

The Novecks' investment in the NASMMF, which offered a fixed rate of return, was available at the Novecks' bank.

7. Between September 1998 and April 1999, the Novecks invested virtually their entire life savings, \$300,000, with Goren, believing that they had purchased shares of the NASMMF. For each purchase, the Novecks received a confirmation. At all times, the shares of the Fund maintained a price per share of \$1.00. The Novecks' investments were made as follows, on or about the following dates:

8. September 4, 1998. The Novecks invested \$120,000 to purchase 120,000 shares of the NASMMF.

9. December 8, 1998. The Novecks invested \$80,000 to purchase 80,000 shares of the NASMMF.

10. January 25, 1999. The Novecks invested \$67,696.07 to purchase 67,696.07 shares of the NASMMF.

11. February 4, 1999. The Novecks invested \$32,363.93 to purchase 32,303.93 shares of the NASMMF.²

12. As indicated on the Novecks' New Times Securities Corporation statements, relevant copies of which were supplied in support of their Claim and which are annexed as Exhibit C hereto, dividends on shares of NASMMF were automatically invested in additional shares of NASMMF. As reflected in the last brokerage statement received by the Novecks, as of December 31, 1999, the Novecks owned 321,010.08 shares of NASMMF, including 21,010.08 shares purchased through dividend reinvestment.

² On April 7, 1999, Goren "transferred" \$26,379.30 to a NTSSI account held by the Novecks to pay for the purchase of certain stocks. On or about April 15, 1999, Goren "transferred" \$26,379.93 back to the Novecks' New Age Securities Corporation account. The Novecks also paid taxes for the purported dividends received in 1998 on their investments.

By Notice Dated March 2, 2001 (the "Notice"), the Trustee communicated his finding that the Novecks had deposited \$300,000.00 with the Debtor for the purchase of shares of NASMMF and that the Claim, to the extent of such deposit, was a "valid customer claim." See Exhibit B hereto. Based upon such finding and determination, the Trustee allowed the Claim "as a claim for cash in the amount of \$300,000.00." The Notice also communicated the Trustee's disallowance of the balance of the claim (\$21,010.08), representing the value of shares acquired by the Novecks through dividend reinvestment. Notwithstanding the allowance of the Claim to the extent of \$300,000.00, the Novecks were advised pursuant to the Notice that the Trustee will pay the claim only to the extent of \$100,000. As explained in the Notice, the difference between the portion of the Claim allowed and the amount undertaken to be paid by the Trustee is based upon the application by the Trustee to the Claim of the payment limitation found in 15 U.S.C. § 78fff-3(a)(1). Such section, which applies only to a claim "for cash," limits the payment obligation of the Trustee to \$100,000.

OBJECTIONS

14. The Novecks object to the Notice to the extent that it characterizes the Claim as one "for cash" rather than "for securities" and, based upon such characterization, applies the \$100,000 statutory limit to the Trustee's payment obligation in respect of the Claim. Upon characterization of the Novecks' claim as one "for securities," the \$500,000 statutory limit would be applicable and the Trustee would therefore be obligated to satisfy the full amount of the Novecks' claim. 15 U.S.C. § 78fff-3(a). The Novecks also object to the disallowance of that portion of their claim having a value of \$21,010.08, representing shares of NASMMF purchased by them through dividend reinvestment.

... 15 U.S.C. § 78fff-2(b). The net equity of the debtor is determined as the dollar amount of the account or accounts of a customer, to be determined by calculating the sum which would have been owed by the debtor to such customer if the debtor had liquidated by sale or purchase on the filing date, all securities positions of such customer. *Id.* At established by the Novecks' account statements, the Novecks' net equity as of the February 17, 2000 filing date was \$321,010.08 based upon ownership of 321,010.08 shares of NASMMF having a value of \$1.00 per share. See Exhibit C hereto.

16. After receipt of a statement of claim, SIPA requires that a trustee promptly discharge "all obligations of the debtor to a customer relating to, or net equity claims based upon, securities or cash, by delivery of securities or the making of payments to or for the account of such customer." 15 U.S.C. § 78fff-2(b).

17. SIPA defines "security" broadly. 15 U.S.C. § 7811(14). It is not disputed by the Trustee or SIPC that the statutory definition of a security covers shares of a money market fund.⁴

³ The Trustee has determined that the Novecks were customers of the Debtor for the purposes of SIPA and accordingly, such status is not at issue. "Customer" is statutorily defined as "any person (including any person with whom the debtor deals as principal or agent) who has a claim on account of securities received, acquired, or held by the debtor in the ordinary course of its business as a broker or dealer from or for the securities accounts of such person for safekeeping, with a view to sale, to cover consummated sales, pursuant to purchases, as collateral security, or for purposes of effecting transfer. The term customer includes any person who has a claim against the debtor arising out of sales or conversions of such securities, and any person who has deposited cash with the debtor for the purpose of purchasing securities..." 15 U.S.C. § 7811(2).

⁴ Shares of money market funds have been acknowledged by SIPC to be securities within the protection of the statute. As stated by SIPC:

Shares of money market funds, although often thought of by investors as cash, are in fact securities when such funds are organized as mutual funds. When held by a SIPC member in a customer's securities account, such fund shares are as protected as any other covered security.

Publication of SIPC, "How SIPC Protects You," at page 7.

characterized all claims based upon purchases of shares of NASMMF, including the Noveck's Claim, as cash claims based upon the fictitious nature of NASMMF. In contrast to its classification of NASMMF claims as "cash claims," net equity claims which have been asserted by customers of the Debtor based upon account statements showing holdings of mutual funds having names conforming to, similar to or close to actual funds, are being treated by the Trustee as claims for securities.⁵ Thus, in classifying claims as either "for cash" or "for securities" the Trustee is making a critical distinction between sham transactions involving sham securities — *i.e.*, the "fictional" NASMMF, shares of which never existed (but which are fungible with hundreds of other money markets) — and sham transactions involving the purported purchases of mutual funds denominated on account statements with names of actual funds or mutual funds with names similar or close to mutual funds which may be quoted in the newspaper, in which neither investors nor the Debtor ever acquired an interest. The Novecks, like the other victims of Goren, do not dispute the Trustee's conclusion that the NASMMF was never actually organized as a money market fund. However, at the same time, the Trustee does not dispute that the Novecks were entirely innocent of any culpability in connection with their purchase of shares of the NASMMF and concedes that the Novecks had no knowledge or suspicion of the non-existence of the NASMMF, which was confirmed to the Novecks and shown on their statements as a legitimate money market fund.

19. Although the Trustee has identified the fictitious nature of the NASMMF as determinative of the classification of the Novecks's claim as one "for cash" for the purposes of application of 15 U.S.C. §78fff-3 (a)(1), it has not specified any authority for reliance on this factor.

⁵ As a consequence of the characterization of the claims of mutual fund investors as claims for securities, the Trustee has undertaken to pay such claims to the extent of the \$500,000 statutory maximum. In addition, whereas the Trustee has disallowed that portion of the claims of NASMMF investors representing shares of NASMMF purchased through dividend reinvestment, the Trustee has allowed that portion of the mutual fund investors' claims that represent shares of such mutual funds purchased by them through dividend reinvestment.

20. All rights reserved. The Trustee's reliance on the Trustee's characterization of the Claim is contradicted by the rules adopted by SIPC for determining whether a customer claim is for cash or for securities. 17 C.F.R. §§ 300.500-300.503 (Series 500 Rules).

20. Rule 501 - "Claim for Cash" provides in applicable part that:

Where the Debtor held cash in an account for a customer, the customer has a "claim for cash," notwithstanding the fact that the customer has ordered securities purchased for the account, *unless: (1) the Debtor has sent written confirmation to the customer that the securities in question have been purchased or sold to the customer's account.*

17 C.F.R. § 300.501(b)(1) (emphasis supplied).

21. Rule 502 - "Claim for Securities," is the corollary of Rule 501 and provides that "Where the Debtor held cash in an account for a customer, the customer has a 'claim for securities' with respect to any authorized securities purchase: (i) if the Debtor has sent a written confirmation to the customer that the securities in question have been purchased for or sold to the customer's account[.]" 17 C.F.R. § 300.502.

22. Accordingly, the Series 500 Rules direct that where a customer has authorized a purchase of securities, it is the sending of a confirmation of that purchase or sale, rather than the execution of a trade, that determines whether the customer's net equity claim is for cash or securities. Here, the Notice includes the Trustee's determination that the Novecks authorized purchases of the NASMMF for their account. Moreover, it is not disputed that the Novecks received written confirmation of their initial purchase of shares, and, in the form of monthly or regular account statements, received confirmation of subsequent purchases by means of dividend reinvestment. In characterizing the Claim as one for cash, the Trustee disregards the apparent purpose and effect of the Series 500 Rules, *i.e.*, to bind the investor to and to allow the investor's reliance upon, written confirmation of his securities transactions. By apparently relying on the distinction between a fictitious money market fund and the fictitious purchase of shares of a money market fund (a distinction without substance) as the basis for the cash/securities determination, the

...the number of the shares which is beyond the control and verification of the investor by its objective, mechanical criteria provided by the Series 500 Rules.

23. The Trustee's misapplication of the Series 500 Rules is demonstrated within this proceeding by the disparate impact on the claims of similarly-positioned customers of the Debtor. In contrast to the NASMMF claimants, the Trustee apparently has determined that customers of the Debtor who entrusted funds to the Debtor for the purchase of shares of mutual funds with names (as denominated on customers' statements) similar or close to mutual funds which may be quoted in the newspaper, but whose transactions were never effected, will have their claims treated as claims for securities even though they never had any actual interest in the securities shown on their account statements. As a result, the Trustee is apparently allowing as valid customer claims "for securities" claims of customers who purchased shares of other non-existent mutual funds, while at the same time denying as valid customer claims "for securities" claims such as that of the Novecks for the purchase of shares of the NASMMF. There is nothing in the Series 500 Rules that suggests this result.

24. Moreover, the radically disparate and inequitable treatment of the NASMMF investors, on the one hand, and the mutual fund investors, on the other, results in undue and unseemly consequence given to the capricious and criminally motivated conduct of Goren rather than to any criterion reflected in the Series 500 Rules or pertaining either to customer conduct, losses or expectations. This disparate treatment is not, however, either required or contemplated by SIPA. Such disparate treatment flies in the face of the expressed Congressional intent for SIPA to satisfy customers' legitimate expectations. See S. Rep. No. 763, 95th Cong. 2d Sess. 2 (1978), reprinted in [1978] U.S. Code Cong. & Admin. News 764, 765. It is, in fact, absurd to suggest that Congress, in passing SIPA, intended for the scope of protection afforded to the investing public

and solicitation of certain new investors by the broker.

25. Like the mutual fund investors, the NASMMF investors, including the Novecks, provided funds for the purchase of securities. As with respect to the funds provided by the mutual fund investors, no securities were ever actually purchased. Like the mutual fund investors, the NASMMF investors, including the Novecks, received confirmations of their purchases and monthly statements showing their security positions. Like the mutual fund investors, the NASMMF investors, including the Novecks, had no basis to question the representations made to them that securities had been purchased for their account and were being held for them by the Debtor. Indeed, the "legitimate expectations" of the NASMMF investors, including the Novecks, are indistinguishable in every respect from those of the mutual funds investors.

26. The equities in favor of treating the NASMMF investors no less favorably than the mutual fund investors are compelling. Like other NASMMF investors, the Novecks chose to purchase money market shares believing that such investment was the most conservative available. It is respectfully submitted that to allow a small group of victims to bear crushing financial loss, while others with indistinguishable claims and expectations receive full statutory protection, is unconscionable. The inequitably disparate treatment reflected by the Trustee's determination of their claims is not mandated by SIPA or the rules promulgated thereunder.

⁶ The inequity of the Trustee's approach to characterizing claims is highlighted by the Trustee's apparent willingness to overlook discrepancies in the names of mutual funds (some of which actually existed and others with fictitious names), or pricing information with regard to purchases of certain mutual funds, appearing on account statements of certain investors and to nonetheless recognize such claims as securities claims. As arbitrary and unfair as it would be to deny a claim merely because Goren was less than meticulous in accurately identifying the mutual fund that he fraudulently represented had been purchased by an investor, it is equally arbitrary and unfair to penalize the NASMMF investors for having been duped into purchasing sham securities.

to the relief requested and that the Court direct the Trustee to allow the full amount of the claim (\$321,010.08) and to satisfy the entire amount of such claim as a claim for securities.

Dated: Uniondale, New York
March 26, 2001

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