

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF NEW YORK

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SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

v.

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

McGINN, SMITH & CO., INC.,
McGINN, SMITH ADVISORS, LLC
McGINN, SMITH CAPITAL HOLDINGS CORP.,
FIRST ADVISORY INCOME NOTES, LLC,
FIRST EXCELSIOR INCOME NOTES, LLC,
FIRST INDEPENDENT INCOME NOTES, LLC,
THIRD ALBANY INCOME NOTES, LLC,
TIMOTHY M. McGINN, AND
DAVID L. SMITH, GEOFFREY R. SMITH,
Individually and as Trustee of the David L. and Lynn
A. Smith Irrevocable Trust UIA 8/04/04,
LAUREN T. SMITH, and NANCY McGINN,

Defendants,

LYNN A. SMITH and
NANCY McGINN,

Relief Defendants,

GEOFFREY R. SMITH, Trustee of the David L. and
Lynn A. Smith Irrevocable Trust UIA 8/04/04,

Intervenor

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**RESPONSE OF STAN AND EVA RABINOVICH TO MOTION OF WILLIAM J.
BROWN, AS RECEIVER, FOR AN ORDER (I) APPROVING PLAN OF
DISTRIBUTION OF ESTATE ASSETS
AND (II) AUTHORIZING INTERIM DISTRIBUTIONS**

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Stan and Eva Rabinovich (collectively, “Claimants”), by and through their attorney, respectfully submit this Response to the Motion of William J. Brown, as Receiver, for an Order (I) Approving Plan of Distribution of Estate Assets and (II) Authorizing Interim Distributions, filed December 31, 2015 (“Proposed Plan of Distribution”) (*see* Docket No. 847).

PRELIMINARY STATEMENT

By Order entered April 17, 2012, the deadline for creditors and investors to file a claim against the MS Entities was June 19, 2012 (*See* Docket No. 481). In accordance with that Order, Claimants timely filed proofs of claims (“Claims”) in this case. (*see* Glavin Affidavit, filed herewith, at ¶ 2). On or about May 1, 2012, the Receiver marked the Claims as “disputed” on the Receiver’s Website of the Claims Schedules. *See Id.* ¶ 3. In response, and at the request and direction of the Receiver, Claimants submitted additional documentation to support the claims. *See Id.* ¶ 4. To date, the Receiver has not indicated whether the Claims will still be “disputed” or provided Claimants with any basis or evidence for why they were marked as “disputed.” *See Id.* ¶ 5. Nor has the Receiver filed a formal objection to the Claims. *See Id.*

Yet, the Receiver’s Proposed Plan of Distribution seeks to “make an interim distribution of the assets of the MS entities at this time” while excluding “investors whose claims are disputed” from receiving any distribution until some future date. *See* Memorandum of Law In Support of Motion of William J. Brown, as Receiver, for an Order (I) Approving Plan of Distribution of Estate Assets and (II) Authorizing Interim Distributions, filed December 30, 2015 (*see* Docket No. 847) (hereinafter “Receiver’s Memorandum”) at pp. 2 and 13. The Proposed Plan of Distribution further provides that “[a] subsequent Motion will be filed with the Court notifying those investors whose claims are disputed.” *Id.* at p. 13. To date, no such motion has been filed nor has the Receiver indicated when he intends to file such motion.

If Claimants are excluded from an interim distribution prior to the Receiver providing

notice to Claimants and the Court of the basis, if any, to dispute the Claims, then the Proposed Plan of Distribution would deprive Claimants of due process. Claimants are aware of no legal basis for making an interim distribution to some investors, while other investors have to wait based on a hypothetical objection that has yet to be asserted, and may or may not be filed until some unidentified future date.

STANDARD OF REVIEW FOR A PLAN OF DISTRIBUTION

“[T]he fundamental principle governing adoption of a distribution plan is that it should be equitable and fair, with similarly-situated investors treated alike.” *See SEC v. Credit Bancorp, Ltd.*, 99 Civ. 11395 (RWS), 2000 U.S. Dist. LEXIS 17171, at *93 (S.D.N.Y. Nov. 29, 2000) (citing *SEC v. Elliott*, 953 F.2d 1560, 1569 (11th Cir. 1992); *United States v. Durham*, 86 F.3d 70, 73 (5th Cir. 1996); *United States v. Vanguard Inv. Co.*, 6 F.3d 222, 226-27 (4th Cir. 1993)). The Court has the authority to approve a plan so long as it is “fair and reasonable.” *See SEC v. Byers*, 637 F. Supp. 2d 166, 174 (S.D.N.Y. 2009) (quoting *SEC v. Wang*, 944 F.2d 80, 81 (2d Cir. 1991); citing *SEC v. Enter. Trust Co.*, No. 08 Civ. 1260, 2008 U.S. Dist. LEXIS 79731, at *10 (N.D. 111. Oct. 7, 2008)).

When a plan seeks to exclude certain members, “procedural due process should be respected.” *See SEC v. Credit Bancorp*, 2000 U.S. Dist. LEXIS 17171, at *149-50 (citing *Elliott*, 953 F.2d at 1566-67. When the SEC “comes to believe that a particular individual is not entitled to take part in the distribution,” the SEC should “notify the Court, the parties, and the individual(s) in question” and act “promptly in bringing such matters to the Court's attention.” *See SEC v. Credit Bancorp*, 2000 U.S. Dist. LEXIS 17171, at *150.

ARGUMENT

I. THE PLAN SHOULD NOT EXCLUDE CLAIMANTS FROM THE INTERIM DISTRIBUTION WITHOUT DUE PROCESS

The Receiver seeks to “make an interim distribution of the assets of the MS entities at this time” while excluding “investors whose claims are disputed.” *See* Receiver’s Memorandum at pp. 2 and 13. Before an investor can be excluded from receiving a distribution, however, such investor must be notified of the Receiver’s decision and the evidence supporting it. *See SEC v. Byers*, 637 F. Supp. 2d 166, 184 (S.D.N.Y. 2009) (“Any investor whom the Receiver intends to exclude from receiving a distribution shall be notified of the Receiver’s decision and the evidence supporting it. The investor will then have an opportunity to respond to the Receiver.”). Claimants are aware of no case law that permits a party to be excluded from a distribution without first formally notifying the Court and that party of the basis for any dispute.

In *SEC v. Credit Bancorp*, the receiver attempted to exclude certain investors from a partial distribution without providing due process, and the court recognized that the plan of distribution was defective for that reason and ordered a modification. In modifying the proposed plan of distribution in that case, the court stated:

The SEC has not proposed a specific procedure for determining whether certain individuals should be excluded from the partial distribution ... Certainly, procedural due process should be respected ... The form which such process should take need not be prejudged.

If the SEC comes to believe that a particular individual is not entitled to take part in the distribution based on his involvement in the Credit Bancorp fraud, then the SEC shall so notify the Court, the parties, and the individual(s) in question. The SEC shall also propose a procedure for resolving the issue. The Court will then determine the appropriate procedure and resolve the dispute. The SEC shall act promptly in bringing such matters to the Court’s attention. For example, if there are individuals whom the SEC has already identified as potential candidates for exclusion, it shall so notify the Court forthwith.

See SEC v. Credit Bancorp, 2000 U.S. Dist. LEXIS 17171, at *149-50.¹

Here, Claimants, although being marked as “disputed” on the Receiver’s website more than three years ago, have never been notified by the Receiver of any basis to dispute the Claims. Claimants in fact submitted supplemental paperwork to further support the validity of their claims. *See* Glavin Affidavit at. ¶ 4. To date, they have received no indication whether the Claims will still be disputed, why the Receiver believes the Claims to be disputed (if they are still being disputed), or when the Receiver intends to articulate the basis for any dispute. Thus, the Proposed Plan of Distribution is unfair to Claimants and violates due process as it seeks to make an interim distribution to some investors, while Claimants have to wait based on a hypothetical objection that has yet to be asserted.²

II. CLAIMANTS SHOULD RECEIVE THEIR DISTRIBUTION AT THE SAME TIME AS THE OTHER INVESTORS

The hallmark of any plan of distribution approved by the Court is that “it should be equitable and fair, with similarly-situated investors treated alike.” *See SEC v. Credit Bancorp*, 2000 U.S. Dist. LEXIS 17171, at *93 (citation omitted). Here, the Receiver has not supplied the Court or Claimants with any evidence showing that Claimants are any different from the other investors who will receive an interim distribution. The Receiver has also not made a motion to this Court or objected to the Claims submitted by Claimants. Thus, Claimants must be treated in the same manner as the rest of the investors and receive a distribution at the same time. If

¹For example, in *SEC v. Merrill Scott & Assocs.*, the proposed distribution plan expressly notified the court and listed the individuals that were being excluded and the reasons for such exclusion. *See SEC v. Merrill Scott & Assocs.*, No. 2:02 CV 39, 2007 U.S. Dist. LEXIS 690, at *5-6 (D. Utah Jan. 2, 2007).

² The Proposed Plan of Distribution is also overly vague regarding collateral recoveries. Specially, the Receiver’s Memorandum states that: “To the extent an investor receives one or more collateral recoveries, the Receiver will reduce payments to such an investor to the extent necessary.” *See* Receiver’s Memorandum at p. 11. There is, however, no notice as to how or to what extent distributions will be reduced.

Claimants do not receive a distribution at this time, then Claimants are not being “treated alike.”

III. CONCLUSION

For the foregoing reasons, Claimants respectfully request that the Court modify and/or clarify the Proposed Plan of Distribution to afford Claimants the requisite due process prior to allowing any interim distributions, and grant Claimants such other relief as the Court deems just and proper.

Dated: February 16, 2016

Respectfully submitted,

/s/ James Henry Glavin IV
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Attorney for Claimants

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Individually and as Trustee of the David L. and Lynn
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LAUREN T. SMITH, and NANCY McGINN,

Defendants,

LYNN A. SMITH and
NANCY McGINN,

Relief Defendants,

GEOFFREY R. SMITH, Trustee of the David L. and
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Intervenor

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State of New York)
)
County of Saratoga)

**AFFIDAVIT OF JAMES HENRY
GLAVIN IV IN SUPPORT OF THE
RESPONSE OF STAN AND EVA
RABINOVICH TO MOTION OF
WILLIAM J. BROWN, AS RECEIVER,
FOR AN ORDER (I) APPROVING PLAN
OF DISTRIBUTION OF ESTATE
ASSETS AND (II) AUTHORIZING
INTERIM DISTRIBUTIONS**

James Henry Glavin IV, being duly sworn, deposes and says:

1. I am a member of the bar of this Court and counsel for claimants, Stan and Eva Rabinovich (“Claimants”), in this action. I have read the foregoing affidavit and the contents thereof are true to the best of my knowledge, information, and belief.

2. On April 17, 2012, this Court ordered that the last day for Creditors and Investors to file a claim against the MS Entities was June 19, 2012 (*See* Docket No. 481). In accordance with that Order, Claimants timely filed Proofs of Claim (“Claims”) in this case.

3. On or about May 1, 2012, the Receiver marked the Claims as “disputed” on the Receiver’s Website of the Claims Schedules.

4. In response, and at the request and direction of the Receiver, Claimants submitted additional documentation to support the Claims.

5. To date, the Receiver has not indicated whether the Claims will still be “disputed” or provided Claimants with any basis or evidence for why the Claims were marked as “disputed” in the first instance. Nor has the Receiver filed a formal objection to the Claims.



James Henry Glavin IV

Sworn to before me
February 16, 2016


Notary Public

Marina Ivulgina Glavin
Notary Public, State of New York
No. 02GL6142734
Qualified in Richmond County
3/20, 2016

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LAUREN T. SMITH, and NANCY McGINN,

Defendants,

LYNN A. SMITH and
NANCY McGINN,

Relief Defendants,

GEOFFREY R. SMITH, Trustee of the David L. and
Lynn A. Smith Irrevocable Trust UIA 8/04/04,

Intervenor

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CERTIFICATE OF SERVICE

I hereby certify that a true copy of the RESPONSE OF STAN AND EVA
RABINOVICH TO MOTION OF WILLIAM J. BROWN, AS RECEIVER, FOR AN
ORDER (I) APPROVING PLAN OF DISTRIBUTION OF ESTATE ASSETS AND (II)
AUTHORIZING INTERIM DISTRIBUTIONS, and the Affidavit of James Henry Glavin

IV in support thereof, was electronically served upon the registered participants to this action as follows:

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I hereby also certify that paper copies of the aforementioned were served via first class mail upon the following:

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Dated: February 16, 2016

s James Henry Glavin IV
James Henry Glavin IV