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 REPLY MEMORANDUM OF LAW IN SUPPORT OF MOTION FOR SUMMARY JUDGMENT

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Plaintiff Securities and Exchange Commission respectfully submits this reply memorandum of law in response to the submissions of David Smith; Lynn Smith; and the David and Lynn Smith Irrevocable Trust U/A 08/08/04, Geoffrey Smith and Lauren Smith opposing plaintiff's motion for summary judgment, and David Smith's cross-motion on damages.[1]

PRELIMINARY STATEMENT

Despite the vehement tone of their opposition papers, David Smith, Lynn Smith and the Smith Trust present little evidence that would support a jury verdict in their favor. And at this point in time – following a three-day evidentiary hearing in June 2010, several years of discovery, sweeping sanctions for concealing relevant material, three (unsuccessful) appeals to the Second Circuit, and a lengthy trial in the parallel criminal case – they have certainly had a sufficient opportunity to develop favorable evidence. Indeed, their responses to the SEC's Statement of Material Facts ("SEC SMF") shows that there are no genuine issues of fact remaining. *See* Exhibits A, B, C, and D (summary charts showing facts in SEC SMF that are admitted and deemed admitted). As a result, summary judgment should be entered on all claims.

First, David Smith attempts the impossible by arguing that he should not be found liable in the civil case when a jury previously found him guilty beyond a reasonable doubt in the criminal case. In addition, Smith's argument that he should not be subject to a substantial disgorgement order, when the victims of his massive fraud have lost nearly $100 million, should be rejected.

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[1]Timothy McGinn and Nancy McGinn have not submitted any opposition to the SEC's summary judgment motion. As a result, summary judgment should be entered against them on the relevant claims in the SAC, and the requested relief imposed. *See Pedroso v. Syracuse Cmty. Health Ctr.*, 2014 WL 3956570, *6 (N.D.N.Y. Aug. 13, 2014) ("in this District, where a non-movant has willfully failed to respond to a movant's properly filed and facially meritorious memorandum of law (submitted in support of its motion for summary judgment), the non-movant is deemed to have 'consented' to the legal arguments contained in that memorandum of law")

Second, Lynn Smith's argument that she alone controlled the Stock Account that was in her name is contradicted by overwhelming evidence that David Smith controlled every aspect of the Stock Account for his personal and professional benefit. As a result, the Stock Account should be treated as an asset of David Smith's and used to satisfy the requested judgment against him.

Finally, the Smith Trust simply cannot escape the significance of the Annuity Agreement, which Lynn Smith and the Trust recognized by trying so hard to conceal it from discovery in 2010. The overwhelming weight of the evidence shows that the Smith Trust was a sham and nothing more than an instrument to conceal assets for the benefit of David and Lynn Smith. As a result, its assets should be applied to satisfy David Smith's requested judgment.

ARGUMENT

I. THE EVIDENCE WARRANTS SUMMARY JUDGMENT AGAINST DAVID SMITH

The SEC's summary judgment motion offers overwhelming evidence of David Smith's violations of the federal securities laws. In response, Smith must come forward with specific facts showing a genuine issue of material fact for trial. A dispute of fact is "genuine" if "the [record] evidence is such that a reasonable jury could return a verdict for the nonmoving party." *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248 (1096). A dispute of fact is "material" if it "might affect the outcome of the suit under the governing law." *Id.*

Smith's submission fails to raise any disputes of material fact, and it is inconceivable that a jury could render a verdict in his favor. As a result, the SEC's summary judgment motion should be granted on the first four claims in the Second Amended Complaint ("SAC") against David Smith.

A. Smith Does Not Dispute the Vast Majority of the SEC's SMF

The SEC's SMF contains extensive and detailed evidence of Smith's fraudulent conduct in connection with the Four Funds, Trust and MSTF offerings, in addition to his convictions in the parallel criminal action. In particular, the SEC SMF details, through an extensive analysis of dozens of bank accounts, the undisclosed payments to redeem investors in prior offerings (¶¶ 75-97); the unauthorized investments in affiliates (¶¶ 98-119); the undisclosed policy linking redemptions to new investor funds (¶¶ 124-136); the misuse of Trust Offering proceeds (¶¶ 145-150); and the constant net capital violations (¶¶ 152-158). Further evidence of Smith's fraudulent conduct came from the criminal trial (¶¶ 159-330).

Smith admits 170 of the SEC's material facts addressing the fraud. *See* Ex. A. With regard to another 113 of the SEC's SMF, Smith fails to adhere to Local Rule 7.1(a) (3), which provides that "[e]ach denial shall set forth a specific citation to the record where the factual issue arises. . . . The Court shall deem admitted any properly supported facts set forth in the Statement of Material Facts that the opposing party does not specifically controvert." NDNY Local Civil Rule 7.1(a)(3). "[T]his court has often enforced Local Rule 7.1(a)(3) by deeming facts set forth in a moving party's statement to be admitted . . . where the nonmoving party has willfully failed to properly respond to that statement[.]" *Pedroso v. Syracuse Cmty. Health Ctr*, 2014 WL 3956570, at *6 (N.D.N.Y. Aug. 13, 2014). *See also* Fed. R. Civ. P. 56(e)(2) ("If a party fails to . . . .properly support an assertion of facts or fails to properly address another party's assertion of fact as required by Rule 56(c), the court may . . . consider the fact undisputed for purposes of the motion"); Advisory Committee Notes (this rule "reflects the 'deemed admitted' provisions in many local rules").

Smith merely lists boilerplate objections such as "improperly states a legal conclusion,"

"contains legal argument, opinion, and conclusory statements," "contains improper characterization," "irrelevant and immaterial," or "vague, overbroad and otherwise irrelevant." These *pro forma* objections – without citation to any record evidence – should be deemed admissions. Moreover, Smith's failure to cite to evidence is especially striking because Smith has had access to the vast record in both the civil and criminal cases. His failure to identify a single piece of evidence as a basis for his denials for 113 facts should be taken as a concession that no such evidence exists.

Failure to adhere to Local Rule 7.1(a)(3) is a basis to grant summary judgment, and the Second Circuit has affirmed summary judgment orders when there has been a "failure to comply with the local rules governing summary judgment submission in the Northern District of New York. Specifically, . . . Local Rule 7.1(a)(3)." *New York State Teamsters Conf. Pension and Ret. Fund v. Express Service, Inc*., 426 F.3d 640, 648 (2d Cir. 2005). *See also Alzawahra v. Albany Medical Center*, et al., 546 Fed.Appx. 53, 54 (2d Cir. 2013) ("we have previously affirmed district court orders granting summary judgment where the opposing party failed to adhere to the requirement of [Local Rule 7.1(a)(3)].)" In *New York Teamsters*, the non-moving party – like Smith – filed "mostly conclusory denials of [movants'] factual assertions and failed to include any record citations." *See* 426 F.3d at 648. As a result, "[t]he district court, applying Rule 7.1(a)(3) strictly, reasonably deemed [movants'] statement of facts to be admitted[.]"). Similarly, Smith's denials without citations to any evidence should be deemed admissions. When these are combined with the SEC's SMF that Smith admits, it is apparent that no issues of material fact exist.

B. Collateral Estoppel on the First through Fourth Claims is Warranted

Smith's argument that his convictions for conspiracy, mail fraud, wire fraud and securities fraud have no collateral estoppel effect should be rejected. His primary argument – that "there are numerous differences" between the Superseding Indictment ("Indictment") and the SAC – is plainly false. Smith Br. at 4. As demonstrated in the SEC's opening brief, the Indictment and the SAC concern the same defendants, the same offerings and the same violations. SEC Br. at 4-5. All of the conduct alleged in the Indictment is also contained in the SAC, with the exception of the tax fraud conduct. In any event, "[t]here is no case law that supports the proposition that a criminal indictment must match a civil complaint exactly in terms of parties and claims for there to be preclusive effect." *SEC v. Blackwell*, 477 F. Supp.2d 891, 900 (S.D.Ohio 2007).

The primary difference between the SAC and the Indictment is the time frames. Both the Indictment and the SAC cover conduct from September 2006 through 2009, but the SAC also includes conduct from September 2003 onward, when the first of the Four Funds offerings was launched. App. Ex. 6 (Indictment); App. Ex. 297 (SAC). As a result, the SAC contains more detail on the Four Funds offerings, which took place in September 2003 (FIIN), January and November 2004 (FEIN, TAIN), and October 2005 (FAIN), and raised more than $85 million. SEC SMF ¶¶ 9-11; App. Ex. 1 at 39 (Palen Ex. 3). The criminal case, however, also implicates the Four Funds, SEC SMF ¶¶ 159-173, and the SEC case implicates all of the Trust and MSTF offerings. SEC SMF ¶¶ 145-150. Smith's argument, therefore, that the civil and criminal cases covered different transactions is incorrect.

David Smith also argues that his acquittals are sufficient to raise a material fact. Smith Br. at 4-5. This is a red herring, however, because acquittals do not result in collateral estoppel.

Rather, it is his multiple securities fraud convictions, in addition to the conspiracy and mail and wire fraud, that are more than enough to justify collateral estoppel. "Convictions for mail fraud, wire fraud, securities fraud, and conspiracy to commit securities fraud suffice to establish claims for securities fraud based on the same facts in a related civil action." *SEC v. Bravata*, __ F. Supp.2d __, 2014 WL 897348, at *16 (E.D. Mich. 2014) (numerous citations omitted).

Smith's convictions on six counts of securities fraud by themselves are sufficient to grant summary judgment on the first four claims in the SAC. The jury instructions on the securities fraud counts track the elements of the antifraud provisions of the federal securities laws (§ 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5), and the jury found beyond a reasonable doubt that Smith was guilty on all six securities fraud counts. App. Ex. 58 at 42-50; App. Ex. 23 at 8-10.

Finally, Smith argues that the collateral estoppel effect of his conspiracy conviction is "ambiguous," and "must be resolved in favor of Mr. Smith," because the conviction could have been based on his intent to defraud either investors or FINRA. Smith Br. at 5. There is no ambiguity, however, in the conspiracy conviction: it supports collateral estoppel on the SAC's securities fraud charges regardless of whether the jury found his intent was to defraud investors or FINRA. As part of an overall scheme to defraud, the SAC alleges Smith's intent to defraud both FINRA and investors. App. Ex. 297 ¶¶ 107, 120 (FINRA); 39-106 (investors).

C. The Restitution Imposed in the Criminal Action is Irrelevant to the Appropriate Amount of Disgorgement in this Action

Smith argues that, if collateral estoppel applies, then "equity" mandates that his disgorgement be limited to the restitution ordered in the criminal action. Smith Br. at 6-9. Smith is wrong. Restitution and disgorgement are distinct concepts. No court has ever held that, under principles of collateral estoppel, restitution in a criminal case is binding on the same defendant in

a parallel SEC case.

As Smith points out, restitution in criminal cases is imposed pursuant to the Mandatory Victims Restitution Act ("MVRA"), which provides that "the court shall order restitution to each victim in the full amount of each victim's losses as determined by the court[.]" 18 U.S.C. § 3663A. The MVRA, however, applies only in criminal cases; it does not apply in SEC cases. And contrary to the specific procedural requirements of the MVRA, courts in SEC actions have broad equitable powers to fashion appropriate remedies when they find violations of the federal securities laws. SEC Br. at 14-16. In this case, where investor losses exceeds $80 million, a disgorgement order that is tied to the total amount raised minus the amount returned – the standard measure of disgorgement in offering fraud cases – is appropriate. *See* SEC Br. at 16-17.

The lack of transparency to the restitution number also shows that restitution is not an appropriate measure of disgorgement. Judge Hurd found that the US Attorney's Office did not prove a $30.2 million loss amount at trial, App. Ex. 26 at 5, but he did not identify any reasons. Instead, he stated without explanation that he would adopt the $6.3 million "loss amount" in the Probation Office's report, which remains nonpublic and under seal.[2] It is not at all clear how the Probation Office determined this loss amount; how the restitution amounts in the criminal judgments relate to the Probation Office's loss amount; which offerings the restitution order is intended to cover; and which victims are intended to receive payments.

In this case, the SEC has submitted uncontroverted evidence that total investor losses from the Four Funds, Trust and MSTF offerings are approximately $100 million. SEC Br. at 14. In addition, the SEC case, which includes the $85 million raised in the fraudulent Four Funds

[2] Smith touts the Probation Office's report but fails to mention that it is nonpublic. The docket sheet for the entries cited by Smith state: "This document has been electronically lodged with the Court and is viewable by ONLY the attorney for the government, the attorney for the defendant, and the presiding judge. Any further distribution or dissemination is prohibited."

offerings after September 2003, should have a much larger disgorgement figure than the criminal case, which was limited to offerings after September 2006.

Smith does not cite to any case where a court adopted a restitution order as the equivalent of disgorgement in a parallel civil case. In fact, courts have recognized that "restitution and disgorgement are separate remedies. . . . 'a disgorgement order might be for an amount more or less than that required to make the victims whole. It is not restitution.'" *SEC v. Hughes Capital Corp.*, 917 F. Supp. 1080, 1085 (D.N.J. 1996) (quoting *SEC v. Huffman*, 996 F.2d 800, 802 (5th Cir. 1993).

Smith vaguely invokes the "rules of equity" as support, but he fails to identify which rule of equity. In fact, nothing could be more inequitable than the disgorgement amount he advocates. Smith should not receive the benefit of this Court's equity when his knowing violations of the securities laws have caused hundreds of investors' large financial losses.

Smith also blames the SEC for not challenging the loss amounts proposed by the Probation Office. Smith Br. at 7. The SEC, however, never received the Probation Office report. In any event, the US Attorney's Office has appealed Judge Hurd's sentence. SEC SMF ¶ 56.

Finally, in support of his mootness argument, Smith refers to language in the Judgment stating that the "cash value" of assets distributed by the Receiver to the victims of Smith's crimes "may be deducted from the total restitution amount." Smith Br. at 8-9; App. Ex. 10 at 6. This provision, however, governs only the calculation of "the total restitution amount" and says nothing about disgorgement in the SEC case. To the extent this provision reduces Smith's restitution to zero – which Smith seems to imply – leaving the hundreds of victims of his fraud uncompensated, then the rationale for a larger disgorgement number is even more compelling.

D. Summary Judgment is Warranted on the Section 5 Claim

Smith does not dispute that the SEC has established a *prima facie* case of a violation of Section 5(a) and (c) of the Securities Act. To avoid liability, therefore, Smith must show that an exemption from registration was available. SEC Br. at 12-13. Instead, Smith argues that the Four Funds were "specialty finance companies," and offers a July 2008 memorandum from outside counsel which argues that the Four Funds need to register under the Investment Company Act ("ICA"). Smith Br. at 9; Statement of Additional Facts ¶ 14. Whether the Four Funds needed to be registered under the ICA, however, is irrelevant to the Section 5 claim. Smith's other argument appears to be that the SEC improperly counted as unaccredited some unnamed investors "whose notes were paid by another family member who would be accredited." Smith Stmt. Add'l Facts, ¶ 14. Smith, however, does not identify any such investors and, in any event, the SEC did not count an investor as unaccredited if there was another investor at the same address. App. Ex. 2 ¶ 8. Smith does not question the SEC's evidence showing that each of the Four Funds had more than 35 unaccredited investors. App. Ex. 2, ¶ 9. Summary judgment should be entered on the Sixth Claim for Relief.

II. NO ISSUES OF MATERIAL FACT EXIST AS TO DAVID SMITH'S OWNERSHIP AND CONTROL OF THE STOCK ACCOUNT

Lynn Smith fails to identify any evidence to support her farfetched argument that she alone controlled the Stock Account. She also cites no authority supporting her claimed right to a jury trial on this issue and fails to challenge the extensive case law cited in the SEC's opening brief establishing this Court's authority to decide this question. *See* SEC's Memorandum of Law in support of its motion for summary judgment at pp. 14-17. Given the paucity of evidence in her favor – apart from her own discredited testimony – the Stock Account should be used to augment the meager funds available to the victims of McGinn and Smith's fraud.

A. Lynn Smith's Claim that the Stock Account Has Always Been in Her Name is False

The bedrock of Lynn Smith's defense is that the Stock Account has always been in her name since 1969. *See, e.g.,* L. Smith Aff. dated May 21, 2010, Dkt. No. 23 at ¶¶ 13-18. The evidence shows, however, that this claim is false. Moreover, there is overwhelming, indisputable evidence that David Smith jointly owned and controlled the Stock Account since 1991.

Account opening statements show that the Stock Account was opened in Lynn Smith's name on November 21, 1991. SEC SMF ¶ 338; App. Exs. 263, 264. Lynn Smith has not presented any documentary evidence to the contrary. Rather, she submits several documents – none of which were produced in discovery – that do not establish that a brokerage account solely in Lynn Smith's name existed before 1991. *See* Ex. A (stock certificates in Lynn Smith's name dating, it appears, from 1970); Ex. B (1970 letters discussing certain stocks she had inherited); Ex. C (letter to Lynn Smith's father referencing a stock that he owned).

Lynn Smith also claims she signed the new account statement in 1991 because Bear Stearns required it. Lynn Smith Opp. Br. at 9-10. This claim is unsupported. The only document showing the origins of this account is the account opening documents from 1991, showing that David and Lynn Smith ***both*** signed the letter of authorization to "journal all cash and securities" into the newly created Stock Account. SEC SMF ¶ 339; App. Ex. 284.

Moreover, the Smiths' joint financial statements for 1984, 1986, 1987 and 1989 report no securities held by either Lynn or David Smith, other than possibly small IRA accounts of unidentified contents (SEC SMF ¶¶ 345; 347) and the only securities listed on the 1984 joint financial statement are specifically identified as "Mr. Smith's securities" (SEC SMF ¶ 345; App. Ex. 181 at 3). And their joint financial statements for 1990 and 1991 report that they held cash and securities totaling $298,000 in 1990 and $302,000 in 1991, with no indication that any were

owned solely by Lynn Smith. SEC SMF ¶¶ 348, 350.[3]

Lynn Smith argues that she did not create these financial statements and does not regard them as accurate. L. Smith Opp. Br. at 11. This self-serving position has no merit in face of the overwhelming documentary evidence to the contrary, is insufficient to create a genuine dispute.[4]

B. Indisputable and Overwhelming Evidence Shows that David Smith Controlled the Stock Account

Lynn Smith argues that David Smith merely acted as a typical broker. However, David Smith's control over the Stock Account far surpassed that of a broker with discretionary authority. David Smith personally benefitted from the Stock Account. Indeed, Lynn Smith has admitted that: "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." *See* L. Smith Response to SEC SMF ¶ 373 – admitted; *see also* Lynn Smith's Response admitting to SEC SMF ¶¶ 361-370; 373-374, regarding numerous joint expenses paid from Stock Account.

Lynn Smith also admits David Smith received at least $2,585,000 in his checking account from the Stock Account between November 1992 and August 1999 with no transfers back (SEC SMF ¶ 372- admitted), and does not rebut the fact that David Smith received at least $4.7 million

[3] Contrary to Lynn Smith's claim, Opp. Br. at 10, the SEC has provided the actual financial statements for each of the referenced years to support its claim (see App. Exs. 181-187, 189, 192, 194, 197, 200, 203, 206-210; SEC SMF ¶ 343) and it is Lynn Smith who fails to provide any documentary evidence to support her claim of an account solely in her name before 1991.

[4] The SEC does not contend, as Lynn Smith suggests, that the Smiths transferred the Stock Account back and forth between March and May 1992. L. Smith Opp. Br. at 11-12. Rather, we agree it was in her name during that period but David Smith obviously considered it a joint asset.

in his checking account from the Stock Account between August 1999 and April 2010 with only $390,000 transferred back (SEC SMF ¶ 371). She tries to diminish this evidence by arguing that whether David Smith benefitted is "irrelevant." L. Smith Op. Br. at 14-15. However, as Lynn Smith has conceded (L. Smith Opp. Br. at 7-8), whether a defendant benefitted from an asset is a relevant factor in determining whether he beneficially owned and controlled it. This rampant commingling of assets between the Stock Account, David Smith's checking account and his businesses, discussed below, is incontrovertible evidence of a joint asset.

David Smith also contributed assets to the Stock Account. Lynn Smith now admits – after years of denial – that David Smith contributed a portion of the money used to purchase the ALBANK stock, which ultimately was converted into the Charter One stock that became one of the Stock Accounts most valuable assets. L. Smith Opp. Br. at 15-16. She also does not dispute that David Smith contributed $610,000 from his QTIP Trust to the Stock Account. *See* SEC SMF ¶¶421-422. Although she argues that the money was supposed to be transferred to another QTIP Trust six months later as part of estate planning (L. Smith Opp. Br. at 17),[5] but was not because "[u]nfortunately, Lynn never received the opportunity to transfer the proceeds back into the QTIP Trust," the more plausible explanation is that she and David Smith intentionally left the funds in the Stock Account for their joint benefit. She also concedes that David Smith deposited $38,430 from his IRA into the Stock Account and that this money is subject to any judgment against David Smith. L. Smith Br. at 18.[6]

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[5] Significantly, App. Ex. 301 which she cites contains a warning from their estate planning attorney that "these transfers will be scrutinized to determine if they were fraudulently conveyed."

[6] If nothing else, by Lynn Smith's own logic, if the $38,430 deposited into the Stock Account is available for a judgment against David Smith, so too should the $610,095 he

Unlike a mere broker, David Smith also benefitted from the repeated and massive transfers of millions of dollars from the Stock Account to and from his various business ventures over the years. For example, brokerage and bank records show transfers of approximately $17.2 million from the Stock Account to McGinn Smith entities and transfers of approximately $13.7 million from McGinn Smith entities to the Stock Account between 1999 and 2010. SEC SMF ¶¶ 401 and 402.

Lynn Smith's claim that the Stock Account transactions were treated no different than for other customers, which required "a letter of authorization signed by the customer after they were fully aware of the opportunity presented to them," L. Smith Opp. Br. at 13, is rebutted by the ample evidence that she signed blank letters of authorization ("LOA's") in bulk, which McGinn Smith employees used whenever David Smith needed to move money back and forth between his business ventures. *See, e.g.*, L. Smith Response to SEC SMF ¶¶ 434-442 (does not dispute; claims lack of knowledge or information). The frequency and complexity of the transfers between the Stock Account and the McGinn Smith businesses undermine Lynn Smith's claim that she gave advance, knowing approval for each such transaction. Indeed, David Smith stated that his wife "really didn't focus much on the business end of things," SEC SMF ¶ 470, and that "she just didn't have a lot of interest in those things." SEC SMF ¶ 469. Accordingly, undisputed evidence compels the conclusion that David Smith jointly owned and controlled the Stock Account.

C. **Lynn Smith's Deceit Is Part of the Record of this Case**

Lynn Smith argues that this Court should not consider evidence that she was found to

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deposited from his QTIP Trust into the Stock account in 2009.

have deliberately concealed evidence, and was sanctioned for doing so. L. Smith Opp. Br. at 19-20, citing to SEC SMF ¶¶ 335, 383, 384. She argues that credibility issues are for the jury to decide and that the record before the Court contains "sworn testimony from Lynn Smith that creates an issue of fact." *Id.* at 20. However, Lynn Smith does not dispute that this Court has the equitable discretion to determine what assets are available to satisfy a judgment against David Smith, including whether he jointly owned and controlled the Stock Account. *See* SEC Br. at 14-17. Lynn Smith's documented misrepresentations and omissions to this Court are part of the record of this case. In evaluating whether a jury could find in her favor, the Court should be able to take into account the prior findings.

D. **The Palen Declaration Is Properly Offered as a Summary Exhibit**

Lynn Smith's argument that the Court should disregard the Declaration of Kerri Palen is without merit. Ms. Palen's Declaration is not being offered as expert testimony, but rather as a summary of voluminous bank and brokerage records and other financial documents. *See* Federal Rule of Evidence 1006 (permitting the use of "a summary, chart, or calculation to prove the content of voluminous writing"). Such evidence is admissible and should be considered.

In addition, Lynn Smith's complaints about the accuracy of the Palen Declaration are unfounded. She first contends that the Palen Declaration improperly "suggests" that a payment of $380,000 from David Smith to the Stock Account on December 20, 2007 was a contribution by him to the Stock Account rather than repayment of a previous "bridge loan" from the Stock Account to MS Funding in November 29, 2007. L. Smith Opp. Br. at 20-21. The Palen Declaration, however, clearly states that the transfer was "[f]unded using money from McGinn Smith Funding. According to Lynn Smith, this relates to repayment of bridge loan in the amount of $375,000 made 11/29/07 to McGinn Smith Funding LLC." App. Ex. 1 at 83 (Palen Ex. 25).

See also SEC's SMF ¶ 457 (stating that on December 20, 2007, $380,000 was "repaid by McGinn Smith Funding to the Stock Account via David Smith's checking account").

Lynn Smith also focuses on Palen Exhibit 24, which summarizes the known cash deposits and cash withdrawals into and out of the Stock Account from 1992 to 1999 and 1999 through 2010 as detailed in Palen Exhibit 25. Ms. Palen makes clear that for the period November 1991 through August 1999 "[b]rokerage statements were not available . . . therefore, I was only able to include transactions that I identified in LOA's, other account statement or accounting records." App. Ex. 1 at 25, 77. In addition, Palen also noted with respect to Exhibit 25, because of the absence of brokerage records prior to August 1999: "I am unable to verify that all transactions in the Stock Account prior to August 28, 1999 are included in Exhibit 25." Palen Decl. ¶ 78. Exhibit 24 does not contain any argument or make any conclusions, it merely summarizes known deposits and withdrawals from 1992 through 1999.

In addition, Lynn Smith's claim of an "unexplained discrepancy" between cash deposits and cash withdrawals between 1991 and 2010 also fails to recognize that Exhibit 24 does not purport to include cash flow from any stock transactions including, transfers into the Stock Account, proceeds of the sale of stock, income earned and gains recognized.

In an absurd argument, Lynn Smith ignores the fact that Exhibit 24 does not purport to list every transaction, and argues that because the known cash withdrawals are more than the known cash deposits, the Palen Declaration must be "a complete fabrication and falsehood." Lynn Smith Br. at 21. Notably, Lynn Smith does not dispute any particular deposit or withdrawal. Instead, through "elementary mathematics," she hopes to poke holes in a simple list of deposits and withdrawals. Unable to undermine anything in the Palen Declaration with actual evidence, however, Lynn Smith resorts to her usual fallback position of distortion and hyperbole.

Lynn Smith also incorrectly claims the Palen Declaration fails to acknowledge that "the majority of the disbursements from the Stock Account covered in the Palen Declaration were the purchases of the real estate in Vero Beach, Florida and Saratoga Springs, Florida, and also for tax purposes which were handled by David Smith, [and] the Palen Declaration lists 'not known' to the majority of them." L. Smith Opp. Br. at 21.

Exhibit 25, however, does list both the $100,000 transferred from the Stock Account on May 7, 2001, and the $300,000 transferred from the Stock account on June 19, 2001, to fund the down payment for the Vero Beach house, as received by David Smith, so these payments certainly were not among the unknown category. *See* SEC SMF ¶¶ 364-366. Exhibit 25 also reports a $70,000 transfer from the Stock Account to David Smith on June 19, 2003 and contains the clarifying note: "Funds were used to put a down payment on 2 Rolling Brook Dr. Saratoga Springs house purchase. The check was written out of David Smith's account." *See also* SEC SMF ¶ 370. Finally, Lynn Smith incorrectly argues that Palen Exhibit 25 fails to note that the $3,000,000 transfer from the Stock Account to IASG on January 14, 2003 was in exchange for a promissory note. In fact, Palen's note to that transaction states: "This represents Lynn Smith's cancellation of the 2-year note to be replaced by a promissory note from the company." [7]

[7] Her complaint that the transfer was actually $3,150,000, not $3,000,000, is unsupported, contradicted by the bank records Palen relied upon and immaterial. Also, only $5,500 out of $7,937,506 in disbursements from 11/21/92 to 8/27/990 and $302,050 out of $25,513,791 in disbursements from 8/28/99 to 4/5/10 were unidentified by Palen. If some of these were additional transfers from the Stock Account to David Smith, this just further supports the SEC's position that David Smith benefitted from the Stock Account.

III. DAVID SMITH BENEFICIALLY OWNED AND CONTROLLED THE SMITH TRUST ASSETS AND THEY SHOULD BE USED TO SATISFY THE REQUESTED JUDGMENT AGAINST HIM

The SEC has asked this Court to exercise its broad equitable powers to apply the assets in the Smith Trust to satisfy the requested judgment against David Smith because the evidence shows that he beneficially owned and controlled the assets in the Smith Trust. Alternatively, it seeks summary judgment on its claim that David and Lynn Smith fraudulently conveyed assets to and from the Smith Trust in violation of New York Debtors and Creditors Sections 276 and 278("NYDCL §§ 276 and 278"). The Smith Trust admits to most of the facts set forth in the SEC's SMF and the various arguments it asserts are without merit.

A. The Smith Trust's Claim that David and Lynn Smith's Actions Have No Relevance is Meritless

The Smith Trust does not challenge the extensive legal authority cited by the SEC in its opening brief, SEC Br. at 14-29, establishing this Court's broad equitable powers to apply the assets in the Smith Trust to satisfy a judgment against David Smith on the ground he beneficially owned and controlled those assets. Instead, it merely complains that the SEC is raising this theory for the first time. In fact, the SEC always has argued that the assets in the Smith Trust were beneficially owned and controlled by David Smith and that those assets should be disgorged. *See, e.g., SEC v. McGinn Smith*, 752 F. Supp. 2d 194, 217 (N.D.N.Y. July 7, 2010), Dkt. No. 86, App. Ex. 345 ("The SEC contends that the Trust is an appropriate relief defendant and that, in the alternative, even if it is not properly named as a relief defendant, David Smith was a beneficial owner of the trust over which he asserted dominion and control.").

The Smith Trust also argues that its assets cannot be "invaded" " because it is a spendthrift trust and a separate legal entity and that "the actions of their parents [David and Lynn Smith] are irrelevant as a matter of law." Smith Trust Opp. Br. at 2. However, it cites no

authority for these claims, which are directly contrary to the New York Debtor and Creditor Law ("NYDCL") § 276, which has no spendthrift trust exception: "Every conveyance made and every obligation incurred with actual intent, as distinguished from intent presumed in law, to hinder, delay or defraud either present or future creditors, is fraudulent as to both present and future creditors." *See also* SEC Trust Opp. Br. at 15-19. Pursuant to NYDCL § 278, a creditor may have such fraudulent conveyances set aside. Thus, NYDCL § 276 makes the Smiths' actions in creating and conveying assets to the Smith Trust directly relevant to whether that transfer can be set aside pursuant to NYDCL § 278.

B. **There are No Material Facts in Genuine Dispute**

The Smith Trust has admitted to most of the facts set forth in the SEC's SMF. Of the approximately 120 facts directly relevant to the SEC's motion as to the Smith Trust assets (SMF ¶¶ 35-46; 471-545; 586-618), the Smith Trust admits 108 of those facts, denies four facts, partially admits and partially denies 4 facts, and neither admits nor denied four facts. It also neither admits nor denies the evidence set forth in SMF ¶¶ 546-585 regarding the other fraudulent conveyances by David and Lynn Smith and others.[8]

C. There is No Genuine Dispute That Lynn Smith Hid the Annuity Agreement From the Court

The Smith Trust argues that there is a genuine dispute whether David and Lynn Smith hid the Annuity Agreement from the Court. However, the Smith Trust admits that prior to August 2010 Lynn Smith failed to inform the Court that the Smiths entered into the Annuity Agreement entitling them to annual payments of approximately $489,000 from the Smith Trust. Smith Trust Response to SEC SMF, Dkt. No. 778-3, at ¶ 494 ("Response"); (2) failed to produce

[8]The Smith Trust's failure to cite to record evidence in support of its denials means that fact is deemed admitted." *See, supra* at 3-6.

the Annuity Agreement in response to discovery requests (Response ¶ 502); (3) failed to disclose the Annuity Agreement or her and David Smith's rights to payments on a court-ordered Statement of Net Assets (Response ¶ 503); (4) failed to disclose the Annuity Agreement in her May 27, 2010 deposition despite being asked questions about her assets (Response ¶ 504); and (5) failed to disclose the Annuity Agreement during her testimony before the Court at the preliminary injunction hearing (Response ¶ 506). The Smith Trust also admits that Judge Homer found that Lynn Smith engaged in "fraud, misrepresentation, and misconduct' in concealing the Annuity Agreement (Response ¶ 37) and further found that Lynn Smith "acted with subjective bad faith" in concealing the Annuity Agreement (Response ¶ 38). *See* SEC SMF ¶¶ 37-40, 44.

The Smith Trust also does not set forth a single fact in its counterstatement that Lynn Smith's repeated concealment of the Annuity Agreement from April through July 2010 was anything but intentional or that her motive for concealing the Annuity Agreement was anything other than to defraud the Court. Thus, there is no genuine factual dispute that Lynn Smith hid the Annuity Agreement from the Court as part of her effort to shield those assets from investors.

D. There is No Genuine Dispute that the Smith Trust Benefitted David and Lynn Smith

The Smith Trust admits that David and Lynn Smith were entitled to receive $489,000 in annual annuity payments from the Smith Trust (Response ¶ 494) and that such payments would result in approximately $10 million in payments to them if they reached their expected life expectancy (Response ¶ 501). In addition, the Smith Trust's own expert, David Evans, has admitted that by entering into the Annuity Agreement with the Smith Trust, the Smiths obtained income and estate benefits, including: deferral and spreading out over many years of the capital gains tax they would otherwise have been subjected to immediately in 2004 when the Charter One stock was converted into cash as a result of a merger; the exclusion of the Charter One stock

from the Smiths' estate; and the avoidance of any gift tax because the stock was "sold" rather than gifted to the Smith Trust. *See* Evans Report dated September 2, 2010, at ¶¶ 28-30).

The only "facts" the Smith Trust cites are Lynn Smith's claim that the Smith Trust was created solely for the benefit of their children, and Geoffrey and Lauren Smith's testimony that they believed the Smith Trust was created for their benefit. *See* Opp. Br. at 4-5; Response ¶¶ 639-641. However, these assertions were refuted by the discovery of the Annuity Agreement. And Geoffrey and Lauren Smith's testimony as to why their parents created the Smith Trust does not suffice to create an issue of fact.[9]

The Smith Trust's reliance on Judge Homer's July 7, 2010 opinion at pp. 3 and 11, to support its claim that the Smith Trust was created for the benefit of the Smiths' children, is grossly misleading. *See* Smith Trust Opp. Br. at 4-5. Obviously, when Judge Homer considered the Annuity Agreement his understanding of the Trust changed, and he re-imposed the asset freeze and concluded that David Smith possessed "an equitable and beneficial interest in the Trust." SEC SMF ¶¶ 28-40. Given the indisputable evidence cited above, there can be no genuine dispute that David and Lynn Smith benefitted from the Smith Trust.[10]

[9] The Smith Trust admits that Lauren Smith never spoke to either David or Lynn Smith about any aspect of the Smith Trust and that Geoffrey Smith never spoke to his mother about the Smith Trust. Responses to SEC'S SMF ¶¶ 523; 527-28; 538.

[10] The Smith Trust also repeatedly and wrongly asserts that: "It has been conclusively established, and now conceded by the plaintiff, that the Trust is a validly created Trust …" See Opp. Br. at 1, 3, 12. The SEC has made no such concession and the Smith Trust provides no support for this claim. To the contrary, the SEC has consistently taken the position that the Smith Trust was created as part of a fraudulent scheme to defraud the Smiths' creditors.

E. There is No Genuine Dispute That David Smith Reported the Smith Trust Assets As His in Financial Documents

The Smith Trust argues that there is a genuine dispute whether David Smith reported the Smith Trust as his asset in financial documents, Smith Trust Opp. Br. at 3-11, but the Smith Trust has admitted that he did so. In fact, it admitted that David Smith listed the assets contained in the Smith Trust, totaling $4,453,022, as among the cash and securities owned by David and Lynn Smith, on his handwritten Financial Statement dated December 31, 2007. Response SMF ¶ 508; Opp. Br. at 10. Indeed, the document cited in support of this fact (App. Ex. 209) explicitly identifies the Smith Trust as one of David and Lynn Smiths' assets.

The Smith Trust has no explanation for this clear evidence, except to speculate that perhaps he listed the Smith Trust as an asset to obtain a loan from a third party. However, the Smith Trust has admitted that David Smith also described himself as the "beneficiary" of the Smith Trust when he prepared handwritten responses to a "Registration Notice and Questionnaire" for the Trustee to sign in connection with an proposed initial public offering of shares owned by the Smith Trust. *See* Response ¶ 509; App. Ex. 268, p. 5. He did so in response to a conflict of interest question whether "you or any of your affiliates or associates" have a material relationship with the underwriter. Moreover, even the most cursory comparison of David Smith's Financial Statements from July 2004 (App. Ex. 206), August 2005 (App. Ex. 207), October 2006 (App. Ex. 208), December 31, 2007 (App. Ex. 209), August 31, 2008 (App. Ex. 210), makes clear that the approximately $4.4 million in assets in the Smith Trust continued to be included as among the approximately $14 million in net assets consistently reported on the Smiths' Financial Statements both before and after they transferred the approximately $4.4 million in Charter One stock to the Smith Trust in 2004. *See also* SEC's SMF ¶¶ 507-508. Thus, it is indisputable that David Smith reported the Smith Trust assets as his own.

F. The Smith Trust Admits Virtually Every Relevant Fact in the SEC's SMF

The Smith Trust admits to the following material facts supporting the SEC's motion:

- In December 2003, David and Lynn Smith were named as defendants in a securities fraud suit based in part on loans made from the Stock Account to facilitate an allegedly fraudulent IPO; and the case was settled in 2004 for $200,000 (Response ¶¶ 471-475);

- In February 2004, the SEC sent David Smith a letter setting forth numerous violations by MS & Co. (Response ¶¶ 476-477);

- 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 (Response ¶ 478);

- At the time when the Charter One stock was transferred to the Smith Trust, the FIIN and FEIN fraudulent offerings, which raised $40 million from investors, were well underway (Response ¶ 485);

- The private placement memorandum for both offerings did not permit investments in affiliates of McGinn Smith but Smith from the beginning invested in affiliates; and as of December 31, 2003, 11% of investments were with affiliates and this grew to 32% by December 31, 2004 (Response ¶ 487);

- At the time of the transfer of the Charter One stock to the Smith Trust, the liabilities of FIIN and FEIN far exceeded their assets (Response ¶ 488);

- David Smith reported the Smith Trust assets as his own on financial documents (Response ¶ 508-509); see also App. Exs. 206-210);

- The Trustee, Thomas Urbelis, routinely signed documents as requested by David Smith and the documents often had instructions to sign immediately and overnight them back to Smith (Response ¶514-515);

- Urbelis took no responsibility for the Smith Trust's tax returns, relied upon David Smith for all investment decisions, never spoke to either of the ostensible beneficiaries of the Smith Trust regarding any aspect of the trust, made no distributions for the benefit of either of the ostensible beneficiaries of the trust, and, according to Lynn Smith's own testimony, the only thing he did was sign tax returns and" I don't think there is anything else he does." (Response SMF ¶¶ 513, 516, 519, 525, 530, 532);

- Neither David nor Lynn Smith ever informed their daughter Lauren that she was a beneficiary of the Smith Trust or had any conversation with her about the Trust (Response ¶ 527-528; 538);

- Despite the fact that Lauren Smith "went through a little bit of a rough period" including being unemployed, collecting unemployment insurance and requiring assistance in paying her rent, including receiving $22,1000 from her parents between March 2007 and May 2009 to pay her rent, Lauren Smith never requested a distribution from the Smith Trust and admitted that she did not know she could do so (Response ¶ 531, 539-541);

- David Smith paid taxes for the Smith Trust from his own money (Response ¶ 545);

- The only persons to receive a distribution from the Smith Trust, amounting to $95,000, were David and Lynn Smith (Response ¶ 543);

- Lynn Smith concealed of the Annuity Agreement despite an obligation to disclose all assets in April through June 2010 (Response ¶¶ 37-38; 502-504; 506).[11]

These admitted facts are more than sufficient for this Court to hold that David Smith beneficially owned and controlled the Smith Trust or, alternatively, that he and Lynn Smith fraudulently conveyed the Charter One stock to the Smith Trust to shield that asset from their present and future creditors.

Finally, the Smith Trust's reliance on *In re Vebeliunas*, 332 F.3d 85 (2d Cir. 2003) is misplaced. Most importantly, the Second Circuit in *Smith v. SEC* pointed out that in *Vebeliunas* "we assumed that New York courts would allow the veil of a trust to be pierced in situations where the complete domination of a trust has been shown" before affirming this Court's finding that the SEC would likely prove that David Smith was the equitable owner of the Smith Trust. *Smith v. SEC*, 432 Fed. Appx. 10 at 13 (2d Cir. 2011). In addition, in *Vebeliunas*, there was no evidence that the transfer of the property to the trust was part of a fraudulent conveyance or that

[11] David and Lynn Smith and the Smith Trust also either admit, or do not rebut, the ample evidence set forth in the SEC's SMF regarding the 2009 fraudulent conveyances of the Vero Beach house and the checking account (Response ¶¶ 558-571).

the trust was created to conceal assets. *Vebeliunas*, therefore, is clearly distinguishable.[12]

G. The Smith Trust Arguments Based on the Trustee's Powers are Without Merit

The Smith Trust advances several additional arguments based on state law as to why the terms of the trust and the annuity agreement allegedly prevent this Court from applying the Smith Trust assets to a judgment against David Smith. Smith Trust Opp. Br. at 4-6. However, as discussed above, given that David Smith beneficially owned the Smith Trust's assets, and given that the Smiths fraudulently conveyed assets to the Trust, , whatever contractual or statutory provisions that might otherwise bear on a Court's right to attach trust assets are irrelevant.

Accordingly, the SEC respectfully requests that the Court find that David Smith beneficially owned and controlled the Smith Trust and order that its assets be applied to satisfy the requested judgment against him; or alternatively, grant summary judgment on the SEC's claims that David and Lynn Smith fraudulently conveyed assets to and from the Smith Trust, in violation of NYDCL § 276, and order that those fraudulent conveyances be set aside and the assets made available to satisfy the requested judgment against David Smith.

[12] The Smith Trust also claims, without citation and incorrectly, that the SEC has "conceded" that the assets in the Smith Trust were "'clean' assets, not associated with any misdeeds of David L. Smith." More to the point, however, it is irrelevant whether the Smith Trust contains any proceeds of David Smith's fraud. Because David Smith beneficially owned and controlled the Smith Trust, its assets are available to satisfy a judgment against him regardless of their origin.

CONCLUSION

For the foregoing reasons, plaintiff respectfully requests that the Court grant its motion for summary judgment; and deny the motions for summary judgment filed by David Smith (including his cross-motion on damages), Lynn Smith and the Smith Trust.

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Respectfully submitted,

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