a failed affiliated entity investment is FEIN's investment in Capital Center Credit Corporation ("C4"). C4 was an MS & Co. entity controlled and used by Smith and McGinn to cover cash short falls in the Pre-2003 Trust Offerings. App. Ex. 1, ¶ 32; App. Ex. 55 at 6-7; App. Ex. 307.

107. On March 23, 2004, Smith wrote to the SEC Broker-Dealer Inspection Program—which had concluded that C4 was "an unregistered broker-dealer," see RMR Ex. 874—to report that "[C4] is a business that will shortly be liquidated" and that "the only solution is to cease any activities [of C4] that might be construed as a securities transaction and to orderly liquidate the [C4]." App. Ex. 56 at 2.

108. In January 2004, FEIN made a $500,000 loan to C4 to redeem an investor. App. Ex. 1 at ¶¶ 32-34. By the end of 2007, the Four Funds had a cumulative total investment in C4 of $720,231, including accrued interest, which was written off in full as of December 31, 2009. Id. at ¶ 34.

109. In June 2004, FEIN loaned MS & Co. affiliated entity JV Associates $95,000, which JV Associates used to pay four delinquent mortgage payments for August to November 2002. App. Ex. 1 ¶ 35. Smith and McGinn were limited partners of JV Associates, each owning approximately 20% interest, and the FEIN promissory note was signed by McGinn on behalf of JV Associates. App. Ex. 342. No interest or principal payments were ever made to FEIN, and the balance remained on FEIN's books through December 31, 2009, when it was written off. App. Ex. 1 ¶ 35.

110. Beginning in 2005, Smith invested Four Funds proceeds in two companies controlled by MS & Co. Senior Vice President of Corporate Finance Mark Casolo: Atlantis Strategic ($12,500) and Caribbean Club International (CCIG) ($1.2 million). App. Ex. 1 at 51 (Palen Ex. 14). Casolo is currently in a state prison after pleading guilty to stealing $1.7 to $2.2 million (after leaving MS & Co.).

111. In 2007, Smith caused FEIN, TAIN and FAIN to invest $2 million in 107th Associates, a company whose assets Smith controlled. App. Ex. 1 at 51 (Palen Ex. 14); see also

Dkt. No. 96 at 13 (107th Associates listed as a Receivership entity "controlled by McGinn and/or Smith").

112. Smith invested a total of $120,000 raised from Four Funds investors in Century Same Day Surgery and approximately $7.6 million in Coventry Resources Corporation ("Coventry"). App. Ex. 1 at 46-51(Palen Ex. 10-14). Smith served as chairman of the board of directors for both entities**.** App. Ex. 369 at 6; App. Ex. 360**.**

113. All of the Four Funds provided loans to Coventry. App. Ex. 290 (Smith Dep. 307:22 – 308:2, December 14, 2011.) McGinn, Smith Partners had an ownership interest in Coventry. App. Ex. 290 (Smith Dep. 308:6-12, December 14, 2011.) The Four Funds continued to invest in Coventry even after losses became apparent. App. Ex. 290 (Smith Dep. 312:20 – 313:4, December 14, 2011.)

114. In his December 2007 memorandum to Smith and McGinn, Livingston criticized the "losses approaching some $45 million" that the Four Funds had suffered, as well as the "HUGE conflicts" in the Coventry investment. App. Ex. 50 at 4.

115. The Four Funds made numerous transfers to McGinn Smith affiliates, including M&S Partners (approximately $604,000); McGinn, Smith Acceptance Corp. ($121,790); McGinn, Smith & Co. Preferred Stock ($820,800); MS Holdings ($350,000); and McGinn, Smith Licensing LLC ($75,000). App. Ex. 1 at 140 (Palen Ex. 14); see also Dkt. No. 96 at 13-14 (Order listing entities "controlled by McGinn and/or Smith").

116. Seton Hall, which received $14,190 from FAIN, was a medical office building in Troy, NY, that Smith and McGinn purchased through a limited partnership; they also financed the mortgage through a private placement. App. Ex. 1 at 51 (Palen Ex. 14); ,Dkt. No. 96 at 14 (Seton Hall Associates listed as a Receivership entity "controlled by McGinn and/or Smith").

117. Smith invested $1.4 million raised from TAIN investors in State Street Hospitality, a hotel project in which MS & Co. had an equity interest. App. Ex. 1 at 51 (Palen Ex. 14).

118. Other Four Funds' investments in affiliated entities are described in Exhibit 14 to the Palen Declaration. App. Ex. 1 at 51-52 (Palen Ex. 14).

119. The Four Funds paid approximately $7.7 million in underwriting, management and administrative fees to MS & Co. during the period 2003 through 2009. App. Ex. 1 at ¶ 39; id. at 58 (Palen Ex. 16); App. Ex. 21. Tax returns reflect that the Four Funds paid MS & Co. fees of approximately $1.5 million in 2004; approximately $2.6 million in 2005; approximately $2.5 million in 2006 and approximately $380,000 in 2007. App. Ex. 1, ¶ 39; id. at 58 (Palen Ex. 16).

4. The Four Funds Commingled Investor Funds and Redeemed Preferred Investors

120. The Four Funds used money from each other to pay investor redemptions and interest. For example, FEIN's January and February 2005 interest payments, and a $2 million investor redemption, were paid in part using nearly $2 million of TAIN investor funds. According to bank and accounting records, in February 2007, TAIN "loaned" FEIN $450,000 to redeem an investor and to pay interest due to investors. App. Ex. 1 ¶ 36; at 51 (Palen Ex. 14).

121. Just before November 25, 2007, around the time Smith acknowledged in writing the "troubling" problems that arose from his "willingness to make substantial investments in affiliated entities, App. Ex. 27 at 3-4, Smith used Four Fund assets to redeem preferred investors approximately $2.7 million. Smith used Pine Street Capital, one of the only assets the Four Funds owned that had any real value, to redeem his preferred customers out of the Four Funds in September and October 2007. App. Ex. 1, ¶ 40 (citing App. Ex. 320 and 317).

5. The Four Funds Ran a Cash Deficit

122. By the end of 2007, the Four Funds owed investors a total of approximately $84 million according to the Funds' financial statements. App. Ex. 1 at ¶ 37, at 51 (Palen Ex. 14). MS & Co. estimated that at that time, the investments held by the Four Funds were worth only approximately $37 million. App. Ex. 1 at ¶ 37 (citing App. Ex. 47 and 48).

123. In addition to the Four Funds' cash deficits and inability to pay fees during 2007, and the problems with redeeming investors' Four Funds notes maturing in 2008, Smith's more immediate concern was the inability to pay the approximately $700,000 due to the brokers for their Four Funds annual commission payment on December 15, 2007. See App. Ex. 47 at 1. As discussed below, the shortfall that MS & Co. was experiencing from the lack of fees coming in from the Four Funds was made up by unauthorized payments made to MS & Co. from the Trusts.

6. Smith Instituted a Redemption Policy

124. By at least December 2006, Smith instituted a policy (hereinafter the "Redemption Policy") that in order for the Four Funds LLC to redeem an existing customer on his or her maturing Four Funds note, MS & Co. brokers needed to find a new customer to purchase that note. *See, e.g.,* App. Ex. 37.

125. The Redemption Policy, which required brokers to find a buyer for maturing notes if the customer wanted to redeem, was a significant departure from the terms of the PPM. The Four Funds PPMs provided that interest payments and redemptions would be made from underlying assets and their cash flow, and contained no language making redemption contingent upon finding a new customer. *See, e.g.,* App. Ex. 86 at 12.

126. The existence of the Redemption Policy is confirmed by numerous emails. On November 14, 2006, at 11:31 am, Guzzetti received an email from Sicluna stating: "Andy, Lex is going to replace all of his clients that are redeeming. We need to know what Frank, Phil, Brian and Dick are going to do." App. Ex. 44.

127. On December 21, 2006, Sicluna forwarded Guzzetti an email exchange between her and Smith. Sicluna had informed Smith that a Rabinovich client wanted to purchase a $100,000 TDM Cable 06 note with the proceeds of a maturing TAIN $100,000 note, and she asked Smith "Is there any problem with him doing this?" Smith responded "yes. Phil needs to replace the $100,000 before doing the trade. I am running on fumes with all these redemptions and cannot afford any more. Please inform Andy [Guzzetti]." App. Ex. 37.

128. In his deposition, Guzzetti testified that this email meant that TAIN did not have sufficient capital on hand to redeem a noteholder, and that Smith's instruction in the email was not consistent with the PPM. App. Ex. 110 at 156.

129. On February 2, 2007, Guzzetti forwarded to Smith an email stating "I want to make sure you are aware of this possible problem." In the email, an administrative staff person noted that "[w]e do not have the funds ava[ilable] [to redeem a $200,000 FEIN note] unless you have cks/pmts that come in today's mail, we would need about 125K to come in to cover this request." App. Ex. 41.

130. On November 10, 2007, Smith emailed Guzzetti after learning that Feldmann and Gamello "were redeeming some Fains in order to roll into First Line." Smith's instructions to Guzzetti were clear: "I want it clear to all brokers that is not permissible. With the interest payment coming due and commissions payable in December I do not have the liquidity. ***Any redemptions have to have replacement sales beforehand***. . . . My preference is for there to be no

redemptions. . . . Please handle this with TLC. We need some team play and cooperation." App. Ex. 42 (emphasis added).

131. Guzzetti responded to Smith the next day and, referring the Guzzetti's regular Monday conference calls with all brokers, told Smith that "[y]ou may have to get on the call Monday afternoon." App. Ex. 42.

132. On November 12, 2007, Guzzetti reported back to Smith on the same day that "[c]all went well. Not a lot of discussion. I am not sure they believe us about redemptions. I have a feeling they are thinking if push comes to shove we have to redeem." App. Ex. 43.

133. On November 15, 2007, Guzzetti emailed an MS & Co. broker to point out that the broker's clients "redeemed $235,000 of the 1yr FAINS and we have not gotten any replacement tickets for the redemptions." App. Ex. 38. Guzzetti followed up on November 16, 2007, by stating "As we have discussed on numerous calls. Dave has asked that you replace all redemption $'s with new money." *Id.*

134. On January 16, 2008, responding to an email from another MS & Co. broker asking for "an answer on payout to [customer] redemptions," Guzzetti stated "Sorry for not getting the answer sooner, but I wanted to connect with Dave Smith. ***Dave [Smith] is not changing his position….if a client wants to redeem out of a 1 yr piece of paper. We must have the fc [financial consultant] replace it***." App. Ex. 46 (emphasis added).

135. The Redemption Policy continued through 2009. On March 17, 2009, in response to an email from an MS & Co. broker requesting immediate redemption for certain TDM Verifier 07R customers, Smith instructed "[i]t would be helpful if you could sell the $125,000 worth of redemptions." The broker responded "[w]hen the TDM was given to the sales force to

sell about 20 months ago, we were not told that investors could only redeem if a new client took them out. My clients continue to ask me if they've bought into a Ponzi Scheme[.]" App. Ex. 39.

136. On November 23, 2009, Guzzetti emailed McGinn and Smith about a client who is "very antsy" about a redemption that had been requested in June. Smith responded the next day: "Andy, Brokers are asked to replace clients seeking redemption." App. Ex. 45.

7. Four Funds Default

137. On or about January 15, 2008, Smith wrote a letter that was sent to Four Funds junior note holders, informing them that their interest payments would be reduced to 5% from 10.25%, and attributing the change to "the sub prime mess."); App. Ex. 121 at 1.

138. The January 2008 reduction in interest on the Four Funds junior notes constituted an Event of Default, as defined in the Four Funds PPMs, because it was "a failure to pay interest on a note" and a "failure to observe or perform any material covenant." *See, e.g.,* App. Ex. 86 at 19. The PPMs provided that if an Event of Default occurred, "the trustee or the holders of at least a majority in aggregate principal amount of the then outstanding notes for such tranche may declare the unpaid principal and any accrued interest on the notes to be due and payable immediately." *Id.*

139. On or about January 25, 2008, an MS & Co. broker emailed Smith that, "I think the fiduciary responsibility to the clients has been breached since none of these clients were aware of the pending problems in the Third Albany Income Notes…. [C]lients have expressed concern that they were misled about material characteristics of these investments. I was not aware that the same investments were put in each note. I went out of my way to make sure clients were spread among the various notes so that they would have DIVERSIFICATION." App. Ex. 371.

140. On or about April 11, 2008, Smith sent a second letter to the junior note holders. App. Ex. 355 at 1.

141. The April 2008 letter stated that in light of the circumstances highlighted in the earlier January 2008 letter, and because two investments had eliminated their dividends or ceased distributions, the Four Funds were "forced" to eliminate the interest payments on Secured Junior Notes for the quarter. App. Ex. 355 at 1-2.

142. On or about October 13, 2008, Smith wrote and caused to be sent a letter to note holders in all tranches of the Four Funds. App. Ex. 356 at 1.

143. The October 2008 letter included an attached restructuring plan extending the maturity dates of the notes and reducing interest payments for all tranches. App. Ex. 356 at 8-9.

144. The October letter stated that MS Advisors and MS & Co. "will be making its own sacrifice" by "forfeit[ing] all such future fees while this reorganization plan is in effect." App. Ex. 356 at 4. The October 2008 letter also described the "financial crisis" broadly, including the collapse of hundreds of banks and mortgage companies, and a 500-point drop in the Dow Jones Industrial Average. App. Ex. 356 at 2-3.

8. McGinn and Smith Misused the Trust Offering Proceeds

145. MS & Co. raised approximately $41 million from investors in the Trust Offerings and MSTF. App. Ex. 1 at ¶¶ 41, 70; id. at 39-40 (Palen Ex. 3, 5).

146. Proceeds raised from the Trust Offerings were supposed to be used to invest in specific streams of receivables, usually related to long term contracts for burglar alarm service, "triple play" (broadband, cable and telephone) service or luxury cruise cabin bookings. App. Ex. 1 at ¶ 42.

147. According to the Trust Offerings PPMs, the funds raised from investors would first be deposited into the Trust's escrow account and, after deducting the disclosed fees and other deal costs, the "net proceeds" would be advanced to a funding entity, which would or had already entered into an agreement with a third party to purchase the underlying asset. App. Ex. 1 at ¶ 42. The funding entity was typically McGinn Smith Funding LLC or TDM Cable Funding LLC. *Id*.; see also App. Ex. 1 ¶ 42; *id*. at 59 (Palen Ex. 17).

148. Once the investor funds were deposited into the escrow account and transferred to the funding entity, they were used to enrich McGinn, Smith or M. Rogers personally, to support MS & Co. or to support other MS & Co. entities as liquidity needs dictated. App. Ex. 1 ¶ 43.

149. For each Trust offering, less than the amount represented in the PPM was actually invested in the specific streams of receivables. App. Ex. 1 ¶ 44.; see also id. at 60-62 (Palen Ex. 18). In the aggregate, only 58% of money raised from Trust Offering investors was invested in disclosed assets, as compared to the 85% promised (in the aggregate) by the Trust Offerings PPMs. App. Ex. 1 ¶ 44 and App. Ex. 1 at 60-62 (Palen Ex. 18).

150. Smith, McGinn and M. Rogers took approximately $4.7 million from Trust escrow and funding entity accounts. App. Ex. 1 at ¶ 47, at 42-43 (Palen Ex. 7). These payments were not authorized by the Trust Offering PPMs. Id. ¶ 47.

9. Funds Raised from Trust Offering Investors Paid Excess Fees to MS & Co.

151. The Trust Offerings PPMs disclosed combined maximum underwriting fees and other fees payable to MS & Co of up to $3.2 million. App. Ex. 1, ¶ 46, id. At 40 (Palen Ex. 5). However, from October 2006 through December 2009, MS & Co. received in excess of $6.4 million in connection with the Trust Offerings. App. Ex. 1, ¶ 46; id. at 41 (Palen Ex. 6).

10. NFS's Termination of MS & Co.'s Clearing Agreement

152. In December 2005, MS & Co. and NFS entered into a Fully Disclosed Clearing Agreement (the "Clearing Agreement"), which required that MS & Co. maintain a minimum net capital of $250,000. App. Ex. 52.

153. NFS kept track of MS & Co.'s net capital through its Focus Reports. In an MS & Co. management meeting on March 17, 2009 attended by McGinn and Smith, one of the agenda items was "[r]eview of current financial position, including net capital[.]" App. Ex. 40.

154. On October 3, 2007, NFS sent a letter to Smith stating that MS & Co.'s Focus Report indicated that its "net capital is below the NFS Net capital requirement." This letter further requested that Smith "address this deficiency immediately as continued violation may result in termination of the [Clearing Agreement]." App. Ex. 52 at 1.

155. Seven subsequent letters from NFS to Smith dated March 28, 2008; April 30, 2008; October 28, 2008; December 1, 2008; January 29, 2009; March 5, 2009; and April 7, 2009, similarly noted MS & Co.'s net capital violation and requested that Smith bring MS & Co. back into compliance. App. Ex. 51, 52.

156. In a letter dated April 24, 2009, which noted that "NFS has sent McGinn Smith numerous notices informing McGinn Smith of such net capital deficiency," NFS exercised its right "to terminate its clearing relationship with McGinn Smith effective May 26, 2009." App. Ex. 51 at 7. NFS rescinded the termination on May 15, 2009, "due to the representation by [MS & Co.] that capital has been infused into the broker dealer to meet the NFS net capital

requirement and contingent upon [MS & Co.'s] agreement to transition all proprietary Promissory Notes from the NFS platform to another custodian." App. Ex. 51 at 9.

157. As soon as June 3, 2009, Smith received yet another letter from NFS stating that its net capital was below the NFS requirement. App. Ex. 51 at 11. Additional violations were noted in letters dated June 29, 2009 and August 31, 2009. App. Ex. 51 at 12, 13. Smith's response to NFS emphasized MS & Co. securities offerings as an answer to its net capital problems. A letter from Smith to NFS dated March 20, 2009, stated "we are presently pursuing as capital raise of approximately $500,000 which we believe will be in place by June 1, 2009." App. Ex. 51 at 5.

158. The final violation letter from NFS dated September 29, 2009, stated that due to MS & Co.'s continued breach of the Clearing Agreement, "NFS has decided to terminate its clearing relationship with McGinn Smith." App. Ex. 51 at 15.

B. **Evidence From the Criminal Trial**

1. **Four Funds Offering Proceeds Were Used for Unauthorized Purposes**

159. Smith was principally responsible for the Four Funds and made the investment decisions. App. Ex. 108 at 3163.

160. David Rees was the comptroller at MS & Co. from August 2002 through April 2009. App. Ex. 105 at 903. As comptroller, Rees' responsibilities were "preparing the financial statements, ensuring brokers were paid, doing accounts payable, maintaining the firm's financial statements, and handling the net capital calculation for the firm." App. Ex. 105 at 905.

161. Rees testified that, "it became difficult for the [Four] Funds to make their regular interest payments." App. Ex. 105 at 913-914.

162. In late 2007, Rees analyzed the Four Funds portfolio and determined that they "were under water by . . . forty million dollars"; in other words, they were worth only about 50% of the amount owed investors. App. Ex. 105 at 914-915. Rees told Smith about the losses in the Four Funds. App. Ex. 105 at 916-917.

163. On December 2, 2007, Smith received an email from Rees showing a $48.8 million deficit in the Four Funds. App. Ex. 108 at 3165-3166.

164. On December 27, 2007, Smith signed a subscription agreement for a $20,000 purchase of a TAIN 7.75% note for an investor named Harold Smith. App. Ex. 174 (GM26). Smith did not alert the investor or his broker to the issues regarding the Four Funds losses or to avoid the sale. App. Ex. 108 at 3168-3169.

165. Smith had access to the bank balances for the Four Funds and could see whether interest payments were being made. App. Ex. 105 at 916.

166. In 2008, interest payments to Four Funds investors were reduced and then eliminated. App. Ex. 121; App. Ex. 122 .

167. Brian Cooper was a senior accountant at MS & Co. from April 2007 to July 2010. App. Ex. 102 at 980. He maintained the Quicken records, reconciled the bank statements, tracked funds in and out of the accounts, and made scheduled payments to investors. App. Ex. 102 at 981-982.

168. At McGinn's direction, however, Cooper testified that certain "preferred investors" received their interest payments while others did not. App. Ex. 102 at 1015-1016. MSTF funds were used to pay the preferred investors. App. Ex. 102 at 1017.

169. Four Funds proceeds, however, as directed by McGinn or Smith, were used to pay MS & Co.'s payroll. See App. Ex. 119; App. Ex. 102 at1021-1023.

170. After the Four Funds were restructured, "they stopped paying interest. There was a preferred bunch of investors that were invested in the Four Funds that were receiving payments from MSTF." App. Ex. 105 at 942; App. Ex. 118. Rees also knew that Four Funds money was moved through MSTF to meet payroll. App. Ex. 105 at 944-945; App. Ex. 119.

171. The Four Funds PPMs did not permit offering proceeds to be used for MS & Co.'s payroll. App. Ex. 107 at 500.

172. Four Funds proceeds were also improperly used to redeem investors in pre-2003 MS & Co. offerings. Cooper kept the books for RTC Trust, a pre-2003 MS & Co. offering. App. Ex. 102 at 982. As a result, he knew that "[t]here was not sufficient money being generated to pay the RTC investors. Money was coming from other sources to pay the [RTC] investors." App. Ex. 102 at 983.

173. When asked if he "mismanaged the assets of the Four Funds," Smith replied that "in hindsight some of my judgments could have been better." App. Ex. 108 at 3169. When asked the same question in his SEC deposition testimony, Smith said "I believe I had some responsibility, yes." App. Ex. 108 at 3170-3171.

2. **McGinn and Smith Misappropriated Investor Funds**

174. McGinn received a total of $1,386,142, and Smith received a total of $1,567,000, from the Trust Offering proceeds. App. Ex. 115 (GA1G). These payments were not authorized by the PPMs for any of the Trust Offerings. The investors did not know that offering proceeds were transferred directly to McGinn and Smith. App. Ex. 109 at 2986. .

175. These unauthorized transfers began in November 2006 with the $3.75 million TDM Cable Trust 06 offering – from which McGinn and Smith received $407,000, and Rogers

received $392,800 –and continued through 2009. App. Ex. 112, 114, 157, 166, 158; App. Ex. 102 at 1004-1005; 996-1001.

176. Smith directed Rees to classify the fees they took from TDM Cable Funding in November 2006 as loans. App. Ex. 105 at 921.

177. Rees learned about the transaction when he saw the wire confirmations. App. Ex. 105 at 923. He was "a little shocked" at the amount of the transactions because it was 33% of a $3 million deal. App. Ex. 105 at 923. Rees considered this "excessively high and didn't seem to jive with my understanding of how origination fees relative to deals would work in that they are typically a couple percent of a deal." App. Ex. 105 at 923-924.

178. Rees initially book them as fees, and saw no evidence they were loans. App. Ex. 105 at 924. Rees subsequently changed to accounting to loans at Smith's instruction. App. Ex. 105 at 927; App. Ex. 143; App. Ex. 357. In 2008, Rees asked when the loan would be repaid, Smith told him that it would be for his "estate to figure out," which Rees understood to mean "there was no real intent to pay it." App. Ex. 105 at 929.

179. Smith instructed Rees to make false accounting entries so that fees taken by Smith, McGinn and Rogers from TDM Cable 06 would be reclassified as loans and therefore not taxable. App. Ex. 105 at 921-922.

3. **Money Was Transferred Between Issuers Depending on Need**

180. When Shea returned to MS & Co. in April 2009, MS & Co. "was failing . . . [t[here was marginally enough capital . . . and their revenues were heavily reliant on related party transactions." App. Ex. 107 at 471. MS & Co. was also having difficulties meeting its net capital requirement due to "lack of revenue, and high expenses." App. Ex. 107 at 472. Shea found approximately 80 entities other than MS & Co. App. Ex. 107 at 475. Shea immediately

became aware of the net capital pressures on MS & Co., and he "personally experienced [this pressure] every month." App. Ex. 107 at at 546.

181. In April 2009, Shea told Smith that the broker-dealer should be shut because "[t]here is not enough money." App. Ex. 107 at 473.

182. Shea knew that Smith and McGinn frequently used funds from one Trust to pay investors in other Trusts. Shea challenged them about this practice because "[i]t would leave investors at risk." Nevertheless, Smith and McGinn continued. App. Ex. 107 at 573.

183. Each of the Trusts had an operating and an escrow account. App. Ex. 105 at 920. Smith and McGinn could move money among the accounts, and McGinn would "very frequently" move money without telling the accounting staff. App. Ex. 105 at 920-921.

184. Rees resigned in April 2009 because "financial pressures on the broker-dealer were causing a lot of stress in my personal life." App. Ex. 105 at 903-904.

185. By 2009, "funds were not there to cover the interest payments. So funds had to be moved in order to make those interest payments to investors." App. Ex. 102 at 992-993.

186. Cooper told McGinn about the dwindling bank account balances. App. Ex. 102 at 993; App. Ex. 161, App. Ex. 163, App. Ex. 164.

187. Cooper testified that "it was stressful that the funds weren't there to cover interest payments . . . there was a lot of pressure on [McGinn] to come up with the funds to make these payments." App. Ex. 102 at 993. McGinn decided where the money would come from the pay investors. App. Ex. 102 at 996; App. Ex. 157 (GG9). See also App. Ex. 102 at 997-1002; App. Ex. 166 (GG30), App. Ex. 158 (GG12) (transfers to McGinn and Smith from Integrated Excellence escrow account).

188. Cooper provided Smith and McGinn with daily information on the bank account balances. App. Ex. 102 at 986-988; App. Ex. 124 (GB10), App. Ex. 126 (GB15); App. Ex. 127 (GB19).

189. Only McGinn and Smith had authority to transfer funds from accounts. App. Ex. 102 at 989 (Cooper). Cooper testified that money was transferred from one trust account to another "[b]ecause the funds were not there to cover the interest payments." App. Ex. 102 at 992 (GA1D) – Integ Excellence transfers to Luxury Cruise Trust 07 and Firstline. App. Ex. 102 at 1005-1006.

190. In an email to McGinn dated February 24, 2009, Smith expressed concerned that MS & Co.'s "net capital will be wiped out" due to inadequate cash flow, and that "if no solution is found in the next couple of weeks we will have to report the net capital violation and more likely than not consider closing our doors." App. Ex. 145.

191. Rees said the financial problems described in Smith's February 24, 2009 email had been occurring since July 2008. App. Ex. 105 at 913.

192. As a result, Smith instructed Rees not to pay certain employees to avoid a net capital violation. App. Ex. 105 at 908; App. Ex. 145.

193. According to Rees, McGinn "very frequently" wired money from the various accounts "without any involvement from the [MS & Co.] staff." App. Ex. 105 at 920.

194. McGinn directed $40,000 of investor fund to be used to pay Matthew Rogers' membership at the Waterville Golf Club in Ireland. App. Ex. 107 at 562; App. Ex. 102 1043-1044; App. Ex. 116.

4. **Fraudulent MSTF Payments**

195. The PPM for MSTF authorized two uses for the money raised in the offering: purchase McGinn Smith preferred stock and bridge financing. Instead, however, McGinn directed payments to certain investors who were not MSTF investors. App. Ex. 107 at 481-482. McGinn also took $230,000. App. Ex. 117.

196. Shea testified that McGinn had directed numerous improper uses of MSTF investor funds, including payments to favored investors. App. Ex. 107 at 484-487. *See also* App. Ex. 134, 135, 136.

197. Rees also testified that MSTF was "used to make payments to investors in other trusts that were being made whole through payments to them from [MSTF]". App. Ex. 105 at 938-939. Rees knew that these payments, which were made at McGinn's instruction, "were not legal, nor authorized by [MSTF's] purpose." App. Ex. 105 at 941

198. Shea knew that McGinn's uses of funds was not authorized by the PPM. App. Ex. 107 at 488.

199. Shea grouped approximately $600,000 the improper MSTF payments into three buckets: (1) payments to Four Funds investors; (2) payments to Joseph Cornacchia, one of McGinn's favored investors; and (3) payments for a "failed investment," SAI Trust. App. Ex. 107 at 488-496; App. Ex. 118; App. Ex. 123.

200. McGinn told Shea that the payments to Cornacchia were "to keep Joe happy . . . to avoid an arbitration." App. Ex. 107 at 633. App. Ex. 105 at 944 (Rees testimony that McGinn directed $5,000 per month payments to Cornacchia). App. Ex. 128 at 1 (schedule of payments to Cornacchia), at 2 (payments to favored Four Funds investors), at 3 (payments to non-MSTF investors with MSTF funds) App. Ex. 209 at 2967-2968.

201. In April 2009, Shea told Smith that non-MSTF investors were being paid with MSTF funds. App. Ex. 107 at 496. Shea testified that Smith told him that he knew that McGinn was doing that and that "it wasn't allowed by the private placement [memorandum]." App. Ex. 107 at 497. *See also* App. Ex. 137; App. Ex. 107 at 577-584 (MSTF).

202. Rees maintained the financial records for MSTF. 938. He noticed payments to McGinn from the escrow accounts. App. Ex. 105 at 938-939; App. Ex. 117.

203. The MSTF escrow account was "used to make payments to investors in other trusts that were being made whole through payments to them from [MSTF]." App. Ex. 105 at 938-939. Rees knew these payments "were not legal, not authorized by [MSTF's] purpose." App. Ex. 105 at 941.

204. MSTF funds were used to pay MS & Co.'s payroll. App. Ex. 105 at 944-945. MSTF also was "used to make payments to investors in other trusts that were being made whole through payments to them from [MSTF]" App. Ex. 105 at 938-939. Rees knew that these payments, which were made at McGinn's instruction, "were not legal, nor authorized by [MSTF's] purpose." App. Ex. 105 at 941.

205. After the Four Funds were restructured, "they stopped paying interest. There was a preferred bunch of investors that were invested in the Four Funds that were receiving payments from MSTF." App. Ex. 105 at 942; App. Ex. 118. Rees also knew that Four Funds money was moved through MSTF to meet MS & Co.'s payroll. App. Ex. 105 at 944-945; App. Ex. 119.

206. Cooper testified that the payments to preferred investors "[weren't] correct . . . [b]ecause these investors invested together as a group of investors. And if some are discontinued not receiving interest payments, they all should not be receiving interest payments." App. Ex. 102 at 1020.

207. In April 2009, Smith and McGinn owed MSTF investors $140,000 in interest payment. App. Ex. 125. To pay the investors, Smith and McGinn took money from TDMM Cable Junior Trust 09 ($53,000), FIIN ($25,000), TDM Luxury Cruise ($10,000), without telling the MSTF investors or the investors in the other offerings. App. Ex. 109 at 2964-2965.

208. On October 9, 2009, McGinn and Smith met with Jay Kaplowitz, MS & Co.'s attorney, for 90 minutes. App. Ex at 370 at 727. They told Kaplowitz "that they had taken monies from some of the funds and used them as advances for other of the funds," and asked him if he "could come up with a solution." App. Ex. 370 at 728.

209. Kaplowitz told them that "what you did was wrong," and that they should "make a settlement amongst all the partners." App. Ex. 370 at 729.

210. On October 10, 2009, Smith faxed to Kaplowitz a twelve-page handwritten letter. App. Ex. 129; 130, 131;132; 107 at 541-550. The letter stated that "[s]tarting in late 2007, the [Four] FUNDS began to realize a shortfall of income sufficient to meet the debt obligations of the FUNDS due to the under performance of its loans and investments." App. Ex. 129 at 2, 130 at 2.

211. The letter stated that "it is apparent to us that there is no place in the PPM of MSTF that permits fees payable to MS. Why we booked fees that are clearly owed by the Funds to MSCH and MSA and then ran them through the books of MSTF is absolutely inexplicable and incredibly stupid." App. Ex. 129 at 6; 130 at 6; 108 at 3189.

212. Smith's letter to Kaplowitz also acknowledged that "arbitrations, in addition to questions that arose during a FINRA routine audit in the fall of 2008, have sent FINRA on a never-ending request for information. . . . Tim and I have sat with an on-the-record, OTR, interview with FINRA in April 2009. In June of 2009, FINRA sent six auditors to our offices to

review the Funds. We have supplied them with approximately 30,000 pages of documentation and over 20,000 emails. On September 30, 2009, FINRA asked for additional information for a large number of related entities, some going back to 1982. In preparing the documentation, we became aware that we had run a number of related transactions through MSTF that were specific to the interests of MS affiliates and its principals. And because of outside investment in MSTF, the use of MSTF as the transaction vehicle was most likely improper. In addition, the documentation supporting these transactions was either unavailable or not up to date. Realizing the possibility that the appearance of these transactions could be interpreted as the improper use of investor funds, or the commingling of funds, we have sought your counsel on how to rectify this mistake." App. Ex. 129 at 3-4; 130 at 3-4.

213. Smith's letter also referred to "advances from MSTF to McGinn Smith & Co.", which Shea testified were "fees paid . . . [for which] there was no commercial reason or wasn't allowed for in the private placement [memorandum]." App. Ex. 107 at 541.

214. The letter also acknowledged the payments to favored customers and stated that this was "where the major risk is. There is no support or plausible reason why monies from MSTF were used to pay clients of the firm." App. Ex. 129 at 6; 130 at 6.

215. These notes discuss paying back funds to MSTF, and state that "Jay has expressed a concern that repaying the monies at the same time as we are being asked to provide financial files looks like a cover-up." App. Ex. 129 at 7; 130 at 7.

216. Kaplowitz testified that he "thought what they did was wrong and they would be drawing attention to it." App. Ex. 370 at 737. App. Ex. 133 (GB34) (additional fax). Kaplowitz also testified that "I have never received a letter from a client admitting to a crime, to what I felt was a crime, at least." App. Ex. 370 at 739.

217. Kaplowitz told Smith and McGinn "that they couldn't alter the records to reflect another way of accounting for the advances they took out." App. Ex. 370 at 740-741.

218. Shea falsified the accounting records on October 12, 2009. Two days later, the falsified records were sent to FINRA. App. Ex. 168; App. Ex. 107 at 534-535.

219. In a letter dated November 16, 2009, Shea, at Smith's direction, forwarded the backdated promissory notes to FINRA. App. Ex. 107 at 563; App. Ex. 169. The notes were prepared on November 2, 2009, although they reflect transactions from 2006. App. Ex. 107 at 564-565.

5. **Smith Directed that Accounting Entries be Falsified**

220. Smith told Shea to make accounting entries to conceal the fact that MS & Co. was failing, such as not properly accruing expenses such as salaries, legal fees relating to arbitrations, and rent on the NYC office. App. Ex. 107 at 472-473.

221. Smith also directed Rees to manipulate MS & Co.'s financial records to avoid a net capital violation by not accruing liabilities for a particular month. App. Ex. 105 at 909-910.

222. In the Fall of 2009, Shea and Smith discussed the MSTF payments and the Four Funds payroll payments. App. Ex. 107 at 500. Smith told Shea "to create certain accounting transactions that would disguise the nature of all these payments." App. Ex. 107 at 501. Shea created the false accounting entries as directed by Smith. App. Ex. 107 at 503-510, 531, 552-556 552 (Shea: "I created false accounting entries" to hide the money that McGinn and Smith were taking); App. Ex. 120; 135; 134 . When Shea questioned Smith, Smith said "this is my money . . . I can do with it whatever we want. Go ahead and make the entries." App. Ex. 107 at 532.

223. In October 2009, Shea received a handwritten notes from Smith that was Smith's "master plan to how to address all these [MSTF] transactions." App. Ex. 107 at Tr. 519. In this

document, Smith listed the transfers by the Four Funds to MSTF. App. Ex. 107 at Tr. 520-21; App. Ex. 136 at 8.

224. In these notes, Smith wrote that "we obviously should not have used MSTF as our personal bank, but [McGinn] had access to the cash." App. Ex. 136 at 9.

6. **McGinn and Smith Concealed the Firstline Bankruptcy from the Brokers**

225. In the four Firstline offerings, MS & Co. raised money from investors that was loaned to Firstline, Inc., an alarm company in Utah. App. Ex. 107 at 571.

226. On August 8, 2007, Firstline's CEO notified McGinn that "[w]e have been notified by ADT by letter and email that they allege we are in breach of our ADT Dealer Agreement." App. Ex. 148. And on October 7, 2007, the allegation was repeated along with the fact that "ADT may seek damages that would exceed $7.5 million." App. Ex. 149 at 7. McGinn never included this material information in the Firstline PPM. App. Ex. 109 at 2920.

227. In late 2007, Firstline engaged MS & Co. to advise it in negotiations with ADT. App. Ex. 150 at 2; App. Ex. 109 at 2890-91

228. Firstline filed for bankruptcy on January 25, 2008, and McGinn found out about the filing almost immediately. 2887. After the bankruptcy filing, Firstline did not make any further payments. App. Ex. 109 at 2910.

229. McGinn and Smith knew about the bankruptcy, that the bankruptcy meant that Firstline could not make the loan payments, and that it was necessary to "continue making payments out of other accounts to fund that interest stream due investors" App. Ex. 105 at 946-947 (Rees).

230. On February 6, 2008, Shea emailed McGinn that due to the bankruptcy filing "the Trusts would not receive any cash until the bankruptcy plan is approved which could be 5 to 9

months! . . . [W]e have to either suspend investor payments or cover them from other sources." App. Ex. 151.

231. McGinn concealed the bankruptcy filing from MS & Co.'s brokers, who continued to offer and sell Firstline. App. Ex. 109 at 2888, 2891. . The bankruptcy was material information that the investors did not have. App. Ex. 109 at 2888.

232. There was a total of $670,979 post-bankruptcy sales. App. Ex. 147

233. McGinn made the decision to keep paying Firstline investors for another 21 months after the bankruptcy. App. Ex. 109 at 2911. McGinn used approximately $2 million taken from other trusts to pay Firstline investors. App. Ex. 109 at 2911-2912; App. Ex. 111.

234. The Firstline PPM states that investors would be paid from monitoring payments received by the Trust, and not from whatever source was available. App. Ex. 67-68; 70-71; 109 at 2915-2918.

235. McGinn signed subscription agreements for post-bankruptcy sales of Firstline, but never told the broker or the customer about the bankruptcy. App. Ex. 109 at 2895-2899.

236. Guzzetti sent 31 post-bankruptcy emails, that McGinn received, notifying brokers that Firstline was available for sale. App. Ex. 146. *See also* App. Ex. 109 at 2899-2901;144. McGinn never told the brokers to stop selling Firstline. App. Ex. 109 at 2901.

237. McGinn directed the transfer of $97,000 from Integrated Excellence to pay Firstline investors. App. Ex. 113; 109 at 1006-1007; 159; 160.

238. McGinn made the decision to continue paying Firstline investors with MSTF funds. App. Ex. 107 at 574. This was not a permitted use of funds under the MSTF PPN. App. Ex. 107 at 574-575.

239. McGinn emailed an MS & Co. broker on February 8, 2009, to say the "[e]verything OK with . . . Firstline." App. Ex. 152;109 at 3043-3044.

240. McGinn directed transfers to Firstline and other accounts so investors could be paid. App. Ex. 102 at 1013-1014; App. Ex. 155-155.

241. On August 4, 2009, at McGinn's direction, $67,000 was diverted from TDM Verifier Trust 07R escrow account to pay Firstline investors. App. Ex. 111.

242. Pursuant to an Agreement dated May 15, 2008, "MSTF has agreed to assume the obligations of Firstline to pay principal and interest to the Trusts pursuant to the terms of the PPM's." App. Ex. 138 (GB52). McGinn signed the Agreement for MSTF and Smith signed for the Firstline Trusts. App. Ex. 138; App. Ex. 107 at 577.

243. Many Firstline sales were made after the May 15, 2008, agreement was signed. Ap. Ex. 147; 109 at 2924-2925. The May 15, 2008 agreement, however, was not executed until June 2, 2009. 2926. McGinn and Smith never told the brokers about the June 2009 agreement, which sold the underlying income stream from the trusts to MSTF. App. Ex. 109 at 2929-2930.

244. McGinn and Smith had ongoing discussions about whether to tell the brokers about the bankruptcy. App. Ex. 109 at 2927-2928.

245. McGinn knew that it would be harder to sell MS & Co. products once the bankruptcy was disclosed. App. Ex. 109 at 2933.

246. Cooper knew that McGinn made decisions about paying Firstline investors, and other offerings, from other sources. App. Ex. 102 at1006-1007; App. Ex. 159, 160, 165.

247. Rees knew that Firstline investors were being paid by other entities. App. Ex. 105 at 947.

248. Investors were not told about the Firstline bankruptcy until they were sent a letter dated September 10, 2009, which McGinn signed as Chairman of MS Capital Holdings. App. Ex. 156 ; App. Ex. 109 at 2919. McGinn's letter attached a memorandum from MS & Co.'s in-house counsel, which stated that "Firstline concealed from [MS Funding] that it was embroiled in a massive disagreement with ADT." App. Ex. 156 at 2.

249. Firstline did not conceal the ADT issue from McGinn. *See supra* ¶¶ 225-228.

250. The letter to investors also states that "[MS] Funding was able to secure immediate financing, securities by its Firstline receivables in order to have funds available to make monthly payments due to its lenders." App. E. 156 (GF41). In fact, the money to pay Firstline investors came from investors in other Trust Offerings. App. Ex. 109 2922-2923; App. Ex. 138.

7. The Trust Offerings Were Driven By the Need For Cash to Prolong the Scheme

251. In Smith's February 24, 2009, email to McGinn, he acknowledged that "[w]e have been living on the edge for some time, and Tim's deals have kept us alive by fronting our profit." App. Ex. 145.

252. Rees testified that McGinn "was sending money from some of these trust LLC entities that [were] created in the form of advanced profits that were sent to [MS & Co.], and we were using that to get cash in the door." App. Ex. 105 at 910. Rees said that "we couldn't live like that forever, but it got us through another payroll run." App. Ex. 105 at 911.

253. Shea assisted Smith and McGinn in the preparation of personal financial statements. App. Ex 107 at 567. Shea testified that McGinn had "a very high level of personal expenses . . . there was always pressure to get deals closed to get money. . . . his paycheck was nowhere near enough money . . . his monthly burn rate was somewhere between thirty and forty

thousand dollars a month . . . the private placements were pulled together very quickly . . . if there was any review from legal, Joe Carr, it may have been, you know, brushed aside in the sake of speed." App. Ex. 107 at 569-70.

8. **The FINRA Examinations**

254. The FINRA examination that Smith referred to in his letter to Kaplowitz began in October 2008, when Steven Rowen and Christopher Rattiner, Principal Examiners with FINRA, conducted a cyclical examination of MS & Co. App. Ex. 106 at 361, 367; 104 at 435. This review lasted five weeks, and covered MS & Co.'s net capital violations, and private placements. App. Ex. 106 at 367-368. At the completion of the 2008 exam, FINRA and Smith attended and exit conference. App. Ex. 106 at 379.

255. Based on areas that were noted during the 2008 exam, FINRA conducted investigative testimony of Smith and McGinn on April 29, 2009. App. Ex 106 at 381.

256. FINRA conducted a for-cause exam of MS & Co., as well as a cyclical exam, that began in June 2009 and continued through September 2009. App. Ex 106 at 381-2.

257. The Four Funds were a focus of the 2009 exam. App. Ex 106 at 383; 104. FINRA also saw evidence of payments to and from L. Smith. App. Ex. 104 at 430.

258. In addition, FINRA learned that in late 2006 TDM Cable Funding had transferred approximately $1 million to Smith, McGinn and Matthew Rogers. App. Ex. 106 at 384; 104 at 440. In early September 2009, FINRA personnel, including Rowen and Rattiner, met with Smith and McGinn to ask about the transfers. App. Ex. 106 at 386. At this meeting, Rowen testified that "Mr. Smith responded that these were fees, and then immediately Mr. McGinn jumped in and noted that these were loans." App, Ex. 106 at 388; 104 at 442-444. FINRA then sent a letter

asking for "all documentation related to the "loans" to Smith, McGinn and Rogers. App. Ex. 167.

259. Cooper testified that the environment during the FINRA exam was "stressed," there was "a lot of pressure from FINRA to get answers," and there was no documentation regarding the "loans" taken by McGinn and Smith. App. Ex. 102 at 1024-1025.

260. Shea testified there was "overriding fear . . . FINRA was obviously all over us . . . there may be legal problems down the road." App. Ex. 107 at 669. Smith told Shea to mark documents as "Attorney/Client Privilege" so "than in the event that they were seized, they couldn't be used against any of us." App. Ex. 107 at 669.

261. McGinn and Smith told Cooper to create a loan document that would then be given to an assistant to create the promissory note. App. Ex. 102 at 1026-1027, App. Ex. 139.

262. Cooper collected the information on the loans. App. Ex. 102 at 1028-1029; App. Ex. 142. The backdated promissory notes were all prepared and executed in November 2009 after FINRA requested them, although they purported to reflect transactions from 2006. App. Ex 102 at 1025, 1038, 1040; GD16, GD18. Smith signed the backdated promissory notes in early November 2009. App. Ex 108 at 3229.

263. On November 2, 2009, at Smith's direction, Shea forwarded to FINRA documents purporting to be the loan agreements pertaining to the 2006 loans. App. Ex. 106 at 398-401, 411, 433, 449. App. Ex. 169, 170, 171, 172.

264. In late 2009, after several arbitral awards were made against MS & Co., FINRA informed MS & Co. that it was not in compliance with FINRA's net capital requirements. App. Ex. 106 at 417; App. Ex 104 at 453.

9. **Smith's 1999 Letter to McGinn**

265. In 1999, Smith wrote a 26-page handwritten letter to McGinn. App. Ex. 108 at 3154. Smith kept the letter in his home office, where it was seized in 2010 when a search warrant was executed.[2] App. Ex. 108 at 3153.

266. In this letter, Smith described the serious financial problems facing the pre-2003 trust offerings, which mirrored the problems that arose later. In the letter, Smith wrote to McGinn: "The business has become addicted to the cash flow from the trust business and without them we will have a difficult time surviving. The default of the trusts will drastically reduce revenues, cause us to lose brokers, and at least their confidence in us, bring on crushing litigation, and devastating publicity, and I am convinced prosecution by regulators or worse. The impact on our employees, customers, friends, and family will be devastating." App. Ex. 108 at 3156

267. Smith also wrote: "I, unlike you, feel that we are vulnerable to criminal prosecution." App. Ex. 108 at 3156.

268. Smith also wrote to McGinn, " While you have previously rejected my characterization of these acts as similar to a 'Ponzi' scheme because new dollars being raised are in fact buying new product and only 'profit dollars' are being used to cover shortfalls. I believe our actions could be defined otherwise. The reason for my beliefs is that we are now in possession of indisputable empirical evidence that the new investments have no chance of being

[2] Portions of Smith's 1999 letter were read to the jury during the criminal trial, but the letter itself was not admitted. The letter, however, has been used in the SEC case. *See* Dkt. 117. Accordingly, the SEC submits the letter as well as a typewritten version prepared by the US Attorney's Office. App. Ex. 54, 55.

repaid in full. Whether less than 100% collections (66%) is due to normal attrition, fraud, billing errors, or poor credit judgment, it really does not matter. The facts are that we will never collect 100% or close to it. Therefore, our 'profits' which we use are not profits at all, but rather monies that should be held in reserve to allow for the deficit collections for the protection of the new investors." App. Ex. 108 at 3159-3160.

269. Smith also wrote to McGinn, "For us not to allow for these deficits by setting up adequate reserves is, in my judgment, bordering on fraud. Certainly by not disclosing in the prospectus our poor history of collections, we are not providing the prospective investor an accurate picture of his risk. We both know why we don't make that disclosure–because such disclosure would cause our salesmen to cease selling and investors to cease buying. Thus, we are misleading both our own employees and customers. Distributions to Tim and Dave going forward should be eliminated. Not only should those monies be set up as reserves for investor protection, but in future litigation, those distributions would be extremely detrimental to us. Hard to justify investors losing half their money while we continue to prosper at compensation levels that would seem obscene to the average citizen sitting in judgment." App. Ex. 108 at 3161-3162.

C. Misrepresentations and Omissions to Investors

1. Thomas Brown

270. Thomas Brown was a New York State employee whose goal was "investing for retirement, strictly for retirement." App. Ex. 90 at 1701

271. Brown purchased a $25,000 TAIN five-year junior note in November 2004. 1705. Based on the PPM, Brown expected to receive quarterly interest payments, and his principal back in 2009. App. Ex. 90 at 1709.

272. Brown believed that his money would be used consistently with "Use of Proceeds" section of the PPM. App. Ex. 90 at 1710. Brown expected that all fees would be disclosed in the PPM, did not expect that his investment would be used to pay MS & Co.'s payroll. App. Ex. 90 at 1710-1711.

273. Brown also invested $10,000 in Firstline Senior Trust 07 in November 2007. App. Ex. 90 at 1712. Brown believed that his money would be used consistently with the PPM, and did not know that McGinn or Smith were planning to use $300,000 to pay themselves. That information would have been important to Brown in making his investment decision. App. Ex. 90 at 1714-1715.

274. Brown did not know that prior to making his investment, ADT had threatened a multi-million dollar lawsuit against Firstline Security, Inc., and that information would have been significant to him. App. Ex. 90 at 1716.

275. Brown's interest payments stopped and he has not received his principal back. App. Ex. 90 at 1718.

2. **Avram Cahn**

276. Cahn, an attorney from New York City, invested a total of $35,000 in Firstline Trust 07 on November 5, 2007, and another $25,000 on April 25, 2008. App. Ex. 91 at 1409-10.

277. At the time he made his investment, Cahn thought his investment would be used consistently with the PPM. App. Ex. 91 at 1413.

278. It would have been important for Cahn at the time to know that Smith and McGinn used more than $300,000 for themselves. App. Ex. 91 at 1414.

279. At the time of his April 2008 investment, Cahn did not know about the ADT lawsuit, and that information would have been important to him at the time. App. Ex. 91 at 1415.

280. Cahn received the September 10, 2009 letter. App. Ex. 91 at 1417. Cahn did not know that other MS & Co. entities were paying the Firstline investors. App. Ex. 91 at 1418.

281. Cahn has not received back his principal form his Firstline investment. App. Ex. 91 at 1418-1419.

3. **Henry Crist**

282. Crist is a doctor who lives in Hershey, PA. 1725. Around 2004, Crist was looking for an investment that was "perfectly secure because I was 64 at the time." App. Ex. 92 at 1726.

283. In October 2007, Crist purchased a $75,000 Firstline junior note, and in January 29, 2008, he purchased another $30,000 Firstline note. App. Ex. 92 at 1728.

284. Crist assumed the investments were being handled consistently with the PPMs, and it would have been important to Crist to know that McGinn and Smith used more than $300,000 in investor funds to pay themselves. App. Ex. 92 at 1732.

285. Crist did not know that a source other than the alarm contracts was paying investors, and it would have been significant to him to know that. App. Ex. 92 at 1733-1734.

286. Crist has not received back his principal. App. Ex. 92 at 1737.

4. **Mary Dale**

287. Dale is a retiree who lives in Florida, who worked for 48 years as a registered nurse. App. Ex. 93 at 1382. Her investment goal was "[t]o be able to retire and live in the manner in which I had been accustomed." App. Ex. 93 at 1384.

288. In December 2007, Dale invested $50,000 in a 4-year Firstline note. App. Ex. 93 at 1386.

289. Dale thought her money would be invested consistently with the PPM. App. Ex. 93 at 1390. She did not know that Smith and McGinn were planning to take $300,000 of investor proceeds, and it would have been important to her to know that. App. Ex. 93 at 1391.

290. Dale also did not know about the ADT lawsuit, or that her payments would be coming from another MS & Co. entity; it would have been important to her to know those things. App. Ex. 93 at 1392-1393.

291. Dale has not received her principal back. App. Ex. 93 at 1397.

5. **Robert DeLeonardis**

292. Ronald DeLeonardis was a high school classmate of McGinn's and they later served in the Army reserves together. App. Ex. 94 at 674.

293. In 2002, DeLeonardis sold the restaurant he had owned and operated in Albany for 34 years. App. Ex. 94 at 674, 676. DeLeonardis "acquired a large amount of money" from the sale, and his "intention was to invest money so that I could retire and make a lot of money and help my children out, as well as being able to enjoy somewhat of the life that I felt I deserved because of all the hard work and sacrifice I had put it." App. Ex. 94 at 676.

294. At McGinn's recommendation, DeLeonardis invested in a total of $170,000 in two five-year junior FIIN notes, that were expected to pay 10.25% quarterly interest. GM43, GM44.

295. DeLeonardis has not received back any of his principal. App. Ex. 94 at 682. Interest payments were made through 2007. App. Ex. 94 at 682. He received $1,250 in interest in 2008"and then the payments stopped." App. Ex. 94 at 682.

296. DeLeonardis believed that his investment would be used in accordance with the terms of the PPM. App. Ex. 94 at 684-685. Based on the PPM, DeLeonardis would have been "shocked" to know that investor funds would be used to meet MS & Co. payroll in 2008. App. Ex. 94 at 684-685; GC1.

297. DeLeonardis testified that he did not believe that FIIN was a risky investment because of "[t]he trust we built over twenty years of investment, I have to rely on their knowledge." App. Ex. 94 at 691-692.

6. **William Ferraro**

298. William Ferraro was an administrator with Empire State College for 34 years. App. Ex. 95 at 696. Smith was a member of the college's foundation, and worked with Ferraro in that capacity. App. Ex. 95 at 696-697.

299. Around 2006, Ferraro started discussing his retirement assets with Smith. 698. On April 8, 2009, Ferraro invested $100,000 with TDM Verifier Trust 07R. App. Ex. 95 at 700; GM10, GA19. He has not received his principal back. App. Ex. 95 at 705. Ferraro believed that his investment would be sued consistently with the terms of the PPM. App. Ex. 95 at 704-705. Ferraro did not know that this investment would be used to pay Firstline investors, and would not have invested had he known that. App. Ex. 95 at 705.

300. On September 25, 2008, Ferraro invested $200,000 with Firstline Trust 08. App. Ex. 95 at 706; GM9. He has not received his principal and interest back. App. Ex. 95 at 709. Ferraro expected that investor funds would be used in accordance with the PPM. App. Ex. 95 at 708; GA13. He would have wanted to know that MS & Co. was taking more than the 6% in fees disclosed in the PPM, and would not have made the investment had he knows. App. Ex. 95 at 709.

301. In September and October 2008, Ferraro invested a total of $175,000 with MSTF. GM35, GM36, App. Ex. 85 (GB2). He has not received his principal back. App. Ex. 95 at 715.

302. Ferraro expected that his investment would be handled consistently with the PPM. App. Ex. 95 at 713. He testified that it would have been important for him to know that MS & Co. had taken more in fees than set forth in the PPM, and that MSTF funds would be used to pay Firstline investors. App. Ex. 95 at 714-715.

303. Ferraro testified that "I put a lot of faith and trust in what David [Smith] was telling me about these things, and they sounded good. And so I went along with the investment." App. Ex. 95 at 710.

7. **Andrew Greenberg**

304. On December 21, 2007, Greenberg invested in TDM Verifier Trust 08. 2033. Greenberg received the PPM, and would have wanted to know if McGinn and Smith were taking money other than as disclosed in the PPM. App. Ex. 96 at 2035.

305. Greeenberg also invested $20,000 in a three-year Fortress Trust note. App. Ex. 96 at 2036. Greenberg expected that his money would be invested as described in the Fortress Trust PPM. App. Ex. 96 at 2037.

306. Greenberg did not know that McGinn and Smith would take more than $800,000 to pay themselves and another person, which is information that would have been important to know when making the investment. App. Ex. 96 at 2038-2039.

307. Greenberg also invested $20,000 in TDM Cable Trust 06. App. Ex. 96 at 2040. Greenberg did not think his investment would be used for purposes other than as set forth in the PPM, and did not know funds from this offering would be used to pay Firstline investors. App. Ex. 96 at 2041.

308. Greenberg also invested a total of $50,000 in MSTF. App. Ex. 96 at 2049. Greenberg never knew that Smith and McGinn were planning to take $250,000 above and beyond the fees in the PPM. App. Ex. 96 at 2051. In late 2009 or early 2010, Greenberg spoke with Smith and McGinn and asked that his MSTF investment be returned. They told Greenberg that the MSTF money was "invested in a number of things, such as "a cruise ship" and "a security company in New York." 2056. Smith and McGinn did not disclose that MSTF was paying up to $3 million to Firstline investors. App. Ex. 96 at 2057-2058, App. Ex. 138 (GB52).

8. **Berta Kogan**

309. Kogan is a retired employee of the New York Police department. In July 2007, Kogan invested $300,000 in a four-year TDM Luxury Cruise Trust 07. App. Ex. 97 at 1432. She did not receive her principal back at maturity. App. Ex. 97 at 1433.

310. Kogan expected that her money would be used consistently with the PPM. App. Ex. 97 at 1435. She did not know that TDM Luxury Cruise Trust funds would be used to pay Firstline investors. App. Ex. 97 at 1435.

311. In April 2008, Kogan invested $150,000 in a four-year Firstline note. App. Ex. 97 at 1436. She expected the investor funds would be sued consistently with the PPM, and she did not know that McGinn and Smith were planning to take $300,000 for themselves. App. Ex. 97 at 1438. That information would have been very significant to het. App. Ex. 97 at 1438-1439.

312. Kogan also did not know about the Firstline bankruptcy or that her payments were coming from other MS & Co. entities, and that information would have been important to her at the time. App. Ex. 97 at 1440. She has not received her principal back. App. Ex. 97 at 1441.

9. **Stephen Novack**

313. Novack, a commodities trader in New Jersey, purchased a five-year $25,000 Integrated Excellence note in August 2008. App. Ex. 98 at 1548-1549.

314. At the time of his investment, Novack believed that his funds would be used in accordance with the PPM, and not for other undisclosed purposes. App. Ex. 98 at 1551.

315. Novack did not know that McGinn and Smith would use $97,000 of funds raised through the Integrated Excellence offering to pay Firstline investors. App. Ex. 98 at 1552.

10. **Robert Pugliese**

316. Pugliese is retired from a military career. App. Ex. 99 at 1563. In July 2007, Pugliese invested a total of $25,000 in two four-year TDM Luxury Cruise notes. App. Ex. 99 at 1567.

317. Publiese expected that his investment would be used consistently with the PPM. App. Ex. 99 at 1569. In November 2007, Pugliese also invested $25,000 in Firstline in November 2007, and another $55,000 in June 2008. App. Ex. 99 at 1570-1571.

318. His subscription agreement was signed by Smith on June 10, 2008. App. Ex. 99 at 1571.

319. Pugliese believed that his investment would be used consistently with the PPM, and he would have wanted to know that Smith and McGinn were taking $300,000 for themselves. App. Ex. 99 at 1572-1573.

320. When Pugliese made his June 2008 investment in Firstline, he did not know that Firstline had filed for bankruptcy, and that information would have been significant to him at the time. App. Ex. 99 at 1574.

321. Pugliese has not received his principal back. App. Ex. 99 at 1575.

11. **Paul Sokol**

322. Sokol is a self-employed home builder. In April 2009, Sokol invested a total of $75,000 in a TDMM Cable Trust 09 five-year note. App. Ex. 100 at 1589. These funds represented Sokol's savings for his son's college education. App. Ex. 100 at 1589.

323. Sokol never received any of the interest payments or principal. App. Ex. 100 at 1590.

324. Sokol expected that his investment would be used according to the PPM. App. Ex. 100 at 1592. Sokol never knew that $30,000 in investor funds would be taken by McGinn, which was information he would have wanted to know before making the investment. App. Ex. 100 at 1593.

12. **Monsignor Robert James Wargo**

325. Wargo is the pastor of St. Joseph's Church in Orefield, PA, and was also in charge of the finance committee at the church. App. Ex. 101 at 2068-2069.

326. The church invested $40,000 on Integrated Excellence Senior Trust 08. App. Ex. 101 at 2070. Wargo expected that the funds raised in the offering would be used consistently with the terms of the PPM. App. Ex. 101 at 2071-2072.

327. Wargo did not know that McGinn and Smith would take an additional $85,000 in fees beyond what was described in the PPM. App. Ex. 101 at 2073; GA1C. Wargo also expected that the interest would come from the investments described in the PPM, and not from sources unrelated to the investment. App. Ex. 101 at 2073-2074.

328. The church also invested in TDMM Cable Senior Trust 09. 2075. At the time of the investment, Wargo thought that that investor proceeds would be used as described in the PPM, or that money from this issuer would be paid to investors in Integrated Excellence. App. Ex. 101 at 2077. This information would have been significant to know. App. Ex. 101 at 2077.

D. The Four Funds Offerings Were Not Registered

329. The Four Funds PPMs made clear that the "notes are being offered only to 'accredited investors,' as that term is defined by Regulation D under the Securities Act . . . who . . . have the expert knowledge to evaluation information and data." *See, e.g.*, App. Ex. 85 at 3; *see also id.* at 10 ("[s]ubscriptions will be accepted only from 'accredited investors'"), at 23 ("[e]ach investors must represent in writing that it qualifies as an 'accredited investor' . . . and must demonstrate the basis for such qualification").

330. In order to purchase a Four Funds note, a subscriber had to sign a subscription agreement attesting that she was an accredited investor. *See, e.g.*, App. Ex. 86 at 38.

VII. DAVID SMITH JOINTLY OWNED AND CONTROLLED THE STOCK ACCOUNT

A. The Stock Account Was Funded from a Joint Stock Account

331. On April 20, 2010, the Court entered a temporary restraining order freezing the assets in a stock account in the name of L. Smith maintained at RMR Wealth Management, LLC containing $1,786,430.01 in assets as of April 30, 2010 (the "Stock Account"). App. Ex. 344 (TRO dated April 20, 2010, Dkt. No. 5); App. Ex. 341 (RMR 6004-6012).

332. On July 8, 2010, the Court granted the Commission's motion for a preliminary injunction freezing the assets in the Stock Account pending resolution of this action. App. Ex. 345 (July 8, 2010 MDO, Dkt. No. 86 at 7-10; 42).

333. In opposing the freeze of the Stock Account, L. Smith stated that the assets in the Stock Account originated solely from a stock account worth approximately $60,000 that she received as part of an inheritance from her father in 1969. App. Ex. 244 (L. Smith 5/21/10 Aff., Dkt. 23), at ¶ 13-14; 170. L. Smith stated that the stock account has always been her "separate property" and has "always been held in my name and my name alone." App. Ex. 244 (L. Smith 5/21/10 Aff. Dkt. 23, at ¶ 17).

334. L. Smith stated that the Stock Account was always kept separate from David Smith's assets, and that the account did not receive any additions to principal from David Smith from his personal or business activities or from any other sources but instead grew solely through David Smith's management and investment returns on the original inheritance. See, e.g., App. Ex. 244 (Lynn Smith 5/21/10 Affidavit, Dkt. 23, at ¶ 17-18); App. Ex. 252 (Lynn Smith 5/27/10 Deposition at 102:13-21).

335. These statements were all false. See below.

336. In 1973, L. Smith used an unspecified portion of the stock account inherited from her father to make a down payment on the Smiths' primary residence in Clifton Park. App. Ex. 244 (Lynn Smith 5/21/10 Affidavit, Dkt. 23, at ¶ 15).

337. L. Smith stated that at some point the stock account she inherited from her father was as low as $10,000. App. Ex. 252 (Lynn Smith 5/27/10 Deposition at 33:11-22).

338. The Stock Account, in the name of L. Smith, Account No. 405-04091, was opened on November 21, 1991 with Bears Stearns as the clearing broker. App. Ex. 343 (MGS DOJ 000164-165); App. Ex. 264, 263 (MGS DOJ 000138 (Report of New Account dated November 11, 1991)).

339. On that date, David and L. Smith transferred all cash and securities from a joint stock account in both their names to the Stock Account. App. Ex. 284 (MGS DOJ 000242).

340. Prior to the opening of the Stock Account, the joint account, No. 405-00065, was the only brokerage account holding the Smiths' cash and marketable securities, aside from small IRA accounts. App. Ex. 284 (MGS DOJ 000242).

341. The Stock Account was managed by David Smith through the McGinn Smith brokerage firm until 2010, when the Stock Account was transferred to RMR Wealth Management after McGinn Smith ceased doing business. See, e.g., App. Ex. 341 (RMR 6004-6012); App. Ex. 221 (MGS DOJ 000185) and App. Ex. 222 (MGS DOJ 000226); App. Ex. 255 (Lynn Smith Answer to SAC, ¶ 114).

342. Prior to the opening of the Stock Account on November 21, 1991, the Smiths' financial statements reported that all the securities they owned were either owned by David Smith or owned jointly by David and L. Smith. See below.

343. David and L. Smith had joint financial statements prepared on at least twenty-one different dates between September 1984 and August 2008. See App. Exs. 181-187, 189, 192, 194, 197, 200, 203, 206-210 (Smiths' Financial Statement from 1984 through 2008).

344. The Smiths' financial reports were sent to regulators at the Pennsylvania Department of Insurance and regulators in Texas. App. Ex. 108 (D. Smith testimony in U.S. v. Smith et al. at Tr. 3224).

345. The Smiths' joint financial statement as of September 30, 1984 report that Mr. Smith owned securities with a market value of $144,348App. Ex. 181 at 4.

346. The Smiths' joint financial statement as of December 31, 1985 report that the Smiths' owed a liability on a short stock position, but held no securities. App. Ex. 182.

347. The Smiths' joint financial statements for 1986, 1987 and 1989 report no securities held by either Smith. App. Exs.183-185.

348. The Smith's joint financial statement as of June 1, 1990 report that they jointly held cash and securities totaling $298,000. App. Ex. 186.

349. The cash and securities contained in the June 1, 1990 financial statement are not reported as owned solely by L. Smith. App. Ex. 186.

350. The Smiths' joint financial statement dated April 1, 1991 reports cash and securities totaling $302,000. App. Ex. 187 at 2.

351. The first available statement for the Stock Account, dated March 3,1992, reports a balance of $446,449 in cash and securities as of March 3, 1992. App. Ex.262. The statement also shows that a deposit in the amount of $55,755 on February 4, 1992 and other smaller transactions were made to the account during the months of January and February 1992. App. Ex. 262 (MGS DOJ 001446-47).

352. The first joint financial statement prepared after the creation of the Stock Account is the joint financial statement dated May 1, 1992. App. Ex. 189.

353. The May 1, 1992 financial statement reports that the Smiths jointly owned cash and marketable securities totaling $530,000. App. Ex. 189.

354. The 1992 Financial Statement for the first time listed the two-family house, three cottages and a lake front lot, which L. Smith stated she inherited from her father, as "owned by Mrs. Smith" (in all prior years they are listed as assets of both Smiths). App. Ex. 189 at 3.

355. However, the 1992 Financial Statement continued to list all cash and securities, totaling $530,000 including the assets in the Stock Account, as joint assets of both Smiths. App. Ex. 189.

356. There is no documented evidence of a non-IRA brokerage account solely in L. Smith's name prior to November 1991.

B. David Smith Controlled the Stock Account

357. David Smith had full trading authorization over the Stock Account, and the right to withdraw money and securities from the Stock Account, since on or about December 3, 1991. App. Ex. 221 (MGS DOJ 000185) App. Ex. 222 (MGS DOJ 000226).

358. "Most" investment decisions were made by David Smith. App. Ex. 252 (L. Smith 5/27/10 Deposition at 34:8-35:3).

359. L. Smith did not know whether any money from the Stock Account was used to invest in any McGinn Smith entities. She left those decisions to David Smith. App. Ex. 252 (L. Smith 5/27/10 Deposition at 78:22-79:8).

360. L. Smith conceded that David Smith was allowed to use the Stock Account for his own benefit on numerous occasions during the at least 15 years preceding the PI hearing. App. Ex. 272 (PI Tr. at 404-405).

C. **The Stock Account Was Routinely Used to Pay the Smiths' Joint Expenses**

361. The Stock Account was frequently used to fund common expenses and fund assets that benefitted both David and L. Smith. App. Ex. 218 (D. Smith Responses to SEC Request for Admissions, ¶ 31) See also below.

362. For example, the Smiths financed the purchase of their prior primary residence in Clifton Park from the Stock Account. App. Ex. 252 (L. Smith 5/27/10 Deposition at 29:24-30:8).

363. In the mid-1980s, the Stock Account was used to purchase a ski condominium in Vermont for approximately $125,000. App. Ex. 252 (L. Smith 5/27/10 Deposition at 35:20-36:19).

364. Money from the Stock Account was used to purchase a residence in Vero Beach, Florida in the name of David and Lynn Smith in 2001. App. Ex. 252 (L. Smith 5/27/10 Deposition at 20:19-25 to 21:1-15); App. Ex. 272 (PI Hearing T.371-72).

365. The Smiths' paid approximately $1,389,000 for the Vero Beach house, including a $130,000 down payment and $270,905 at closing on or about June 21, 2001. App. Ex. 286, (HUD-1 Settlement Statement).

366. Brokerage records show that a transfer of $100,000 from the Stock Account to David Smith's checking account was made on May 7, 2001 and a transfer of $300,000 was made from the Stock Account to David Smith's checking account on June 19, 2001, two days before the closing. App. Ex. 1 (Palen Ex. 25).

367. The Smiths financed their two children's college education from the Stock Account. App. Ex. 252 (L. Smith 5/27/10 Deposition at 30:7-10).

368. Brokerage records show that the Stock Account contributed approximately $142,500 to IRAs for David Smith, Lynn Smith, Geoffrey Smith and Lauren Smith over the years. App. Ex. 1 (Palen Ex. 24 at 2).

369. Bank records show that on two occasions, April 14, 2006 and April 10, 2007, David Smith used monies from his checking account, $4,500 and $5,000 respectively, to fund an IRA in L. Smith's name and used monies from his checking account to fund IRAs for himself, and the Smiths' children Geoffrey and Lauren Smith. App. Ex. 1 (Palen Ex. 26); App. Ex. 244 at

19 (L. Smith 5/21/10 Declaration, Ex. B); App. Ex. 252 (L. Smith 5/27/10 Deposition at 58:19-60:3; 61:6-9).

370. Brokerage and bank records show that on June 19, 2003, $70,000 was transferred from the Stock Account to David Smith's account. The funds were used to make the down payment on the Smiths' residence in Saratoga Springs, NY that was purchased in both their names. App. Ex. 252 (L. Smith 5/27/10 Deposition at 24:15-25); App. Ex. 1 (Palen Exs. 25 and 26) App. Ex. 204 at 1-3.

371. David Smith caused numerous other transfers of stocks and monies to be made from the Stock Account for the benefit of himself, his family and various McGinn Smith entities. For example, brokerage and bank records show that between August 28, 1999 and April 5, 2010, approximately $4.7 million was transferred from the Stock Account to David Smith's checking account, and only $390,000 was transferred back from David Smith's checking account to the Stock Account. App. Ex. 1 (Palen Ex. 24 at 1).

372. From November 21, 1992 through August 27, 1999, a period for which incomplete records exist, brokerage records show that at least $2,585,000 was transferred from the Stock Account to David Smith's checking account, with no known transfers back to the Stock Account from the checking account. App. Ex. 1 (Palen Ex. 24 at 2).

373. David Smith repeatedly used funds transferred from the Stock Account to his checking account to pay large common expenses of him and L. Smith, such as mortgage payments on their primary residence in Saratoga Springs, New York, and their home in Vero Beach, Florida, golf club dues, federal and state taxes, payments to their children Geoffrey and Lauren Smith, car payments and insurance. App. Ex. 1 (Palen Ex 25 and 26).

374. L. Smith testified at the preliminary injunction hearing that David Smith used: "his checking account for items that maybe I could not afford to write checks out of mine. We had two mortgages, car payments, insurance, and so on. And that's what he used his account for, the big things. And I used mine for household daily, lawn service, groceries, that kind of thing." App. Ex. 272 (PI Tr. at 283:8-13).

D. David Smith Contributed Assets to the Stock Account Even After It Was Opened

375. David Smith also made contributions to the Stock Account. For example, David Smith used monies he obtained as a loan from McGinn Smith to partially fund the purchase of ALBANK stock that was eventually converted into the Charter One stock. See below.

376. On March 23, 1992, David Smith placed an order for 50,000 shares of ALBANK Financial Corporation at a price of $10.00 per share, and submitted $500,000 in payment. App. Ex. 237 (Dep. Ex. 446); App. Ex. 238 (Dep. Ex. 447).

377. $354,000 of that amount consisted of money withdrawn from the Stock Account on March 16, 1992. App. Ex. 235.

378. $150,000 of that $500,000 consisted of a loan that David Smith took out from McGinn Smith and Co on March 23, 1992. App. Ex. 235 (Dep. Ex. 444), App. Ex. 236 (Dep. Ex. 445).

379. Because of demand for the ALBANK shares, David Smith was issued only 40,688 shares of ALBANK stock on or about April 5, 1992. App. Ex. 239 (Dep. Ex. 448).

380. On March 31, 1992, a check in the amount of $93,674.85 was issued to David Smith from Albany Savings Bank, including $544.85 in interest as a refund for the 9,322 shares that were not issued to him. App. Ex. 239 at 2 (Dep. Ex. 448). Thus, David Smith purchased 40,688 shares of ALBANK stock for approximately $406,880 dollars, using portions of the

$349,000 withdrawn from the Stock Account and portions of the $150,000 David Smith borrowed from McGinn Smith. See also App. Ex. 290 (D. Smith 12/14/11 Dep. at 328:5-25).

381. The 40,688 shares of ALBANK stock were not deposited into the Stock Account until September 18, 1992. App. Ex. 234 (Dep. Ex. 443).

382. In opposing the freeze of the Stock Account, L. Smith stated that: "In approximately April 1992, using assets in my stock account, I purchased 40,000 shares of Albank stock at $10 per share at the initial public offering. … I held this stock in my brokerage account for many years and, because of subsequent mergers and acquisitions involving Albany Savings Bank, Citizens Bank and Charter One Financial, and the resulting stock splits and increases in value, my holdings in this banking institution increased to 110,735 shares of Charter One stock by 1999…. [the shares were] valued at $24.75 per share in August 1999. App. Ex. 244 (L. Smith 5/21/10 Affidavit, Dkt. 34, at ¶ 3).

383. This statement was also false because, as demonstrated above, David Smith also contributed money to purchase the initial ALBANK stock.

384. L. Smith's statement was also false because Charter One stock was not held in the Stock Account for many years. See below.

385. By the end of August 1999, the Stock Account had 110,735 shares of Charter One worth $24.75 per share, or $2,740,691. App. Ex. 280 (Dep. Ex. 451-Summary Chart of Charter One stock transactions).

386. Each September from 1999 to 2002, Charter One issued a 5% stock dividend resulting in a total of an additional 21,269 shares added to the Stock Account. App. Ex. 280 (Dep. Ex. 451). The Charter One stock also continued to appreciate during this time. App. Ex. 280 (Dep. Ex. 451); App. Ex. 218 (D. Smith's Responses to Requests for Admission, ¶ 35).

387. During the period from August 1999 to September 2002, the Smiths sold a total of 24,530 shares of Charter One stock from the Stock Account for a gross profit of approximately $800,000, and transferred an additional 2,574 shares of Charter One stock out of the Stock Account. App. Ex. 280 at 4 (Dep. Ex 451); App. Ex. 218 (D. Smith's Responses to Requests for Admission, ¶ 36).

388. By early October 2002, the Stock Account had 105,000 shares of Charter One stock worth over $3 million. App. Ex. 280 (Dep. Ex. 451).

E. The Stock Account's Assets Were Routinely Used by David Smith to Fund McGinn Smith and its Related Entities Business Interests

389. The Stock Account was also used to benefit David Smith's professional interests. See below. See also, App. Ex. 218 (D. Smith's Responses to SEC's Requests for Admissions, ¶ 31).

390. In explaining the reasons for certain transfers from the Stock Account to McGinn Smith entities, David Smith admitted that the transfers were loans from both him and his wife. For example, he stated: " Defendant's best recollection is that he and his wife lent to MS Holdings $150,000 in July 2007 that was to be repaid as soon as possible, but no later than one year from the loan date. Financial circumstances at McGinn Smith prevented that schedule from being fulfilled, with $50,000 being paid through October 2008 and the balance of $100,000 remaining outstanding." App. Ex. 217 (D. Smith Responses to Plaintiff's First Request for Interrogatories, ¶ 16 Response).

391. Brokerage and bank records show that the $150,000 was transferred from the Stock Account to MS Holdings on July 30, 2007. App. Ex. 1 (Palen Ex. 25).

392. David Smith also admitted that: "…in late April or early May of 2009 the Smiths lent an additional $100,000 to MS Holdings." App. Ex. 217 (D. Smith Responses to Plaintiff's First Request for Interrogatories, ¶ 16 Response).

393. Brokerage and bank records show that the $100,000 was transferred from the Stock Account to David Smith's checking account on April 30, 2009 and a corresponding transfer of $100,000 from David Smith's checking account to McGinn Smith's Operating account occurred on the same date. App. Ex. 1 (Palen Exs. 25 and 26), App. Ex. 346 (MS-E-3101383).

394. On October 14, 2002, all 105,000 shares of Charter One stock in the Stock Account were journaled out of the Stock Account and were deposited as a "loan" into an account for KC Acquisition Corp., a McGinn Smith Entity. App. Ex. 270 at 57 (PI EX. 126 (10/14/02 LOA)); App. Ex. 280 (Dep. Ex. 451 -also Dkt. 662-3).

395. David Smith was Treasurer of KC Acquisition Corp. App. Ex. 270 at 57 (PI EX. 126 (10/14/02 LOA)); App. Ex. 218 (D. Smith's Responses to Requests for Admissions, ¶38); App. Ex. 265 (Lynn Smith Responses to Requests for Admissions, ¶ 12).

396. The 105,000 shares of Charter One stock were loaned to KC Acquisitions, in part, so that it could obtain a "going concern" letter from its auditors. App. Ex. 304 (Dep. Ex. 374, paras. 118-129).

397. The 105,000 shares of Charter One stock remained out of the Stock Account from October 14, 2002 to July 29, 2003, when the shares were journaled back into the Stock Account from the KC Acquisition Corp. account. App. Ex. 270 at 57 (PI EX. 126 (10/14/02 LOA)App. Ex. 280 at 4 (Summary Chart of Charter One stock transactions – also Dkt. 662-3); App. Ex.

265 (Lynn Smith's Response to Requests for Admissions, ¶ 13; App. Ex. 218 (D. Smith Responses to Requests for Admissions, ¶ 39).

398. David Smith, as the treasurer of KC Acquisition Corp., signed the letter authorizing the transfer of shares back to the Stock Account. App. Ex. 270 at 57 (PI EX. 126 (10/14/02 LOA); App. Ex. 218 (D. Smith Responses to Requests for Admissions, ¶ 40).

399. The assets in the Stock Account were extensively co-mingled with the assets held in accounts for MS & Co. or related entities throughout the existence of the Stock Account. For example, David Smith and MS & Co. personnel routinely initiated, created, authorized and/or requested transfers from the Stock Account to meet liquidity needs of MS & Co. or related entities or to provide bridge financing for MS & Co. related entity deals. App. Ex. 244 (L. Smith 5/21/10 Affidavit at 27).

400. Brokerage and bank records show that from August 28, 1999 through April 5, 2010, approximately $ 17.2 million was transferred from the Stock Account to various McGinn Smith related entities. App. Ex. 1 (Palen Ex. 24).

401. Brokerage and bank records show that from August 28, 1999 through April 5, 2010, approximately $13.7 million was transferred from various McGinn Smith related entities to the Stock Account. App. Ex. 1 (Palen Ex. 24).

402. For example, during this period, brokerage and bank records show that approximately $7.9 million was transferred from the Stock Account to Capital Center Credit Corp ("C-4"), and approximately $7.2 million was transferred from C-4 to the Stock Account. App. Ex. 1 (Palen Ex. 24 at 1).

403. C-4 was owned by David Smith and Timothy McGinn. App. Ex. 289 (D. Smith 12/13/11 Dep. at 53:10-21).

404. Brokerage and bank records show that approximately $2,000,000 was transferred from the Stock Account to FIIN and approximately $2,015,556 was transferred from FIIN to the Stock Account. App. Ex. 1 (Palen Ex. 24 at 1).

405. Brokerage and bank records show that approximately $300,000 was transferred from the Stock Account to MS & Co. and approximately $29,500 was transferred from MS & Co to the Stock Account. App. Ex. 1 (Palen Ex. 24 at 1).

406. Brokerage and bank records show that approximately $1.2 million was transferred from the Stock Account to McGinn Smith Advisors, LLC. App. Ex. 1 (Palen Exhibit 24 at 1).

407. Brokerage and bank records show that approximately $300,000 was transferred from the Stock Account to McGinn Smith Firstline Funding, LLC. App. Ex. 1 (Palen Exhibit 24 at 1).

408. Brokerage and bank records show that approximately $395,000 was transferred from the Stock Account to McGinn Smith Funding, LLC. App. Ex. 1 (Palen Exhibit 24 at 1).

409. Brokerage and bank records show that approximately $150,000 was transferred from the Stock Account to McGinn Smith Holdings, LLC. App. Ex. 1 (Palen Exhibit 24 at 1).

410. Brokerage and bank records show that approximately $300,000 was transferred from the Stock Account to TDMM Benchmark Trust 09. App. Ex. 1 (Palen Exhibit 24 at 1).

411. Brokerage and bank records show that approximately $100,000 was transferred from the Stock Account to TDMM Cable Funding and approximately $260,000 was transferred from TDMM Cable Funding, LLC to the Stock Account. App. Ex. 1 (Palen Exhibit 24 at 1).

412. Brokerage and bank records show that approximately $175,000 was transferred from TDMM Cable Jr. Trust 09 to the Stock Account. App. Ex. 1 (Palen Exhibit 24 at 1).

413. Brokerage and bank records show that $3,143,625 was transferred from the Stock Account to Integrated Alarm Services ("IA"), a McGinn Smith related entity, and $3,339,625 was transferred from IA to the Stock Account. App. Ex. 1 (Palen Ex. 24 at 1).

414. Brokerage and bank records show that approximately $599,000 was transferred from the Stock Account to and approximately $149,000 was transferred from McGinn Smith Capital Holdings to the Stock Account. App. Ex. 1 (Palen Ex. 24 at 1).

415. In addition, between November 21, 1992 and August 27, 1999, a period for which there are incomplete records, financial records show at least $3.3 million was transferred from the Stock Account to McGinn Smith & Co., and at least $1.5 million was transferred from the Stock Account to C-4. App. Ex. 1 (Palen Ex. 24 at 2).

416. During the same period, financial records show that at least $2 million was transferred from McGinn Smith & Co. to the Stock Account and at least $762,000 was transferred from C-4 to the Stock Account. App. Ex. 1 (Palen Ex. 24 at 2).

417. On September 29, 2006, David Smith loaned approximately $2,625,000 from FIIN to TDM Cable Funding, LLC. App. Ex. 289 (D. Smith 12/13/11 Dep. at 5-28); App. Ex. 215 (Dep. Ex. 508).

418. On October 3, 2006, David Smith, Timothy McGinn and their partner Matthew Rogers each received $350,000 from TDM Cable Funding LLC. App. Ex. 295, 296, 245 (Dep. Exs. 509; 510; 511).

419. On October 4, 2006, Timothy McGinn used $85,000 of the monies he received from TDM Cable Funding LLC to repay the Stock Account a portion of a loan he had received from the Stock Account. App. Ex. 1 (Palen Ex. 25) App. Ex. 347 (M&T01193-011195 at 2 and 3) .

420. In February and March 2009, David Smith caused cash and securities totaling at least $635,000 to be transferred to the Stock account. App. Ex. 272 (PI Tr. 300-301); see also below.

421. In February 2009, David Smith transferred all of the cash and securities, valued at $610,095.54 as of February 1, 2009 from the David L. Smith Lifetime QTip Trust to his personal brokerage account. App. Ex. 292 (D. Smith QTip Trust Statement dated 2/28/09); App. Ex. 293 (D. Smith brokerage statement dated 2/28/09).

422. The QTip Trust was created with funds that were transferred from David Smith's personal account ending in 9965 that were proceeds of the fraud. For example, on May 10, 2007, D. Smith received $310,000 from MS Funding, LLC. App. Ex. 1 (Palen Ex. 26).

423. These funds from MS Funding LLC were improperly diverted funds payments to David Smith made in connection with the Firstline Trust offering. App. Ex. 337 (GJ1A).

424. On May 25, 2007, David Smith transferred those funds to the QTip Trust. App. Ex. 1 (Palen Ex. 26).

425. Again, on October 10, 2008, David Smith transferred $230,000 from his checking account to the QTip Trust. App. Ex. 1 (Palen Ex. 25). The funds were received from NEI Capital LLC on October 3, 2008 ($265,000) and on October 6, 2008 ($75,000). App. Ex. 1 (Palen Ex. 25). These were unauthorized payments made to David Smith in connection with the Fortress offering. App. Ex. 337 (GJ1A).

426. Thus, the Stock Account received fraudulent proceeds of the McGinn Smith fraud through its receipt of funds, totaling $610,095.54 from David Smith's QTip Trust.

427. In addition, on February 4, 2009, David Smith caused a transfer of $38,430.46 from C-4 to the Stock Account. App. Ex. 1 (Palen Ex. 25); App. Ex. 252 (L. Smith 5/27/10 Deposition at 62:23-63:10; Dep. Ex. 612).

428. This transfer was not repayment of any loan from the Stock Account to C-4. App. Ex. 252 (L. Smith 5/27/10 Deposition at 62:23-63:10).

429. L. Smith stated that this transfer was a "gift" from David Smith. App. Ex. 252 (L. Smith 5/27/10 Deposition at 62:23-63:10).

430. The Court found that David Smith's transfers of certain of these assets to the Stock Account in 2009 were done "for no apparent reason other than to shield those assets from investors. *SEC v. McGinn Smith et al.*, 752. F. Supp.2d 194 at 203 (MDO dated 7/7/10, Dkt No. 86, at 10) citing PI Hearing Tr. 290-92; 296-301).

431. The Smiths used monies from the McGinn Smith entities for their personal benefit. For example, in 2010, the Smiths leased two cars, an SUV Lexis and a compact Infiniti. Prior to the assets freeze, the leases were paid for by MS & Co. L. Smith 5/27/10 App. Ex. 252 (Deposition at 27:24-2815).

432. The transfers from the Stock Account were frequently made pursuant to Letters of Authorization ("LOA"). App. Ex. 270 (PI Ex. 126); App. Exs. 177-180; 188; 190; 191; 193; 195; 196; 198, 199; 201; 202; 204; 205.

433. L. Smith signature appears on the majority of the LOA's. App. Ex. 1 (Palen Ex. 24); App. Ex. 270 (PI Ex. 126); App. Exs. 177-180; 188; 190; 191; 193; 195; 196;198, 199; 201; 202; 204; 205.

434. However, at times, David Smith directed McGinn Smith employees to cut and paste L. Smith's signature on LOAs. For example, on March 6, 2002, David Smith asked Patty

Sicluna to prepare a wire and to do a "cut and paste job," indicating that the L. Smith signature line on the LOA should be cut from one document and pasted to another. App. Ex. 178 (MGS DOJ 000526 and MGS DOJ 000518).

435. Also on March 6, 2002, a LOA for a $3,000 wire transfer to David Smith's account has attached to it a handwritten instruction from David Smith : "Patty: Wire $3,000 into my account at M&T… cut and paste again." App. Ex. 177 (MGS DOJ 000525; MGS DOJ 000524).

436. During the period from at least 2001 to 2009, L. Smith typically signed 10-15 LOAs in blank, i.e., with no information concerning the amount to be transferred or the recipient, and provided them to David Smith to be used for making transfers from the Stock Account. App. Ex. 271, 272 (PI Hearing Tr. at 175-184; 188-189; 219-220; 341-43, 384-86, 413-14).

437. David Smith then gave these blank but signed authorizations to a subordinate to be maintained in the subordinate's desk for use as directed by David Smith. App. Ex. 271, 272 (PI Hearing Tr. 175-84, 341-43, 384-86, 413-14).

438. Over 137 LOAs were processed by various McGinn Smith employees in connection with transfers into and out of the Stock Account. App. Ex. 1 (Palen Ex. 25); App. Ex. 270 (PI Ex. 126); App. Ex. 177-180; 188; 190; 191; 193; 195; 196;198, 199; 201; 202; 204; 205.

439. For a period of time, MS & Co, was required by their clearing broker to have a second signature on the LOAs. David Smith, Timothy McGinn, Patty Sicluna, and David Rees, provided these authorizations. App. Ex. 1 (Palen Ex. 25); App. Ex. 270 (PI Ex. 126); App. Ex. 177-180; 188; 190; 191; 193; 195; 196;198, 199; 201; 202; 204; 205.. App. Ex. 300 (P.Sicluna 11.2.11 Deposition at 39-40).

440. Many of the LOAs reflected the need for urgent transfers of funds. For example, on June 3, 1999, Brian Shea wrote to Patty Sicluna, "$400,000 Lynn Smith to Capital Center Credit Corp. Need ASAP. Thank you." App. Ex. 199 at 18-19 (1999 – Letters of Authorization: MGS DOJ 000162-3). This LOA contained a second approval signature by Timothy McGinn. Id.

441. Timothy McGinn, rather than David Smith, countersigned over 80 of the LOAs. App. Ex. 1 (Palen Ex. 25); App. Ex. 270 (PI Ex. 126);App. Ex. 177-180; 188; 190; 191; 193; 195; 196;198, 199; 201; 202; 204; 205. At times, other McGinn Smith employees, such as Patty Sicluna and David Rees, provided the second signature. *Id.*

442. Many of the transfers to McGinn Smith were short term infusions of capital to help the entities continue operations or meet minimum raise thresholds so that deals could go forward. For example, financials records show a transfer of $125,000 from the Stock Account to C-4 on November 1, 1995 and a transfer of $125,000 from C-4 back to the Stock Account on November 30, 1995. App. Ex. 1 at 70 (Palen Ex. 25).

443. Financial records show a transfer of $325,000 from the Stock Account to C-4 on June 27, 1997 and a transfer of $325,000 from C-4 to the Stock Account on July 11, 1997. App. Ex. 1 at 70 (Palen Ex. 25).

444. Financial records show a transfer of $160,000 from the Stock Account to C-4 on February 5, 1999 and a transfer of $160,000 from C-4 back to the Stock Account on April 14, 1999. App. Ex. 1 at 71 - 72 (Palen Exhibit 25).

445. Financial records show a transfer of $300,000 from the Stock Account to C-4 on September 30, 1999 and a transfer of $300,000 from C-4 back to the Stock Account on October 1, 1999. App. Ex. 1 at 72 (Palen Exhibit 25).

446. Financial records show a transfer of $500,000 from the Stock Account to C-4 on October 22, 1999 and a transfer of $502,630 from C-4 back to the Stock Account on November 15, 1999. App. Ex. 1at 72 (Palen Exhibit 25).

447. Financial records show a transfer of $350,000 from the Stock Account to C-4 on July 2, 2001 and a transfer of $350,000 from C-4 back to the Stock Account on July 5, 2001. App. Ex. 1 at 75 (Palen Exhibit 25).

448. Financial records show a transfer of $500,000 from the Stock Account to C-4 on September 28, 2001 and a transfer of $500,000 from C-4 to the Stock Account on October 1, 2001. App. Ex. 1 at 75 (Palen Exhibit 25).

449. Financial records show a transfer of $550,000 from the Stock Account to C-4 on October 30, 2002 and a transfer of $552,712 from C-4 back to the Stock Account on November 19, 2002. App. Ex. 1 at 78 (Palen Exhibit 25).

450. Financial records show a $3,000,000 transfer from the Stock Account to IASG was made on January 14, 2003 for "working capital" to effect the public offering and was repaid on July 29, 2003 with offering proceeds. App. Ex. 1 (Palen Ex. 25); App. Ex. 450 (Excerpt from Prospectus, PI Ex. 450 at Gersav 0015923).

451. L. Smith could not recall whether she had ever loaned money to IASG. App. Ex. 272 (PI Tr. 344: 18-23).

452. On October 1, 2003, financial records show that the Stock Account transferred $2 million to First Independent Income Notes. FIIN repaid the amounts to the Stock Account on October 30, 2003, along with $15,556 in interest. App. Ex. 1 at 80 (Palen Exhibit 25).

453. Financial records show that, on June 5, 2009, two transfers, totaling $366,000, were made from the Stock Account for the benefit of TDMM Cable Funding, LLC. App. Ex. 1

at 85 (Palen Ex. 25); App. Ex. 244 (L. Smith 5/21/10 Affidavit at 27); App. Ex. 291 (MS- N-00777476).

454. Financial records show that the Stock Account was repaid $160,800 of these monies on June 10, 2009 and $175,000 of these monies on July 30, 2009 from investor funds raised by TDMM Cable Jr. Trust 09. App. Ex. 1 at 85 (Palen Ex. 25); App. Ex. 294 (MERC 000045; MERC 000233).

455. Although a promissory note was prepared at some point in connection with this transfer, L. Smith never signed the note, did not see it before the transfer was made and never even saw it until after this case was brought. App. Ex. 252 (L. Smith 5/27/10 Deposition at 53:5-55:20); App. Ex. 254 (L. Smith 5.21.10 Aff.).

456. Financial records show that on November 29, 2007, $375,000 was transferred from the Stock Account to McGinn Smith Funding, LLC to provide a bridge loan for the Firstline Trust offering. App. Ex. 1at 83 (Palen Ex. 25); App. Ex. 252 (L. Smith 5/27/10 Deposition at 61:19-62:15).

457. Financial records show that on December 20, 2007, the $375,000, plus an additional $5,000, was repaid by McGinn Smith Funding to the Stock Account via David Smith's checking account. App. Ex. 1 at 83 (Palen Exs. 25 and 26).

458. L. Smith did not know the circumstances concerning the bridge loan, why the loan was made or what McGinn Smith Funding was at the time of the loan. App. Ex. 252 (L. Smith 5/27/10 Deposition at 61:19-62:15).

459. Financial records show that on March 10, 2008, the Stock Account transferred $200,000 to M&S Partners; the money was then transferred to McGinn Smith Holdings LLC, then to TAIN's Operating Account, then to TAIN's account at NSF to meet a margin call. App.

Ex. 1 at 83 (Palen Ex. 25); App. Ex. 288 (M & T 001634; M&T 001820; M&T 003257; NFS008405-8412; MS-E-1092268).

460. Financial records show that on October 30, 2009, the Stock Account made a $300,000 investment in TDMM Benchmark Trust 09. App. Ex. 1 at 85 (Palen Exhibit 25).

461. Few if any of these transfers were accompanied by any formal "loan' documentation.

462. In a letter dated May 13, 2002 to Brian Shea, a McGinn Smith employee, David Smith summarized the business reasons for various transfers from the Stock Account and other sources to McGinn Smith entities. David Smith stated: "You have asked me to summarize the various investments and loans that Lynn and I have made over the last several years to McGinn Smith & Co. and its affiliates….The attached summary can be used to confirm the status of both principal and interest for all of the investments and to serve as a record for my estate should I predecease the satisfaction of these loans and investments." David Smith also noted that various of the "loans" had no loan documentation prepared. App. Ex. 246 (MGS DOJ 001392-94).

F. Lynn Smith Had Minimal Input Into and Knowledge of the Transfers From the Stock Account

463. L. Smith could not explain the business reasons for certain large transfers from the Stock Account that occurred as recently as the prior year. For example, L. Smith did not know the reason for transfers of $15,000 from the Stock Account to David Smith on February 20, 2009 or for a $100,000 check from McGinn Smith payable to the Stock Account on May 4, 2009. App. Ex. 252 (L. Smith 5/27/10 Deposition at 89:23-90:22).

464. L. Smith did not recall lending money to a company called Mobile Search Security. App. Ex. 252 (L. Smith 5/27/10 Deposition at 91:8-92:2).

465. L. Smith did not recall whether she owned certificates in Benchmark despite the fact that money from the Stock Account had been used to purchase Benchmark notes on October 30, 2009. App. Ex. 252 (L. Smith 5/27/10 Deposition at 92:4-92:18).

466. Money from the Stock Account was also used to make large personal loans to David Smith's business partner Timothy McGinn. A $900,000 loan was made from the Stock Account to Timothy McGinn in 2003. App. Ex. 259 (L. Smith Statement of Net Assets dated March 31, 2010; App. Ex. 252 (L. Smith Deposition dated 5/27/2010 at 16:5-25-17:1-11).

467. Another loan of $15,000 was made from the Stock Account to Timothy McGinn. App. Ex. 259 (L. Smith Statement of Net Assets dated March 31, 2010); App. Ex. 252 (L. Smith Deposition dated 5/27/2010 at 16:5-25-17:1-11).

468. L. Smith never spoke to Timothy McGinn in connection with either of these loans. App. Ex. 272 (PI Tr. at 278).

469. David Smith described his wife's ability to understand financial and business matters, both with respect to the Smith Trust and the Annuity Agreement discussed below and generally, as follows:

> A. My recollection is I would have given her the basic background, reasons, benefits, talked about the annuity payment and, you know, 15 minutes later if given a quiz, she would have failed, but that notwithstanding that I had that discussion.
>
> Q. Why did you say that?
>
> A. Because the nature of the beast is my wife is, you know, totally dependent on – well, let me rephrase that. She had a great deal of confidence in my business acumen and experience. She had virtually none. The experience had been reasonably good for all the years we've been married and she quite frankly – and this is not to denigrate her skill sets or her intellectual capacity whatsoever, she just didn't have a lot of interest in those things. She knew that we were reasonably well off, that our future ability to enjoy a post-retirement was fairly well in place and just did not bother with the details. And like a lot of wives post making that signature, as I said, if I went back to her and had some period of time and asked her what I had just told you ad gave her a test, she would probably fail it.

App. Ex. 290 (David Smith 12/14/11 Deposition Tr. at 346:17-347:13).

470. David Smith also admitted: "That's an accurate statement, yes." when asked: "All right, Now, I think I understand you to say that your wife really didn't focus that much on the business end of your finances? App. Ex. 290 (D. Smith 12/14/11 Deposition Tr. at 348:23-349:2).

VIII. THE SMITHS BENEFICIALLY OWNED AND DAVID SMITH CONTROLLED THE SMITH TRUST

471. In December 2003, David Smith, L. Smith, Timothy McGinn, MS & Co. and other entities controlled by Smith and McGinn were named as defendants in a securities fraud suit filed in the United States District Court for the Southern District of New York arising from the June 2003 initial public offering of IASG, Meyers v. Integrated Alarm Services Group, Inc., et al, 03-cv-09748 (S.D.N.Y.). App. Ex. 304 (Dep. Ex. 374); App. Ex. 265 (Lynn Smith Response to First Request for Admissions, ¶ 30); App. Ex. 218 (D. Smith Responses to Requests for Admissions, ¶ 58); App. Ex. 282 (T. McGinn Responses to Requests for Admissions, ¶ 58).

472. The complaint asserted 23 causes of action and sought $3 million in damages for each claim. App. Ex. 304 (Dep. Ex. 374).

473. The Complaint included factual allegations relating to two $3 million loans by L. Smith to certain entities to facilitate a public offering of IASG, a company affiliated with Smith and McGinn. App. Ex. 304 (Dep. Ex. 374, paras. 118-129).

474. The Stock Account was used to make these loans. See above at 377-383..

475. The case was settled in the spring of 2004 and included payments totaling $200,000 to the plaintiff from M&S Partners and IASG. App. Ex. 250 (Dep. Ex. 453 - Settlement Agreement). L. Smith and David Smith were signatories to the Settlement Agreement. Id.

476. On February 26, 2004, Steven Vitulano, Branch Chief of the SEC's Broker-Dealer Inspection Team sent David Smith, in his capacity as President of McGinn Smith, a letter setting forth violations of various rules and regulations promulgated under the Securities Exchange Act of 1934 and the National Association of Securities Dealers, Inc. that McGinn Smith had been found, during on-site inspections, to have violated, including a violation of Section 15(a) of the Exchange Act in that McGinn Smith controlled C-4 as an unregistered broker-dealer and a violation of Section 5 of the Securities Act of 1933 in that McGinn Smith had accepted funds for the purchase of IASG's initial public offering prior to the effective date of the offering. App. Ex. 298 (Dep. Ex. 542 – February 26, 2004 Letter from Vitulano).

477. The SEC's letter also detailed numerous recordkeeping violations. App. Ex. 298 (Dep. Ex. 542 – February 26, 2004 Letter from Vitulano).

478. At the time of the transfer of the Charter One Stock to the Smith Trust, David Smith was aware of the consequences of committing fraud and that his actions could result in significant financial loss. In a lengthy, prior undated, handwritten "personal confession" to McGinn, Smith wrote that:

> The business has become addicted to the cash flow from the trust business, and without that we will have a difficult time surviving. . . . The default of the trusts will drastically reduce revenues, cause us to lose brokers and at least their confidence in us, bring on crushing litigation and devastating publicity and I am convinced prosecution by regulators or worse. . . . I am just overwhelmed by the thought of the financial losses, the humiliation, the perceived betrayal of trust. . . . I, unlike you, feel that we are vulnerable to criminal prosecution. . . .
>
> > [W]e are now in possession of indisputable empirical evidence that the new investments have no chance of ever being repaid in full. . . . For us not to allow for these deficits by setting up adequate reserves is, in my judgment, bordering on fraud, certainly, by not

> disclosing in the prospectus our poor history of collections, we are not providing the prospective investors an accurate picture of this risk. We both know why we don't make that disclosure – because such disclosure would cause our salesman to cease selling and investors to cease buying. Thus, we are misleading both our own employees and customers. . . . This is wrong. I strongly believe that in civil or criminal litigation we would lose badly on this point. . . .
>
> [B]oth you and I are violating the high standards of integrity and ethics that have been the historical standard for us. That bothers me very very much. But what terrifies me is the possibility of being indicted for such conduct, and worse, the prospect of conviction. I cannot emphasize enough how strongly I feel about this point.

App. Ex. 54 at 4-8; App. Ex. 55 (typed version).

479. On May 4, 2004, Charter One publicly announced that it was being acquired in an all-cash deal by Citizens Financial Group, which paid $44.50 per share. The deal was completed on August 31, 2004. App. Ex. 214 (D. Smith Answer to SAC, ¶ 19); App. Ex. 265 (Lynn Smith Response to First Request for Admissions, ¶ 26); App. Ex. 218 (D. Smith Responses to Requests for Admissions, ¶ 54). David and L. Smith knew, therefore, that their Charter One stock would be converted to cash as a result of the buy-out. Id.

480. David and L. Smith created the David L. and Lynn A. Smith Irrevocable Trust U/A dated August 4, 2004 (the "Smith Trust") pursuant to a Declaration of Trust. App. Ex. 226 (Dep. Ex. 369 – Declaration of Trust); App. Ex. 265 (Lynn Smith Response to First Request for Admissions, ¶ 19); App. Ex. 218 (D. Smith Responses to Requests for Admissions, ¶ 47).

481. The Smith Trust had no assets when it was created. App. Ex. 265 (Lynn Smith Response to First Request for Admissions, ¶ 20); App. Ex. 218 (D. Smith Responses to Requests for Admissions, ¶ 48).

482. L. Smith stated that she "transferred 100,000 shares of Charter One stock, then valued at $44.50 per share, to the trust." App. Ex. 254 (Lynn Smith 5/21/10 Aff., Dkt, 34, at ¶ 5).

483. On September 1, 2004, 100,000 shares of Charter One stock were transferred from the Stock Account to the Smith Trust account. At the time of this transfer, the fair market value of the Charter One stock was approximately $4.45 million. App. Ex. 214 (D. Smith Answer to SAC, ¶ 20); App. Ex. 255 (L. Smith Answer to SAC, ¶ 128).

484. On the same day that the 100,000 shares were transferred from the Stock Account to the Smith Trust account on September 1, 2004, the cash merger occurred, resulting in the Smith Trust account being credited with $4,450,000 in cash. App. Ex. 214 (D. Smith Answer to SAC, ¶ 20); App. Ex. 255 (L. Smith Answer to SAC, ¶ 129); App. Ex. 265 (Lynn Smith Response to First Request for Admissions, ¶ 28); App. Ex. 265 (Smith Trust Trustee, G. Smith and Lauren Smith Response to First Request for Admissions, ¶ 28); App. Ex. 218 (D. Smith Responses to Requests for Admissions, ¶ 56). The creation of the Smith Trust and the transfer of the stock through the Annuity Agreement therefore served to shelter this large sum of cash. Id.

485. At the time of the transfer of the Charter One stock to the Smith Trust, the FIIN and FEIN fraudulent offerings were well underway. The FIIN offering dated September 15, 2003 and the FEIN offering dated January 16, 2004 each raised $20 million from investors, for a total of $40 million. App. Ex. 1, Ex. 3.

486. The private placement memoranda for both offerings did not permit investments in affiliates but Smith from the beginning invested with affiliates. **See above at 69-74.**

487. As of December 31, 2003, 11% of the investments were with affiliates, and this grew to 32% by December 31, 2004. App. Ex. 1, Exs. 10-12. Smith therefore knew that he would likely become liable to the defrauded investors and/or to the Commission as a result of his ongoing violations of the federal securities laws. Id.

488. In addition, at the time of the transfer to the Smith Trust, the liabilities of FIIN and FEIN far exceeded their assets. As a result, Smith knew that he would be unable to meet the payment obligations of these Funds to investors. Id.

489. L. Smith stated that her reason for creating the Smith Trust was: "to take advantage of available estate planning laws to fund a trust for my children, from which they could benefit during my lifetime, instead of having these assets sit in a brokerage account until my death." App. Ex. 254 (L. Smith 5/21/10 Aff., Dkt. 34, at ¶ 4).

490. In a separate Affidavit, L. Smith stated that she and her husband created the Smith Trust: "… to provide security for my children's future apart from my stock account. … My children were adults, had completed college, and could begin to make financial decisions on their own." App. Ex. 244 (L. Smith 5/21/10 Aff., Dkt. 23 at ¶ 23).

491. In her deposition on May 21, 2010, L. Smith stated that: "The trust, the purpose of the trust was our children are 27 and 30 years old. Presently, we started this about four years ago, this particular trust and I wanted them to be able to have an opportunity to if they wanted to start a business, own a home, I wanted them to have the rewards, reap the rewards of my husband's business and so we both agreed on putting that in the trust." App. Ex. 252 (L. Smith 5/27/2010 Deposition at 39:16-30:18).

492. In her Affidavits submitted in opposition to the freeze of the Stock Account and the Smith Trust, L. Smith repeatedly stated that she and her husband had no interest in the assets of the Smith Trust. For example, L. Smith stated: "From the time the trust was created in August 2004, my husband and I have had no interest in or expectation of an interest in the David L. and Lynn A. Smith Irrevocable Trust. It exists solely, exclusively and permanently for the benefit of my children." App. Ex. 254 (L. Smith 5/21/Affidavit, Dkt. 34, at ¶ 6).

493. L. Smith also stated: "We cannot take money out of the trust." App. Ex. 252 (L. Smith 5/27/2010 Deposition at 41:2-8).

494. L. Smith failed to inform the court that in return for transferring the Charter One stock, worth approximately $4,450,000, to the Smith Trust, the Smiths entered into a Private Annuity Agreement (the "Annuity Agreement") with the Smith Trust on or about August 31, 2004, that entitled the Smiths to yearly annuity payments from the Smith Trust of $489,000 a year beginning in September 2015 and continuing until the death of the last of the Smiths. App. Ex. 227 (Dep. Ex. 370 – Annuity Agreement).

495. Both David and L. Smith signed the Annuity Agreement with the Smith Trust. App. Ex. 227 (Dep. Ex. 370 - Annuity Agreement); App. Ex. 265 (Lynn Smith Response to First Request for Admissions, ¶ 23); App. Ex. 218 (David Smith Response to First Request for Admissions, ¶ 51).

496. The effective date of the Annuity Agreement was August 31, 2004. App. Ex. 279 (Smith Trust Trustee, G. Smith and Lauren Smith Responses to First Request for Admissions); App. Ex.265 (Lynn Smith Response to First Request for Admissions, ¶ 21); App. Ex. 218 (D. Smith Responses to Requests for Admissions, ¶ 49).

497. The Annuity Agreement is a valid and enforceable agreement. App. Ex. 218 (D. Smith Responses to Requests for Admissions, ¶ 53).

498. The Annuity Agreement stated that the Smiths "are the owners of 100,000 shares of stock … and desire to sell the Property to the Transferee to be relieved of the burden and risk associated with owning and managing the Property in order to receive investment income and a portion of the principal on a regular basis." App. Ex. 227 (Dep. Ex. 370 – Annuity Agreement).

499. The Annuity Agreement required the Smith Trust to: "hold full title to the Property, free and clear of all liens and encumbrances, and there shall be no collateral liens of any kind on the Property or any other assets of the Transferee to secure payment of the obligations to the Transferors under this Agreement." App. Ex. 227 (Dep. Ex. 370 – Annuity Agreement, at ¶ 3.

500. In connection with the Annuity Agreement, David and Lynn Smiths' joint life expectancy was calculated as 31 years. App. Ex. 227 (Dep. Ex. 370 – Annuity Agreement). The Smiths therefore have a joint life expectancy of approximately 20 years from the date the payment obligations are scheduled to begin in September 2015. Id.

501. The annual payment of $489,932, if paid out over the 20-year joint life expectancy, would entitle David and/or Lynn Smith to payments totaling approximately $10 million from the Smith Trust. Id.

502. L. Smith failed to produce of a copy of the Private Annuity Agreement in response to discovery requests for all documents relating to her assets and liabilities prior to the preliminary injunction hearing. App. Ex. 219 (D. Stoelting 8.3.10 Decl. – Dkt. 103-2, at ¶ 12-14); App. Ex. 278 (Plaintiff's First Request for the Production of Documents to Relief Defendant Lynn Smith at paras. 1 -4; 9-11; 17).

503. L. Smith did not disclose the Annuity Agreement, or her and David Smiths' joint right to annuity payments of $489,932 a year beginning in 2015 on the court ordered Statement of Net Assets as of March 31, 2010. App. Ex. 259 (Lynn Smith 3/31/10 Net Asset Statement).

504. L. Smith did not disclose the existence of the Annuity Agreement during her May 27, 2010 deposition in this case despite being asked questions concerning her assets and the Smith Trust, including why the assets of the Smith Trust were listed as assets of David and Lynn

Smith in several financial statements reporting the Smiths assets and liabilities. App. Ex. 252 (See, e.g., Lynn Smith 5/27/10 Dep. at pp. 79-85).

505. L. Smith did not disclose the existence of the Annuity Agreement during her testimony before the Court at the preliminary injunction hearing on June 10, 2010. App. Ex. 272 (PI Tr. 271-420).

506. L. Smith did not disclose the existence of the Private Annuity Agreement in the affidavits she submitted to this Court on May 21, 2010 (Dkt. 23) , May 26, 2010 (Dkt. 34) and June 9, 2010, (Dkt. 69-1), in connection with the preliminary injunction hearing. App. Ex. 244, App. Ex. 254 and App. Ex. 260, respectively.

507. In a Financial Statement dated August 2008, the Smiths listed as part of their cash and securities assets in the Smith Trust. . App. Ex. 210 (Pl 00 3518); App. Ex. 252 (Lynn Smith 5/27/10 Dep. Ex. 10.).

508. A handwritten Financial Statement dated December 31, 2007 prepared by David Smith also listed assets the Smith Trust's assets, totaling $4,453,022 as one of the Smiths' assets. App. Ex. 252 (Lynn Smith 5/27/10 Dep. Ex. 13).

509. In a subscription agreement submitted on behalf of the Smith Trust, David Smith described himself as the "beneficiary" of the Smith Trust, stating: "David Smith, beneficiary of the David L. Smith and Lynn A. Smith Trust dated 8/4/04 as the principal shareholder and president and CEO of the McGinn, Smith & Co , a member of the NASD. McGinn. Smith is an investment banking firm that has served as an underwriter." App. Ex. 268 (PI Dep. Ex. 24 – Deerfield Subscription Agreement).

510. Thomas Urbelis, a lifelong friend of David and Lynn Smith, was appointed Trustee at the request of David Smith. App. Ex. 252 (L. Smith 5/27/10 Dep. at 37:19-38:7).

511. Urbelis was a lawyer whose specialty was municipal law, zoning and land use. App. Ex. 283 (T. Urbelis 6/1/10 Dep. at 6:11-7:8).

512. Urbelis recalled that it was either David or Lynn Smith but "probably" David Smith who asked him to be Trustee. App. Ex. 283 (T. Urbelis 6/1/10 Dep. at 10:3-8).

513. Urbelis made clear to David Smith that he would not take responsibility for preparing tax returns. He testified: "I wanted assurance that I was not going to be responsible for preparing tax returns… I make no bones about it. I don't understand it." App. Ex. 283 (Urbelis 6/1/10 Dep. at 12: 7-19).

514. From 2004 until his resignation in 2010, Urbelis routinely signed documents regarding the Smith Trust when David Smith or employees of McGinn Smith asked him to do so. See, e.,g, Dkt. No. 46-7.

515. Documents were sent to Urbelis from David Smith or McGinn Smith employees with instructions for him to sign them immediately and return them via overnight mail. *See, e.g.*, Dkt. 46-8.

516. Urbelis relied upon David Smith for all investment decisions for the Smith Trust. App. Ex. 283 (Urbelis 6/1/10 Dep. at 12:20-14:18).

517. Urbelis signed letters of authorization permitting transfers of approximately $297,786 from the Smith Trust to accounts in the name of either David or Lynn Smith. App. Ex. 275 (Dkt. 46, Ex. 1).

518. Urbelis understood that the money was for payment of the Smith Trust taxes, but he did not know what the Smiths did with the money after he sent it to them. App. Ex. 283 (Urbelis 6/1/10 Dep. at 52:1-53:8).

519. When asked what Urbelis did to manage the Smith Trust, L. Smith stated: "He pays the – well, he signs some things so we can pay the taxes on the trust and I don't think there is anything else he does." App. Ex. 252 (L. Smith 5/27/10 Dep. at 38:16-20).

520. Geoffrey Smith, one of the two named beneficiaries of the Smith Trust, did not learn of the Smith Trust until Thanksgiving 2004, when David Smith told Geoffrey Smith that he and L. Smith had created a trust for Geoffrey and Lauren Smith that was valued at approximately $4 million funded from Charter One stock. App. Ex. 248 (G. Smith 11/16/11 Deposition at 109:12-25).

521. During this conversation, Davis Smith showed Geoffrey Smith the Declaration of Trust. App. Ex. 248 (G. Smith 11/16/11 Deposition at108:19-111:25).

522. David Smith did not discuss the role of the Trustee, Thomas Urbelis, with Geoffrey Smith during this conversation. App. Ex. 248 (G. Smith 11/16/11 Deposition at 112:6-9).

523. Geoffrey Smith did not discuss the Smith Trust with this mother. App. Ex. 248 (Geoffrey Smith 11/16/11 Deposition at 112:17-23; 121:9-11).

524. Geoffrey Smith stated that he "never" had a discussion with his parents about the fact that the Smith Trust had entered into an annuity agreement with his parents that entitled them to yearly payments of $489,000. App. Ex. 248 (G. Smith 11/16/11 Deposition at 114:10-16; 125:9-23).

525. Geoffrey Smith had no discussions with Thomas Urbelis, the Trustee of the Smith Trust from 2004 until 2010. App. Ex. 248 (G. Smith 11/16/11 Deposition at 113:3-21).

526. When Geoffrey Smith was considering a distribution of approximately $200,000 to $300,000 from the Smith Trust in 2009 to start a business venture, he discussed it with his

father, David Smith, not with the Trustee, David Smith. App. Ex. 248 (G. Smith 11/16/11 Deposition at 123:7-124:15).

527. Neither David nor Lynn Smith ever informed their daughter Lauren Smith that she was the beneficiary of the Smith Trust, containing over $4,000,000 in assets. App. Ex. 256 (Lauren Smith 11/28/11 Deposition at 43:8-15; 46:6-8).

528. Lauren Smith had no conversations whatsoever with her parents about the Smith Trust. App. Ex. 256 (Lauren Smith 11/28/11 Deposition at 43:8-15; 46:6-8).

529. The Smith family was "close." App. Ex. 256 (Lauren Smith 11/28/11 Deposition at 21:9). Lauren Smith spoke with her parents about five times a week during the period from 2006 to 2009 when she lived in the Boston, Massachusetts area. App. Ex. 256 (Lauren Smith 11/28/11 Deposition at 21:10-12). Lauren Smith knew Thomas Urbelis, the Smith Trust Trustee her entire life. App. Ex. 256 (Lauren Smith 11/28/11 Deposition at 42:22-25).

530. Lauren Smith never spoke with the Smith Trust trustee, Thomas Urbelis, about the Smith Trust. App. Ex. 256 (Lauren Smith 11/28/11 Deposition at 43:5-7; 46:24-47:2).

531. Lauren Smith was unemployed and collected unemployment insurance for approximately one and a half years after the Smith Trust was created. App. Ex. 256 (Lauren Smith 11/28/11 Deposition at 12: 2-7).

532. Lauren Smith never withdrew any money from the Smith Trust. App. Ex. 256 (Lauren Smith 11/28/11 Deposition at 43:8-15; 46:6-80.

533. Lauren Smith learned about the existence of the Smith Trust and the fact that she was a named beneficiary from a brief conversation with her brother Geoffrey Smith one Thanksgiving sometime after the Smith Trust was created. App. Ex. 256 (Lauren Smith 11/28/11 Deposition at 43:16- 44:4).

534. Geoffrey Smith recalled the conversation with Lauren Smith occurring over the Thanksgiving week-end in 2004 when he first learned of the Smith Trust. App. Ex. 248 (G. Smith 11/16/11 Deposition at119:19-120:5).

535. Geoffrey Smith told Lauren Smith the trust was worth about $4 million but he did not recall discussing with her whether they would be able to use the funds in the Smith Trust. App. Ex. 248 (G. Smith 11/16/11 Deposition at 120:13-121:4).

536. Geoffrey Smith told Lauren Smith: "It wasn't money that was going to be touched." App. Ex. 256 (Lauren Smith 11/28/11 Deposition at 43:18-23).

537. Lauren Smith understood from Geoffrey Smith that the money was supposed to be for their future but they "did not get into details" when he told her about the Smith Trust. App. Ex. 256 (Lauren Smith 11/28/11 Deposition at 45:20-23).

538. Lauren Smith never spoke with her parents about the Smith Trust after learning of it. App. Ex. 25 (Lauren Smith 11/28/11 Deposition at 46:6-8).

539. Between March 27, 2007 and May 27, 2009, L. Smith sent 19 checks totaling $22,100 to Lauren Smith. Most of the checks were in the amount of $1,000. A number of the checks indicate they are for rent. App. Ex. 224 (Dep. Ex. 417).

540. Lauren Smith "went through a little bit of a rough period" and her parents helped her pay her rent in Boston for a year. App. Ex. 256 (Lauren Smith 11/28/11 Deposition at 84:17-19).

541. When asked why she didn't withdraw money from the Smith Trust during this period, Lauren Smith stated, in part: "I didn't know I had access to the money. The trust had been set up for my future…" App. Ex. 256 (Lauren Smith 11/28/11 Deposition at 85:5-12).

542. Prior to April 2010, when the Smith Trust was frozen, the only individuals who benefitted from distributions from the Smith Trust were David and Lynn Smith. App. Ex. 275 (Dkt, 46, Ex. 1 - Summary of Smith Trust Distributions).

543. In April 2010, Geoffrey Smith, after a conversation with David Smith, caused a transfer of $95,000 from the Smith Trust to L. Smith's checking account, $66,500 of which was used to pay the Smiths federal income taxes, $$8,500 of which was used to pay the Smiths' New York state taxes and $20,000 of which was used for payment of the Smith Trust's taxes. App. Ex. 271-273 (PI Tr. 101; 320-321; 397; 416; 463; 513-16); App. Ex. 252 (L. Smith 5/27/10 Deposition at 92:19-95:2); App. Ex. 269 (PI Dep. Ex. 15) ;App. Ex. 214 (D. Smith Answer to SAC, ¶ 21); App. Ex. 255 (Lynn Smith Answer to SAC, ¶ 130).

544. L. Smith stated that if she needed money to pay her personal taxes, her son and daughter would definitely take money from the Smith Trust to pay the taxes. App. Ex. 252 (L. Smith 5/27/10 Deposition at 100:16-23).

545. David Smith also paid the Smith Trust's taxes one year from his own funds without reimbursement from the Smith Trust. App. Ex. 272 (PI Tr. 464-66).

IX. FRAUDULENT TRANSFERS BY THE MCGINNS AND SMITHS

A. The Smiths Engaged in Additional Fraudulent Transfers of Their Assets in 2009

546. In a 2007 document discussing the Four Funds, David Smith stated:

> 5. A major negative on the cash flow has been that a number of the investments got into trouble early and there was no attempt to adjust the coupons on the bond. … I approached the problem by making more equity type investments that would provide greater yields, but with obviously more risk. For the most part, these riskier investments have only aggravated the problem.
> 6….In addition, we felt that other investment returns would make up for the shortfall in cash flow from the alarm contracts. That proved not to be the case.
> 7. One of the more troubling aspects of the investments has been my willingness to make substantial investments in affiliated entities, both because they were

> available and in some cases, such as Coventry, new investments were needed to support part investments.…In all cases, this has proved to be a poor decision and has not only aggravated our cash flow problems, but puts us in some legal jeopardy as well.

547. App. Ex. 129 (Dep. Ex. 530 at 3 D. Smith 10.10.09 letter to Kaplowitz).

548. In 2008-2009, McGinn Smith found itself in need of capital for both working capital purposes and regulatory purposes. App. Ex. 218 (D. Smith Responses to Plaintiff's First Request for Interrogatories, ¶ 16).

549. Internal MS & Co. emails in 2009, including many by McGinn and Smith, reveal a constant need to raise millions of dollars, a growing desperation to make payroll, meet interest payments and assuage investors complaining of a Ponzi scheme, in order to keep their house of cards from collapsing. For example, on February 24, 2009, Smith emailed McGinn regarding an upcoming payroll. He stated: "We have been living on the edge for some time and Tim's deals have kept us alive by fronting our profit. However, the $200,000 + that we are losing every month is just too difficult to keep pace with." App. Ex. 145**.**

550. On February 25, 2009, another MS & Co. Partner emailed Smith: "In our many conversations over the last year, I came to understand the depths to which the firm has sunk relative to its revenue." App. Ex. 348.

551. In 2009, after an investigation by the Financial Industry Regulatory Authority (FINRA) into MS & Co. had commenced, and as Smith and McGinn learned that they and their firm were named as Respondents in a number of FINRA arbitrations filed by investors, they began to move assets to their wives. See below**.**

552. L. Smith knew in 2009 that a number of FINRA arbitrations had been filed against McGinn Smith and it concerned her. App. Ex. 272 (PI Tr. at 295:8-25); App. Ex. 252 (L. Smith 5/27/10 Deposition at 22:18-23).

553. L. Smith understood that the FINRA arbitrations filed by customers sought money and she was concerned that if those arbitrations were successful she could lose money. App. Ex. 272 (PI Tr. at 296:1-23).

554. David and Lynn Smith began moving assets that had been jointly held into solely L. Smith's name. App. Ex. 217 (D. Smith Responses to Requests for Admissions, ¶ 42. See also below.

555. In a January 7, 2009 letter from David Smith to Martin Finn, of Lavelle & Finn, LLP, the Smiths' financial planner, David Smith stated: "Also, I am interested in reducing my exposure to personal liability as a result of the very litigious business that I am in. You mentioned transferring my share in the Vero Beach and Saratoga residence to Lynn or a Trust." App. Ex. 305 (1/7/2009 Letter from D. Smith to M. Finn. - SEC-USAO_NDNY-P-0000556-561).

556. In a letter misdated January 11, 2009 (instead of 2010), after his customer David Chang had been awarded a judgment of over $800,000 against David Smith and others, David Smith stated:

> I am beginning to realize that by not taking those fees to pay for various liabilities, including attorney's fees, that I am foolishly compromising the rest of my life. I will be forever burdened with at the very least a lien on my wage, and there is some risk that the equity that is not in my wife's name or protected by Trusts could be served with a lien to satisfy the judgments. This equity is primarily in the form of two properties, my home in Saratoga (jointly owned) and my home in Florida (transferred to my wife solely last April).

App. Ex. 213 (Dep. Ex. 610 - D.Smith Letter to David Franceski).

557. In an e-mail dated January 14, 2009 from David Smith to Timothy McGinn, Smith stated that "Lynn and I have to shift money around between us." App. Ex. 349.

E. The Smiths' Fraudulent Conveyance of Their Joint Checking Account

558. From the beginning of their marriage in 1968, David and Lynn Smith maintained a joint checking account into which they deposited both of their paychecks and from which they paid their household bills. App. Ex. 254 (Lynn Smith 5/21/10 Aff. at ¶ 16); App. Ex. 252 (Smith 5/27/10 Deposition at 30:13-22).

559. David Smith's payroll checks from McGinn Smith were routinely deposited into the joint checking account. App. Ex. 272 (PI Tr. at 282).

560. In or about July 2009, L. Smith opened a checking account at the Bank of America in her name only. App. Ex. 272 (PI Tr. at 282); App. Ex. 252 (L. Smith 5/27/10 Deposition at 31:22-32:4).

561. David and Lynn Smith caused the assets in their joint checking account at the Bank of America to be transferred to the BOA checking account opened in L. Smith's name alone. App. Ex. 214 (D. Smith Answer to SAC, par. 23).

562. From that time forward, David Smith's McGinn Smith payroll checks began to be deposited into the L. Smith checking account. App. Ex. 272 (PI Tr. at 282).

563. Between July 15, 2009 and April 8, 2010, David Smith payroll checks totaling $129,096.67 were deposited into the L. Smith checking account. App. Ex. 275 (Daniello 6/3/10 Supp. Decl., Ex. C; - Dkt. No. 46).

564. L. Smith stated that she opened the checking account in her name only because she wanted "to have some independence" and wanted to be able to write checks to her

unemployed daughter without David Smith looking over her shoulder, not to shield assets from creditors. App. Ex. 272 (PI Tr. at 375-376; 405).

565. However, L. Smith had been writing $1,000 checks to her daughter Lauren Smith to assist in rent payments from the Smiths' joint checking account almost every month from at least March 2007 without any need for a separate checking account. See below.

566. The Court found L. Smith's testimony concerning the reason for transfer of the Vero Beach property and her reasons for transferring the joint checking account into her name only "incredible." SEC v. McGinn Smith et al., 752. F. Supp.2d 194 at 203, fn. 13; 7/7/10 MDO, Dkt. No. 86 at p. 9, fn 13.

C. The Smiths' Fraudulent Transfer of Vero Beach House

567. In September 2009, the Smiths also transferred title of their Vero Beach residence, which had been held in both their names since its purchase in 2001 to L. Smith's name alone. App. Ex. 214 (D. Smith Answer to SAC, paras. 18; 22); App. Ex. 255 (Lynn Smith Answer to SAC, ¶ 122).

568. L. Smith testified that in 2009 she "demanded that he [David Smith] put the house solely in my name because I funded the purchase of the house." App. Ex. 252; App. Ex. 272 (L. Smith 5/27/10 Deposition at 21:8-13. See also, PI Tr. at 280-281).

569. When asked why she waited nine years after the purchase of the house to demand that it be placed in her name alone, Ms. Smith testified, in part, that: "In light of what was going on in the economy, I wanted the house in my name to protect it." App. Ex. 252 (L. Smith 5/27/10 Deposition at 21:25-22:12).

570. The transfer of the Vero Beach house was contrary to advice the Smiths had received from their estate planning lawyer that "it was more beneficial for you to own those

properties [the Vero Beach and Saratoga Springs homes] jointly as tenants by the entirety." App. Ex. 252 (L. Smith 5/27/10 Deposition at 21:25-22:12); App. Ex. 175 (Dep. Ex. 438 – 1.28.09 Letter from Finn to the Smiths).

571. David Smith testified at the criminal trial that the Vero Beach house was worth $2.2 million, and that he transferred it to his wife's name . App. Ex. 108 at 3205. In 2009, Smith was aware of arbitrations. App. Ex. 108 at 3207-3208. Smith wrote that he shouldn't be forced to share his earning for the rest of his life with the likes of Dr. Chang, the investor who received the large FINRA award. App. Ex. 108 at 3208.

D. Timothy and Nancy McGinn's Fraudulent Conveyance of Their Primary Residence

572. Timothy McGinn purchased the Niskayuna house in his name alone in 2003. App. Ex. 267 (N. McGinn 11/28/11 Dep. at 15:19-16:2); App. Ex. 401 (Dep. Ex. 401); App. Ex. 230 (Dep. Ex. 402).

573. Timothy McGinn and Nancy McGinn began living together at that time. App. Ex. 267 (N. McGinn 11/28/11 Dep. at 15:18-24).

574. Timothy McGinn and Nancy McGinn were married in July 2006. App. Ex. 267 (N. McGinn Dep. at 15:13-15).

575. Nancy McGinn did not contribute any money to the marriage or for household expenses after she stopped working, in approximately 2004, through 2010. App. Ex. 267 (N. McGinn Dep. at 13:14-25; 18:14-19:13).

576. On October 13, 2009, Timothy McGinn attended the testimony of William Lex, a McGinn Smith broker, in connection with a FINRA arbitration hearing arising from a customer filed against Timothy McGinn, David Smith, McGinn Smith Advisors, McGinn Smith Capital

Holdings Corp., Lex, and others. App. Ex. 350 (FINRA Arbitration No. 08-04924, Dispute Resolution Award dated December 31, 2009.

577. The claimants were seeking compensatory damages of $2,577,000, commissions, interest, attorneys' fees and punitive damages. App. Ex. 350 (FINRA Arbitration No. 08-04924, Dispute Resolution Award dated December 31, 2009).

578. Timothy McGinn emailed Nancy McGinn from his iPhone: "Lex is very poor witness. We have important points to make. David and I will do so Thurs & Friday. I hate the retail business.' App. Ex. 223 (Dep. Ex. 400).

579. On October 19, 2009, Timothy McGinn transferred title to his residence located in Niskayuna, New York to his wife, Nancy McGinn, for one dollar consideration. App. Ex. 230 (Dep. Ex. 402 - Quitclaim Deed dated October 19, 2009 transferring Niskayuna residence from Timothy McGinn to Nancy McGinn;); App. Ex. 282 (T. McGinn's Response to SEC Request for Admissions, ¶ 59).

580. The Niskayuna residence was a five bedroom home which Timothy McGinn bought for approximately $600,000 in 2003 and put approximately $235,000 in improvements into the home. App. Ex. 229 (Dep. Ex 401); App. Ex. 267 (N. McGinn 11/28/11 Dep. at 37:5-38:5. 66:6-22).

581. On December 31, 2009, a FINRA arbitration panel held that McGinn Smith and Co, Lex and David Smith were jointly and severally liable to the claimants for $805,111 in compensatory damages and other fees. Timothy McGinn was not found liable for any payments. App. Ex. 350 (FINRA Arbitration No. 08-04924, Dispute Resolution Award dated December 31, 2009). Nancy McGinn knew that Timothy McGinn was called to testify on a number of

occasions in connection with a FINRA investigation. App. Ex. 267 (N. McGinn 11/28/11 Dep. at 31:9-32:2).

582. Timothy McGinn brought up the idea of making the transfer of the Niskayuna residence in October 2009. App. Ex. 267 (N. McGinn 11/28/11 Dep. at 41:17-22; 74:15-75:3).

583. Between October 29, 2003 and March 15, 2010, Timothy McGinn made payments totaling at least $65,000 to Nancy McGinn for payment of common living expenses and taxes. App. Ex. 267 (N. McGinn 11/28/11 Dep. at 44:17- 49:13).

584. Timothy McGinn maintained a separate checking account during this period into which his McGinn Smith paychecks were deposited. App. Ex. 267 (N. McGinn 11/28/11 Dep. at 49:14-20); App. Ex. 231 (Dep. Ex. 403 – Summary Chart re transfers to Nancy McGinn).

585. When the McGinns purchased a house in Florida in approximately 2008, they placed it in both Timothy and Nancy McGinn's name. App. Ex. 267 (N. McGinn 11/28/11 Dep. at 60:6-22).

E. Fraudulent Transfers From the Smith Trust After July 7, 2010

586. Five days after the Smith Trust was temporarily unfrozen on July 7, 2010, Lauren Smith requested that $75,000.00 be wired to her from the Smith Trust as a down payment to her parents for the purchase of the Sacandaga Lake property. App. Ex. 256 (Lauren Smith 11/28/11 Deposition at 55:23- 56:15).

587. Lauren Smith was unaware of any plans to have the Smith Trust purchase the Sacandaga Lake property before the Smith Trust was unfrozen. App. Ex. 256 (Lauren Smith 11/28/11 Deposition at 62:3-5).

588. On the same date, Lauren Smith requested that $1,800 be withdrawn from the Smith Trust and wired to her for use as a rent security deposit and that $6,200 wired to her to pay

off credit card debt she had accumulated. App. Ex. 232 (Dep. Ex. 412 (TR00003250); App. Ex. 256 (Lauren Smith 11/28/11 Deposition at 53:22-55:22).

589. Lauren Smith received $83,500 from the Smith Trust after July 7, 2010. App. Ex. 279 (Smith Trust Trustee, G. Smith and Lauren Smith Answer to SAC, ¶ 151); App. Ex. 285 (Dkt; No. 142-2 (Trustees' Verified Accounting)).

590. That amount included the $75,000 that she gave to L. Smith as a partial down payment for the Sacandaga Lake property. App. Ex. 285.

591. On July 9, 2010, $95,741 was wired from the Smith Trust to the Dunn Law Firm. App. Ex. 228 (Dep. Ex. 371 - TR000063-66); App. Ex. 285 (Trustees' Verified Accounting - Dkt. 142-2).

592. On July 12, 2010, $96,500 was wired from the Smith Trust to Geoffrey Smith. App. Ex. 228 (Dep. Ex. 371 -TR000063-66); App. Ex. 285 (Trustees' Verified Accounting – Dkt. 142-2); App. Ex. 248 (G. Smith 11/16/11 Deposition at 156:3 16).

593. Geoffrey Smith used $75,000 of those monies to pay his mother L. Smith a partial down payment for the Sacandaga Lake property and used the remaining $21,500 to pay off credit card debt, for health insurance and other small uses. App. Ex. 248 (G. Smith 11/16/11 Deposition at 156:3-13).

594. On July 16, 2010, $200,000 was transferred from the Smith Trust to Geoffrey Smith, which he described as an investment by the Smith Trust in his new business venture Capacity One Management, LLC. App. Ex. 228 (Dep. Ex. 371 -TR000063-66); App. Ex. 285 (Trustees' Verified Accounting- Dkt. 142-2); App. Ex. 248 (G. Smith 11/16/11 Deposition at 157:15-159:14); App. Ex. 279 (Smith Trust Trustee, G. Smith and Lauren Smith Answer to SAC, ¶ 150).

595. On July 20, 2010, David Smith faxed documents relating to the Annuity Agreement to David Wojeski, the Smith Trust Trustee, including a "Private Annuity Contract" signed by David Smith on October 19, 2004 and a contract term sheet evidencing the Smith Trust's obligation to make yearly payments of $489,932 to the Smiths beginning in September 2015. App. Ex. 241 (Dep. Ex. 472 (TR0000237-241).

596. Wojeski's time records reflect that on July 20, 2010, he read and did research regarding private annuity trusts. App. Ex. 359 (Dep. Ex. 473 -TR0000406-408).

597. Geoffrey Smith learned of the Annuity Agreement no later than July 20, or July 21, 2010 when he received a telephone call from Wojeski asking about the Annuity Agreement. App. Ex. 248 (G. Smith 11/16/11 Deposition at 116:6-117:14).

598. Following the call, Geoffrey Smith spoke with David Smith about the Annuity Agreement on either July 20 or July 21, 2010. App. Ex. 248 (G. Smith Deposition at 117:8-22; 138:11-16).

599. Geoffrey Smith and David Smith met with Wojeski at Wojeski's office on July 21, 2010. App. Ex. 248 (G. Smith 11/16/11 Dep. at 148:19:150:2); App. Ex. 249 (G. Smith 12/9/11 Dep. at 231:11-232:14); App. Ex. 359 (Dep. Ex. 473 (TR0000406-408)).

600. Geoffrey Smith and Wojeski performed certain calculations to determine how much money the Smith Trust would need to earn to meet its annuity payment obligations to the Smiths. App. Ex. 249 (G. Smith Dep. at 222:22-224:9).

601. On July 22, 2010, L. Smith executed an Indenture releasing all rights to the Sacandaga Lake property to the Smith Trust. App. Ex. 228 (Dep. Ex. 371 -TR000063-66); App. Ex. 242 (Dep. Ex. 474 -TR0000289-294).

602. On July 22, 2010, $2,000,000 was wired from the Smith Trust to a newly created bank account at Kinderhook Bank. App. Ex. 228 (Dep. Ex. 371 -TR0000063-66); App. Ex. 285 (Wojeski Verified Accounting - Dkt. 142-2).

603. On July 23, 2010, $449,878 was wired from the Smith Trust's Kinderhook Bank account to L. Smith as the remainder of the payment for the Smith Trust's purchase of the Sacandaga Lake property. App. Ex. 248 (G. Smith 11/16/11 Deposition at 154:22-155:5); App. Ex. 228 (Dep. Ex. 371 -TR0000063-66); App. Ex. 285 (Wojeski Verified Accounting - Dkt. 142-2); App. Ex. 255 (Lynn Smith Answer to SAC, ¶ 149); App. Ex. 279 (Smith Trust Trustee, G. Smith and Lauren Smith Answer to SAC, ¶ 149).

604. On July 22, 2010, Wojeski and David and Lynn Smith also entered into an "Indemnity and Hold Harmless Agreement" pursuant to which David and Lynn Smith agreed to release, indemnify and hold harmless Wojeski from any and all current and future claims arising out of the Smith Trust including relating to any "financial transactions, investments, obligations or distributions, and the potential tax consequences thereof, relating to said Trust, its Donors and its beneficiaries…" App. Ex. 240 (Dep. Ex. 462 - TR0000242).

605. After the asset freeze went into effect, Geoffrey Smith made a number of payments for his parents' living expenses. App. Ex. 249 (G. Smith 12/9/11 Dep. at 235:23-254:9).

606. On July 15, 2010, L. Smith gave Geoffrey Smith a check in the amount $28,500 in partial repayment of these expenditures out of the above-referenced proceeds she received from the Smith Trust for the sale of the Sacandaga Lake property. App. Ex. 249 (G. Smith 12/9/11 Dep. at 253:4-254:9).

607. The Receiver subsequently sold the Sacandaga Lake property, pursuant to Court order, for $575,000.00. App. Ex. 302 (Receiver Report filed 3.19.14 -Dkt. 687)

608. Geoffrey Smith submitted an affidavit, dated October 5, 2010, in opposition to the Commission's motion for reconsideration of that portion of the Court July 7, 2010 MDO lifting the asset freeze on the Smith Trust, in which he stated that he did not learn of the existence of the annuity agreement until "late July, only after the SEC claims to have discovered the document for the first time." App. Ex. 247 G. Smith 10/5/10 Aff. at ¶ 5 (Dkt. 148).

609. The SEC had previously submitted an Declaration of David Stoelting stating that the SEC first learned of the existence of an annuity agreement on July 22, during a telephone call with the Trust's attorney Jill Dunn and did not obtain a copy of the Annuity Agreement until July 27, 210 when it received a copy for the first time from Thomas Urbelis. App. Ex. 219 (D. Stoelting 8/3/10 Decl. at ¶ 4. (Dkt. No. 103-2)).

610. As the facts set forth above, Geoffrey Smith's statement that he did not learn of the Annuity Agreement until after the SEC learned of it was false as he learned of it before the July 22 telephone call between Jill Dunn and David Stoelting.

F. Recent Efforts By David and Lynn Smith to Defraud the Court and Their Creditors

611. On October 18, 2013, L. Smith filed a motion with this Court requesting a modification of the asset freeze to provide her with monthly living expenses of $4,144 due to her "financial hardship" and to provide $100,000 in partial payment of counsel fees. App. Ex. 261 (Dkt. 610).

612. In her Affidavit submitted in support of this motion, L. Smith stated that: "Meeting simple daily living expenses has become so difficult that on September 12, 2013, I applied for food stamps. App. Ex. 261 (L. Smith 10/18/13 Aff. at ¶ 5 -Dkt. 610-1).

613. She further stated that she had a monthly income of $965, plus $50 in food stamps, had at least $17,000 in credit card debts, was faced with a $900,000 sanction order in this case, owed $441,573 in legal fees and that she currently had monthly expenses of $5,159. App. Ex. 261(L. Smith Aff. at paras.7-9; 13; 30 - Dkt. 610-1).

614. The Court denied that motion on January 8, 2014. Dkt. 667.

615. On January 3, 2014, L. Smith submitted an Affidavit in support of a motion by the Smith Trust to amend the Smith Trust to cancel the Private Annuity Contract. In that Affidavit, L. Smith stated that she and her husband David Smith wanted to cancel the annuity contract, which entitled her and David Smith to yearly annuity payments of $489,932, beginning in September 2015, or, alternatively, "renounce all rights to future payments from the Trust." App. Ex. 258 (L. Smith 1/3/14 Affidavit at paras. 2-3 -Dkt. 662).

616. L. Smith stated that her reason for cancelling the annuity contract, or alternatively renouncing her and her husband's rights to substantial annuity payments, was because the federal gift tax exclusion had increased from $1,500,000 in 2004 to $5,250,000 in 2013and since the principal remaining in the Smith trust is less than the current gift exclusion amount there is no longer any need for the annuity agreement. App. Ex. 258 (L. Smith 1/3/14 Affidavit at ¶ 10-11 - Dkt. 662).

617. She further stated that: "I believe the Trust Amendment will allow the Trust to continue with its original purpose, which his for the benefit of my children." App. Ex. 258 (L. Smith 1/3/14 Affidavit at ¶ 12 - Dkt. 662).

618. L. Smith did not make any reference to any actual or potential judgments against her and David Smith as a reason for renouncing their right to annuity payments nor did she

explain why she was renouncing her rights to these payments given her current purportedly dire financial condition. App. Ex. 258 (L. Smith 1/3/14 Affidavit -Dkt. 662).

Dated: New York, NY
July 8, 2014

Respectfully submitted,

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UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION,	:	
Plaintiff,	:	
v.	:	**10 Civ. 457 (GLS/CFH)**
McGINN, SMITH & CO., INC., et al.,	:	
Defendants.	:	

PLAINTIFF'S APPENDIX TO STATEMENT OF MATERIAL FACTS

David Stoelting
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SECURITIES AND EXCHANGE COMMISSION
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July 8, 2014

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