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October 22, 2010

Hon. David R. Homer
United States Magistrate Judge
United States District Court
445 Broadway
Albany, NY 12207

Re: **SEC v. McGinn, Smith & Co., et al.**
10-CV-457 (GLS/DRH)

Dear Judge Homer:

Please accept this letter in response to the letter filed with the Court on Friday by attorney David Stoelting on behalf of the Securities and Exchange Commission.

In his letter filed (Document 158), Mr. Stoelting purports to "correct the record" by alerting the Court that his colleague, Kevin McGrath, made an assertion in a legal brief which was untrue at the time it was made. Mr. Stoelting provided no reason for the inaccuracy of Mr. McGrath's earlier assertion, but it is my understanding that his letter was filed at the insistence of David Smith's attorney. Apparently to deflect the impact of his colleague's misleading assertion, Mr. Stoelting purports also to "correct the record" with respect to two passages in a legal brief which I recently filed on behalf of the Trust defendants.

Mr. Stoelting's accusation in this regard is devoid of merit. First, there was nothing incorrect in the quoted passages, which were in fact legal arguments, not "representations." Second, his abbreviation and inaccurate paraphrasing of the second passage is a blatant attempt to alter the meaning and to render the passage inaccurate. That portion of his letter stretches the bounds of zealous advocacy.

In Point I of the Trust's Surreply Memorandum at page 7, the Trust, in arguing against the consideration of evidence obtained by the SEC from the U.S. Attorney's office, compared this case to the facts and outcome in *SEC v. Rajaratnam*, Docket No. 10-CV-462 (2d Cir., Sept. 29, 2010). In that case, which involved evidence obtained with a wiretap warrant, Rajaratnam was defending an SEC civil enforcement action while under indictment in a securities fraud criminal prosecution. Both cases were in their respective discovery phases, and the SEC demanded that the defendant disclose to it evidence which his counsel had obtained during discovery in the criminal case. The defense had not yet obtained rulings in the criminal case regarding the legality of the search and the relevance of the information seized and

therefore objected to the district court's order directing him to disclose the evidence to the SEC. In that case, the Second Circuit ruled it an abuse of discretion for a district court to allow disclosure to the SEC in a civil enforcement action of evidence obtained pursuant to a warrant in a parallel criminal investigation.

In the case at bar, the SEC has argued that this Court should consider, as evidence in a motion to reconsider its July 7 decision unfreezing the Trust, a letter seized from David Smith's home pursuant to a warrant. In response, the Trust defendants requested that the Court direct Mr. Stoelting and his colleagues to identify the date or dates on which they learned of the existence of the letter and the date on which the letter came into their possession. Although the SEC asserted in a footnote of its brief that it was not claiming that the letter was "newly discovered" evidence, it did not rescind the argument that the letter should be considered by the Court on this motion. Thus, when and how the SEC obtained the letter is relevant to this motion.

To the best of my knowledge, there has been no grand jury action and no criminal charges have been filed in the ongoing parallel investigation being conducted by the U.S. Attorney's office here. No defendants have been named, let alone been able to avail themselves of any procedural mechanism to obtain access to the evidence in the possession of the U.S. Attorney. I learned this week that property belonging to Geoffrey and Lauren Smith was also seized by the FBI, and I am in the process of identifying the property and seeking its return. There does not appear to be a pending criminal action in which anyone could challenge the search or the relevance of the evidence obtained by the search warrant, and any such challenge may not have been ripe, but for the SEC having publicly disclosed the seized evidence in this civil case. The parties here should be afforded at least the same, if not greater protection than the defendant in the *Rajaratnam* case, and it matters not whether the SEC has provided copies to the defendants of any or all of the documents which it obtained from the U.S. Attorney, since the Court, and not the SEC, is the appropriate filter by which to adjudicate the propriety of disclosure of documents seized with a search warrant.

Therefore, contrary to Mr. Stoelting's assertion, the Trust correctly argued:

> "***Consequently***, no defendant has been afforded access to the documents obtained by the U.S. Attorney, nor have they been afforded the protections of the constitution or the opportunity to challenge the search warrant or its execution or the relevance of the evidence obtained thereby." (emphasis added)

Mr. Stoelting deliberately omitted the transitional word "Consequently," which was selected by the Trust's counsel in an effort to lead the Court to the conclusion sought, which is the very purpose of a legal argument. The quoted passage was a legal argument, not, as Mr. Stoelting asserts, a "representation" which is "not correct" and it is the Trust's position that this legal argument is, in fact, correct.

With respect to the second passage which Mr. Stoelting asserts is "not correct", he quoted an abbreviated portion of a sentence from the Trust's brief, and then substituted his own words after the quotation mark in a deliberate attempt to alter the context and modify the meaning of the Trust's argument. Mr. Stoelting asserts that the Trust has argued that it has not received copies of the seized documents which the SEC obtained from the U.S. Attorney's office. That misstates the Trust's argument, which is that the U.S. Attorney's office has denied access to the defendants while granting access to the SEC.

Mr. Stoelting correctly states that on June 1 and June 3, 2010, the SEC provided me with copies of documents which the SEC says it obtained from the U.S. Attorney's office. That information did not in any way contradict the passage from the Trust's brief until Mr. Stoelting modified the language from the Trust's brief. The Trust has never asserted that the SEC failed to disclose documents to the Trust or to other defendants; rather, the Trust argues that, while the SEC has had seemingly unfettered access to seized evidence held by the U.S. Attorney's office, the defendants have not had that same access.

The Trust and other defendants should not be limited to the documents which the SEC obtained from the U.S. Attorney's office; rather, the defendants should be entitled to direct access and should not have to ask the SEC to obtain documents from the U.S. Attorney, which has been offered by the SEC but obviously would provide the SEC with a glimpse into the defense strategy. Without having direct access to the original evidence in the possession of the U.S. Attorney's office, there is also no way of testing whether the documents produced by the SEC are complete and were produced within the context in which they were maintained, or to determine the chain of custody or the authenticity of the evidence. Thus, the value to the defendants is substantially diminished when the defendants can only obtain documents through the SEC, itself a secondary source.

Thus, whether or not *the SEC* provided to the defense copies of documents which it obtained from the U.S. Attorney is irrelevant. The SEC is merely a party to a civil lawsuit and should not have been given access to seized evidence in a manner that subordinates the constitutional rights of other litigants, including the owners of the evidence. To the best of my knowledge, the search warrant application and warrant return have never been unsealed by this Court, yet the U.S. Attorney's office has provided untold amounts of "evidence" seized pursuant to that warrant to the SEC, who has then published that evidence by using it in a public hearing, referring to it and including it in documents publicly filed and has even asserted in the Amended Complaint the fact that evidence utilized to support the complaint was obtained with a search warrant.

For example, in filing the pending motion for reconsideration, the SEC asked the Court to consider, among other items, Exhibit 14 to David Stoelting's declaration, which was an undated, handwritten letter, the contents of which were also cited in the Amended Complaint. The undisputed source of Exhibit 14 – a search warrant in a criminal investigation in which no charges have been filed -- is what led to the inclusion of the second passage from the Trust's brief which Mr. Stoelting has

mischaracterized. Given that the search warrant application, warrant and return are apparently still under seal and have not been provided to the subjects of the investigation, it is unclear what authority there was for the release of this and other documents by the U.S. Attorney to the SEC, or the subsequent public disclosure of the evidence by the SEC. The quoted passage from the Trust's brief argues, and I believe it correctly argues, that it is fundamentally unfair for the U.S. Attorney's office to have granted the SEC access to seized evidence, allowing it to be published widely outside a pending criminal investigation, all while denying access to that evidence to its owners and before any Court has adjudicated the legality of the search and the relevance of the evidence seized. It is equally unfair, and possibly a violation of the rights of certain individuals, for the SEC to have used and published seized evidence in pursuit of this civil action, "all while the defendants have been denied access to the same evidence and their due process rights." That is the passage with which Mr. Stoelting takes issue, and that is the context in which the passage was written.

The comparison between this case and the *Rajaratnam* case should lead the Court to the conclusion that the defendants in this civil enforcement action have greater rights and protections than Mr. Rajaratnam, who was already a defendant in parallel criminal and civil proceedings. Despite the fact that evidence obtained with a wiretap warrant receives heightened protection, it remains fundamentally unfair for the SEC to be utilizing evidence seized with a warrant, when the warrant application has not been unsealed and the constitutional protections normally afforded to individuals in a federal criminal case have neither been adjudicated by this Court, nor are they likely to be ripe for adjudication prior to the disposition of this motion.

The passages from the Trust's brief which are quoted in Mr. Stoelting's letter are correct; he has merely taken them out of context and applied them to an argument which was not made. The Trust's argument was and is quite straightforward: Search warrants are not available to the SEC to pursue civil enforcement actions or state law claims, and the SEC should not be allowed to trample on the constitutional rights of litigants by utilizing the fruits of a search warrant issued by this Court in a criminal investigation before the Court has unsealed the warrant, or had the opportunity to review the legality of the search it authorized and the relevance of the evidence obtained thereby.

Very truly yours,

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JAD/jc