

UNITED STATES OF AMERICA
BEFORE THE
COMMODITY FUTURES TRADING COMMISSION

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In the Matter of

:
: CFTC Docket No. 04-29
: OFFICE OF PROCEEDINGS
: RECORDS CLERK

G. Victor Johnson and Altschuler,
Melvojn & Glasser, LLP,

: ORDER MAKING FINDINGS AND
: IMPOSING REMEDIAL SANCTIONS
: AGAINST RESPONDENTS G. VICTOR
: JOHNSON AND ALTSCHULER
: MELVOIN & GLASSER, LLP

Respondents. :

I.

On September 30, 2004, the Commodity Futures Trading Commission (the "Commission") issued a Complaint and Notice of Hearing against G. Victor Johnson ("Johnson") and Altschuler, Melvojn & Glasser, LLP ("AMG") (collectively the "Respondents"). The Complaint charges, *inter alia*, that Johnson violated Commission Regulation 1.16(d)(1), 17 C.F.R. § 1.16(d)(1)(2004), and engaged in improper unprofessional conduct pursuant to Commission Regulation 14.8(c), 17 C.F.R. § 14.8(c)(2004), and that AMG is liable for Johnson's violations and improper unprofessional conduct pursuant to Section 2(a)(1)(B) of the Commodity Exchange Act, as amended (the "Act"), 7 U.S.C. § 2(a)(1)(B)(2002). To resolve this matter, the Respondents have each submitted Offers of Settlement ("Offers") that the Commission has determined to accept.

II.

Without admitting or denying the findings of fact in this Order, Johnson and AMG acknowledge service of the Order, consent to the use of the findings in the Order in this proceeding and any other proceeding brought by the Commission or to which the Commission is a party.¹

III.

A. Summary

Melrose Asset Management, Inc. ("Melrose") was a registered commodity pool operator ("CPO") and John Martin Lofgren ("Lofgren") was its chief executive officer.

¹ Johnson and AMG do not consent to the use of the Offers or this Order, or the findings to which they have consented in the Offers, as the sole basis for any other proceeding brought by the Commission other than a proceeding to enforce the terms of this Order. They do not consent to the use of the Offers or this Order, or the findings to which they have consented in the Offers, by any other person or entity in this or any other proceeding.

Melrose operated a commodity pool entitled The Melrose Fund, L.L.C. (“the pool”). AMG is a public accounting firm and performed annual audits of the pool’s financial statements (“the financial statements”) for the years ending December 31, 2000 and December 31, 2001. Johnson was the engagement partner for the audits.

AMG issued unqualified reports for both years that the financial statements were free from material misstatement, and Johnson signed the auditor’s reports on behalf of AMG. In fact, Lofgren had misappropriated pool funds on various occasions between January 2001 and February 2002 and the financial statements were materially misstated.

Johnson failed to conduct the audits of the financial statements in accordance with generally accepted auditing standards (“GAAS”). Specifically, he reviewed and tested certain of Lofgren’s misappropriations and failed to obtain sufficient competent evidence of the transactions before issuing the auditor’s report. In addition, Johnson failed to exercise due professional care and professional skepticism in conducting the audits.

Johnson’s failure to conduct the audits in accordance with GAAS violated Commission Regulation 1.16(d)(1) and constituted improper unprofessional conduct under Commission Regulation 14.8(c).

B. Respondents

G. Victor Johnson is a certified public accountant licensed in Illinois. Johnson is a Managing Director with the Financial Services Team of American Express Tax and Business Services (“AET”). AET is a wholly owned subsidiary of American Express Inc. AMG leased Johnson’s services from AET to conduct the audits.

Altschuler, Melvoin & Glasser, LLP, is a public accounting firm and an Illinois limited liability partnership located at One South Wacker Drive, Suite 800, Chicago, Illinois 60606-7494.

C. Facts

1. Lofgren’s Misappropriations

On January 18, 2001, Lofgren misappropriated \$500,000 from the pool. On February 21, 2001, he misappropriated another \$300,000. On February 22, 2002, he misappropriated another \$750,000. In each instance, Lofgren wired the funds from a pool account at Sentinel Management Group, Inc. (“Sentinel”) to an account at Burling Bank in the name of Melrose Asset Management, Inc. (“the Burling Bank account”).

2. AMG’s Audits

AMG was initially engaged by Melrose to audit the pool’s financial statements for the period ending December 31, 1999 (“the 1999 audit”). AMG’s audits for commodity pools include a Risk Identification and Planning Form. In completing the form for the 1999 audit, Johnson noted that the pool’s major asset was equity in commodity futures

trading accounts and that there was a significant risk of misappropriation. Johnson also noted that Melrose lacked internal controls.

The 2000 Audit

Johnson's Discovery that Melrose was Not Providing Account Statements

In December 2000, AMG was engaged to audit the pool's financial statements for the period ending December 31, 2000 ("the 2000 audit"). In September or October 2000, an outside accountant, who prepared Melrose's account statements for pool participants, informed Johnson that Melrose had not provided required account statements to pool participants since July 2000.² The accountant informed Johnson that he had refused to release the account statements to Lofgren until he resolved a dispute with Lofgren involving certain trades by Lofgren. The dispute was resolved, as documented in Melrose's letter to the accountant dated February 9, 2001, when Lofgren agreed to repay \$350,000 to the pool.

Johnson was aware that the failure to distribute account statements was a violation of the Commission's regulations and an illegal act. Despite this knowledge, he did not attempt to understand the dispute between Lofgren and the pool's outside accountant or the transactions underlying the dispute. In March 2001, AMG's lead auditor on the engagement, at Johnson's direction, met with Melrose regarding the failure to distribute account statements. The auditor advised Melrose that it needed to notify the Commission it had not been distributing account statements. This was Johnson's only response to the discovery that Melrose had failed to send participants required account statements for a period of nearly nine months. Ultimately, Melrose did not notify the Commission, and Johnson made no attempt to verify that the Commission had been notified.

Johnson's failure to adequately inform himself of the nature of the dispute and the underlying transactions that resulted in Melrose's failure to distribute required account statements to pool participants demonstrated a reckless lack of due professional care and professional skepticism.

Johnson's Review of Subsequent Events

The financial statements for the December 31, 2000, audit contain a note on subsequent events that states, "During January and February 2001, two members made partial withdrawals of \$800,000 from the Fund." In fact, the "partial withdrawals" were the misappropriations on January 18, 2001 and February 21, 2001, described above.

In March 2001, Johnson reviewed the work of AMG's lead auditor. AMG's lead auditor reviewed statements for the pool account at Sentinel that reflected the January misappropriation. The auditor saw the \$500,000 transfer to Burling Bank on January 18, 2001, and asked Melrose the purpose of the transfer. Melrose responded that it was a withdrawal by a participant. In an effort to obtain sufficient competent evidence of the

² In fact, Lofgren had been giving the pool participants false statements that hid his misappropriations.

transaction, the auditor requested a copy of the withdrawal request. Melrose sent a copy of a letter, purportedly from the participant, notifying Lofgren that the participant wanted to withdraw the funds. In fact, the letter was a fabrication. Lofgren had a previous withdrawal request from the participant and altered its date and the amount requested so that it would appear as if the participant had requested the \$500,000 withdrawal in January 2001.

Although the purpose of the fabricated letter was to disguise his misappropriation, Lofgren made an incriminating error that revealed the letter to be a fabrication. The participant's original letter instructed that funds be sent to Bank One. Lofgren failed to alter this instruction and left it in the fabricated letter. By leaving in the letter the instruction for the funds to be sent to Bank One rather than Burling Bank (which is where the misappropriated \$500,000 was transferred), Lofgren provided incriminating evidence that the participant had not actually requested the withdrawal. Thus, the fabricated letter did not provide competent evidence of the transaction and, in fact, provided contradictory evidence, which required additional investigation.

Johnson and the AMG staff accepted the fabricated letter as sufficient competent evidence of the transaction and failed to either obtain copies of the wire transfer documents for the transaction or contact the participant to confirm the withdrawal. If Johnson and AMG had obtained either the wire transfer documents or contacted the participant to confirm the withdrawal, they would have learned that the withdrawal did not occur as represented. Specifically, the wire transfer documents for the transaction showed that the funds went to an account at Burling Bank, not Bank One, and the participant would have disclosed the misappropriation.

By failing to either obtain the wire transfer documents or contact the participant to confirm the withdrawal, Johnson recklessly failed to obtain sufficient competent evidence of the transaction and exercise due professional care and professional skepticism.

AMG's lead auditor also reviewed statements for the pool account at Sentinel that reflected the \$300,000 misappropriation on February 21, 2001. The Sentinel statements showed a \$300,000 transfer to Burling Bank. As with the January transaction, the auditor asked Melrose about the purpose of the \$300,000 transfer. Melrose said it was a participant withdrawal. The auditor asked for supporting documentation. Melrose provided a copy of the participant's letter asking for the withdrawal. Unlike the letter for the January withdrawal, the letter Melrose provided to support the February transfer was a legitimate request from a pool participant. However, the letter revealed that the participant's letter asking for the funds was dated December 27, 2000, and the transfer of funds did not occur until February 18, 2001. Rather than honoring the request, Lofgren had diverted \$300,000 into his own account before eventually providing the funds to the participant.

As with the January transfer, Johnson and the AMG staff accepted the participant's letter as sufficient competent evidence and failed to obtain copies of the wire transfer documents for the transaction or contact the participant to confirm the

withdrawal. Either would have revealed that the withdrawal did not occur as represented. Specifically, the wire transfer documents for the transaction showed that the funds went to an account at Burling Bank in the name of Melrose, not the participant, and the participant would have disclosed that the withdrawal had not occurred as represented.

By failing to either obtain the wire transfer documents or contact the participant to confirm the withdrawal, Johnson recklessly failed to obtain sufficient competent evidence of the transaction and exercise due professional care and professional skepticism.

Furthermore, the participant's letter stated that he was withdrawing his funds from the pool because, among other reasons, he was unhappy over Lofgren's inability to provide him with reliable information regarding his investment. This information should have prompted additional inquiry from Johnson; however, he failed to contact the participant or otherwise inquire about the complaint. By failing to conduct any inquiry on the suspicious information, Johnson recklessly failed to exercise due professional care and professional skepticism.

The 2001 Audit

Johnson's Review of Partner Capital Transactions

In December 2001, AMG was engaged to audit the pool's financial statements for the period ending December 31, 2001 ("the 2001 audit"). AMG's audit plan for commodity pools includes an "Audit Program for Partnership Capital" that, among other objectives, tests that "partnership capital transactions have been properly authorized, approved and recorded." For the 2001 audit, AMG performed this test by selecting three additions and three withdrawals for testing. The withdrawals tested included the January and February 2001 misappropriations. Thus, after reviewing the January and February misappropriations in the subsequent events review for the 2000 audit, AMG now specifically tested the same transactions as part of the review for partnership capital in the 2001 audit.

Pursuant to AMG's procedures for testing partner capital transactions, AMG's lead auditor requested copies of the wire transfer documents for the January and February 2001 withdrawals. Melrose could not produce copies. The auditor specifically noted in the audit work papers that Melrose "did not keep adequate records regarding withdrawals."

Johnson and the AMG staff accepted Melrose's inability to produce routine documentation and failed to obtain copies of the wire transfer documents for the transactions from the entities involved in the transactions. If Johnson and the AMG staff had obtained the wire transfer documents for these transactions they would have learned that the transactions did not occur as represented.

By failing to either obtain the wire transfer documents or contact the participants to confirm the withdrawals, Johnson recklessly failed to obtain sufficient competent

evidence of the transactions and exercise due professional care and professional skepticism.

Johnson's Review of Subsequent Events

The financial statements for the 2001 audit contain a note on subsequent events that states: "During February 2002, a member made a partial withdrawal of \$750,000 from the Fund." The February withdrawal described in the note was the February 22, 2002 misappropriation.

Johnson and the AMG staff again failed to either obtain copies of the wire transfer documents for the \$750,000 withdrawal or contact the participant who purportedly withdrew the funds to confirm the transaction. If Johnson and the AMG staff had obtained the wire transfer documents or contacted the participant to confirm the withdrawal, they would have learned that the withdrawal did not occur as represented. Specifically, the wire transfer documents for the transaction showed that the funds went to an account at Burling Bank in the name of Melrose, not the participant, and the participant would have disclosed the misappropriation.

By failing to either obtain the wire transfer documents or contact the participant to confirm the withdrawal, Johnson recklessly failed to obtain sufficient competent evidence of the transaction and exercise due professional care and professional skepticism.

3. The Pool's Financial Statements Were Materially Misstated

The pool's December 31, 2000 financial statements were materially misstated because the subsequent event note on the purported withdrawals in January and February 2001 did not adequately disclose the events. The note presented the transactions as "partial withdrawals by two members." In fact, the transactions were misappropriations of pool funds by the pool operator.

The supplementary information to the pool's December 31, 2001, financial statements were materially misstated because the January and February 2001 misappropriations were included in the equity computations as withdrawals by the non-managing participants and, therefore, the financial statements supplementary information understate the non-managing participants' equity in the pool. In addition, the subsequent event note on the February 2002 misappropriation did not adequately disclose the event. The note presented the transaction as "a partial withdrawal by a member." In fact, the transaction was a misappropriation of pool funds by the pool operator.

4. Johnson's Departures From GAAS

Johnson departed from GAAS by recklessly failing to obtain sufficient competent evidence about material assertions made in the pool's financial statements and exercise due professional care and professional skepticism in conducting the audits.

GAAS includes ten standards divided into three areas: General Standards, Standards of Fieldwork and Standards of Reporting. Interpretation and practical guidance on the ten standards is provided in periodic Statements of Auditing Standards (“SAS”), which are grouped under auditing topics known as “AUs.”

The third Standard of Fieldwork states: “Sufficient competent evidential matter is to be obtained through inspection, observation, inquiries, and confirmations to afford a reasonable basis for an opinion regarding the financial statements under audit.” AU 326 on “Evidential Matter” provides guidance on what constitutes competent and sufficient evidence. AU 326 states that while the auditor should exercise judgment in determining whether evidential matter is sufficient, the accumulation of evidence should be “persuasive.” AU 326 also states that in evaluating evidential matter the auditor should be thorough, unbiased, recognize the possibility that the financial statements may not be fairly stated and should not form an opinion on the entity’s financial statements until he or she has obtained sufficient evidence to “remove any substantial doubt about a material assertion.”

The third General Standard states that: “Due professional care is to be exercised in the planning and performance of the audit and the preparation of the report.” AU 230 on “Due Professional Care in the Performance of Work” states that due professional care requires an auditor to exercise professional skepticism and explains that professional skepticism is an attitude that includes a questioning mind and a critical assessment of audit evidence. Professional skepticism means the auditor does not assume that management is dishonest nor does he assume management’s unquestioned honesty.

Johnson recklessly failed to obtain sufficient competent evidence about material assertions made in the pool’s financial statements. Johnson and the AMG staff failed to obtain sufficient competent evidence for the January and February 2001 misappropriations when they were reviewed in the subsequent review for the 2000 audit. They failed to obtain sufficient competent evidence for the January and February 2001 misappropriations when they were tested in AMG’s equity analysis for the 2001 audit. Finally, they failed to obtain sufficient competent evidence for the February 2002 misappropriation when it was noted in the subsequent review for the 2001 audit. In each instance, obtaining copies of the wire transfer documents or confirming the purported participant withdrawal with the participant provided a simple and inexpensive method by which Johnson and the AMG staff could have obtained competent evidence of the transactions that would have revealed they had not occurred as represented by Melrose.

Johnson also failed to exercise due professional care and professional skepticism when he: 1) received suspicious information from Melrose's outside accountant regarding the dispute the accountant had with Lofgren regarding Melrose's transfers from the pool's accounts and Melrose's resulting failure to provide participants with timely account statements, 2) learned that a pool participant was withdrawing his funds from the pool because, among other things, he could not receive reliable information from Lofgren on the value of his account and 3) learned that Melrose did not provide requested routine documentation on purported participant withdrawals.

IV.

OFFERS OF SETTLEMENT

The Respondents have submitted Offers of Settlement in which they acknowledge service of this Order and admit the jurisdiction of the Commission with respect to the matters set forth in the Order and waive (1) a hearing and all post-hearing procedures, (2) judicial review by any court, (3) any objection to the staff's participation in the Commission's consideration of the Offer, (4) all claims that they may possess under the Equal Access to Justice Act, 5 U.S.C. § 504 (2000) and 28 U.S.C. § 2412 (2000) and part 148 of the Commission's Regulations, 17 C.F.R. §§ 148.1, *et seq.* (2004), relating to, or arising from this action, and (5) any claim of double jeopardy based upon the institution of this proceeding or the entry in this proceeding of any order imposing a civil monetary penalty or any other relief.

The Respondents stipulate that the record basis on which the Order is entered consists of the Order and the findings in the Order consented to in the Offers. The Respondents consent to the Commission's issuance of this Order, which makes findings as set forth herein and orders that Johnson and AMG: (1) cease and desist from violating the provisions of the Commission Regulations they have been found to have violated; (2) pay a joint and several civil monetary penalty in an amount of \$150,000 (One Hundred Fifty Thousand Dollars); (3) undertake to pay joint and several restitution to defrauded pool participants in the amount of \$200,000 (Two Hundred Thousand Dollars); (4) disgorge to defrauded pool participants \$13,200 (Thirteen Thousand Two Hundred Dollars) in audit fees, and (5) comply with their undertakings as set forth in the Offers and incorporated in this Order.

V.

FINDING OF VIOLATIONS

Solely on the basis of Johnson and AMG's consent, as evidenced by the Offers, and prior to any adjudication on the merits, the Commission finds that Johnson violated Commission Regulation 1.16(d)(1) and engaged in improper unprofessional conduct within in the meaning of Commission Regulation 14.8(c) and that AMG is liable for Johnson's violations and improper unprofessional conduct pursuant to Section 2(a)(1)(B) of the Act.

VI.

ORDER

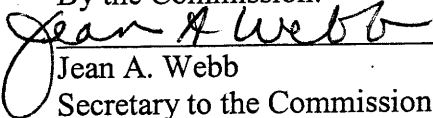
Accordingly, **IT IS HEREBY ORDERED THAT:**

- A. Johnson shall cease and desist from violating Commission Regulation 1.16(d)(1) and engaging in improper unprofessional conduct within in the meaning of Commission Regulation 14.8(c);
- B. AMG shall cease and desist from failing to employ reasonable efforts to supervise its agents in connection with the reasonable detection and prevention of violations of Commission Regulation 1.16(d)(1) and improper unprofessional conduct within in the meaning of Commission Regulation 14.8(c);
- C. Johnson and AMG shall pay a joint and several civil monetary penalty in the amount of \$150,000 (One Hundred Fifty Thousand Dollars) by electronic funds transfer, U.S. postal money order, certified check, bank cashier's check, or bank money order, made payable to the Commodity Futures Trading Commission, and sent to Dennese Posey, Division of Enforcement, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, N.W., Washington, D.C. 20581, under cover of a letter that identifies the name and docket number of this proceeding within thirty (30) days of entry of this Order;
- D. Johnson and AMG shall disgorge to defrauded pool participants \$13,200 (Thirteen Thousand Two Hundred Dollars) in audit fees, to be paid, within thirty (30) days of entry of this Order, to the Receiver appointed by the court in CFTC v. Lofgren, et al., (Docket No. 02-C-6222), in the United States District Court for the Northern District of Illinois (the "Receiver"), to be distributed pursuant to an order by the Court; and
- E. Johnson and AMG shall comply with the following undertakings as set forth in the Offers:
 1. Johnson and AMG shall pay joint and several restitution to defrauded pool participants in the amount of \$200,000 (Two Hundred Thousand Dollars), to be paid, within thirty (30) days of entry of this Order, to the Receiver, to be distributed pursuant to an order by the Court.
 2. For a period of two (2) years from the date of entry of this Order, any and all AMG accounting professionals (excluding interns or temporary employees) participating in an audit of a commodity pool or Commission registrant must undergo training in Statement of Auditing Standards ("SAS") 99, and shall not participate in any audit of any commodity pool or Commission registrant until their training has been completed.

3. For a period of two (2) years from the date of entry of this Order, any and all AMG accounting professionals (excluding interns or temporary employees) participating in an audit engagement of a commodity pool or Commission registrant must undergo fraud examination training from a certified fraud examiner, and shall not participate in any audit of any commodity pool or Commission registrant until their training has been completed.
4. For a period of two (2) years from the date of entry of this Order, a second AMG "Reviewing Partner" shall conduct a concurring review on 10% of AMG's commodity pool audit engagements.
5. AMG shall review those portions of its audit program module applicable to commodity pools that address participant withdrawals, and shall make appropriate changes or modifications as determined from the results of such review. AMG shall submit a report of its review within 180 days of the date of this Order to the Division of Enforcement.
6. AMG shall review how it ensures compliance with its audit program module applicable to commodity pools that address participant withdrawals and shall make appropriate changes or modifications as determined from the results of such review. AMG shall submit a report of its review within 180 days of the date of this Order to the Division of Enforcement.
7. Commencing with the date of this Order, Johnson shall not participate in any audit of any commodity pool or Commission registrant as an engagement partner, reviewing partner or member of an engagement team on such audit, until after December 31, 2005, but may provide technical and general advice and consultation in connection with such audits.
8. Neither Johnson nor AMG, nor any of their agents or employees under their authority or control, shall take any action or make any public statements denying, directly or indirectly, any finding in this Order, or creating, or tending to create, the impression that this Order is without a factual basis; provided, however, that nothing in this provision shall affect any partner or employee of AMG or Johnson's (i) testimonial obligations; or (ii) right to take legal positions in other proceedings to which the Commission is not a party.

The provisions of this Order shall be effective on this date.

By the Commission:



Jean A. Webb

Secretary to the Commission

Commodity Futures Trading Commission

Dated: June 13, 2005 .