

UNITED STATES OF AMERICA
Before the
COMMODITY FUTURES TRADING COMMISSION

In the Matter of:

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

Respondents.

CFTC Docket No. 04-29

COMPLAINT AND NOTICE OF
HEARING PURSUANT TO SECTIONS
6(c) AND 6(d) OF THE COMMODITY
EXCHANGE ACT, AS AMENDED AND
PART 14 OF THE COMMISSION'S
REGULATIONS

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The Commodity Futures Trading Commission ("Commission") has received evidence from its staff which tends to show, and the Commission's Division of Enforcement ("Division") alleges, that:

I.

SUMMARY

1. At all times relevant herein, Melrose Asset Management, Inc. ("Melrose") was a registered commodity pool operator ("CPO") and John Martin Lofgren ("Lofgren") was Melrose's chief executive officer. Melrose operated a commodity pool entitled The Melrose Fund, L.L.C. ("the pool"). At various times between at least January 2001 and February 2002, Lofgren misappropriated pool funds and attempted to disguise the misappropriations as withdrawals by pool participants.

2. Respondent Altschuler, Melvoin and Glasser, LLP ("AMG"), a public accounting firm, performed annual audits of the pool's financial statements ("the financial statements") for the years ending December 31, 2000 and December 31, 2001. Respondent G. Victor Johnson ("Johnson") was the engagement partner for the audits.

3. AMG issued unqualified auditor's reports that the pool's financial statements were free from material misstatement and Johnson signed the reports on behalf of AMG. In fact, the financial statements were materially misstated and Johnson failed to conduct the audits of the financial statements in accordance with generally accepted auditing standards ("GAAS"). Specifically, Johnson and AMG's audit team reviewed and tested certain of the misappropriations Lofgren disguised as withdrawals, but failed to obtain sufficient competent evidence of the transactions. In addition, Johnson failed to exercise due professional care in conducting the audits. Johnson's failure to conduct the audits in accordance with GAAS violated Commission Regulation 1.16(d)(1), 17 C.F.R. § 1.16(d)(1) (2004), and constituted improper unprofessional conduct under Commission Regulation 14.8(c), 17 C.F.R. § 14.8(c) (2004).

II.

RESPONDENTS

4. 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.

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

III.

RELEVANT SECTIONS OF THE ACT AND REGULATIONS

6. Commission Regulation 1.16(d)(1), 17 C.F.R. § 1.16(d)(1) (2004), requires that audits conducted pursuant to the Commission's regulations be conducted in accordance with GAAS.

7. Commission Regulation 14.8 (c), 17 C.F.R. § 14.8(c) (2004), provides that the Commission may, after notice and opportunity for a hearing in the matter, deny, temporarily or permanently, the privilege of appearing or practicing before it in any way to any person who is found by the Commission, by a preponderance of the evidence, to have engaged in unethical or improper unprofessional conduct either in the course of an adjudicatory, investigative, rulemaking or other proceeding before the Commission or otherwise.

8. Section 2(a)(1)(B) of the Act, 7 U.S.C. § 4 (2002), provides that the act, omission or failure of any official, agent or other person acting for any individual, association, partnership, corporation or trust within the scope of his employment or office shall be deemed the act, omission or failure of such individual, association, partnership, corporation or trust, as well as of such official, agent or other person.

IV.

FACTS

Lofgren's Misappropriations

10. On January 18, 2001, Lofgren misappropriated \$500,000 from the pool. On February 21, 2001, Lofgren misappropriated another \$300,000. On February 22, 2002, Lofgren misappropriated another \$750,000. In each instance, Lofgren wire transferred the funds from a pool account ("the 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”).

AMG’s Audits

11. AMG was initially engaged by Melrose to audit the pool’s financial statements for the period ending December 31, 1999 (“the 1999 audit”). Johnson was the engagement partner responsible for planning, supervising and reviewing the 1999 audit. Megan Hannigan (“Hannigan”), an employee of AMG, was the lead or in-charge auditor for the engagement.

12. AMG’s audits for commodity pools include a Risk Identification and Planning program. In completing the program 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.

13. In or around December 2000, AMG was engaged to audit the pool’s financial statements for the period ending December 31, 2000 (“the 2000 audit”). Johnson was the engagement partner responsible for planning, supervising and reviewing the 2000 audit. Hannigan was the lead or in-charge auditor for the 2000 audit. In September or October 2000, Melrose’s outside accountant, who also prepared the account statements for pool participants, informed Johnson that Melrose had not provided account statements to pool participants since July 2000. The accountant informed Johnson that he had refused to release the account statements to Lofgren until he resolved a dispute with Lofgren involving approximately \$350,000 that the accountant maintained Lofgren had

improperly transferred from accounts belonging to the pool to an account belonging to a third party that Lofgren managed.

14. On or about March 6, 2001, Hannigan, under the direction of Johnson, met with Melrose regarding Melrose's failure to distribute account statements to pool participants. After consulting with Johnson, Hannigan advised Melrose that Melrose needed to notify the Commission it had not been distributing account statements to pool participants. Melrose did not notify the Commission that it had not been distributing account statements and Johnson did not follow-up to see that the Commission was notified.

15. 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, Johnson failed to attempt to understand the nature of the dispute between Lofgren and the pool's outside accountant or the transactions underlying the dispute. Johnson failed to exercise due professional care and professional skepticism when he learned of the dispute between Lofgren and the pool's outside accountant over the transfer of pool funds to a third party's account and Melrose's failure to distribute required account statements to pool participants. By failing to adequately inform himself of the nature of the dispute and the underlying transactions, Johnson was reckless.

16. On or about March 27, 2001, AMG issued its auditor's report for the 2000 audit. AMG issued an unqualified report that the financial statements were free from material misstatement. Johnson signed the auditor's report on behalf of AMG. The financial statements 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 described in paragraph 10 above.

Johnson’s Review of the \$500,000 Misappropriation

17. In or around March 2001, Hannigan reviewed statements for the pool account at Sentinel reflecting the January 2001 misappropriation and asked Melrose the purpose of the \$500,000 transfer “from Sentinel to Burling Bank.” Melrose responded that it was a withdrawal by a participant. Hannigan requested a copy of the withdrawal request. A Melrose employee sent a copy of a letter to Hannigan, purportedly from the participant, advising Lofgren that he wanted to withdraw funds.

18. The letter referred to in paragraph 17 was not authentic. Rather, it was fabricated by Lofgren. Specifically, Lofgren had taken an earlier letter from the participant who purportedly requested the \$500,00 withdrawal and altered its date, the amount requested, and other information so that it would appear as if the participant requested the withdrawal of the \$500,000 in January 2001.

19. Although the purpose of the fabricated letter was to disguise his misappropriation, Lofgren made an incriminating error that revealed it as a counterfeit. The participant’s original letter instructed that funds be sent to Bank One. Lofgren, however, failed to alter this instruction and left it in the counterfeit 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 actually was sent), Lofgren left incriminating evidence that the participant did not request the withdrawal of funds. At a minimum, the counterfeit letter did not provide sufficient competent evidence of the legitimacy of the transactions.

20. In his review of Hannigan's work, Johnson simply accepted this counterfeit letter as sufficient competent evidence and failed to either obtain copies of the wire transfer documents for the transaction or contact the participant to confirm the withdrawal. If Johnson had obtained either the wire transfer documents and reviewed the documents or contacted the participant to confirm the withdrawal, he 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. As a result, pursuant to GAAS principles, Johnson would not have been able to issue an unqualified report for the 2000 audit. Johnson failed to exercise due professional care when he failed to obtain the wire transfer documents or contact the participant to confirm the withdrawal in his review of the \$500,000 withdrawal. Johnson's failure to obtain the wire transfer documents or contact the participant to confirm the withdrawal was reckless.

Johnson's Review of the \$300,000 Misappropriation

21. In or around March 2001, Hannigan also reviewed statements for the pool account at Sentinel reflecting Lofgren's \$300,000 February 2001 misappropriation. In this scheme, Lofgren had misappropriated \$300,000 from a participant by diverting into his own account funds sought to be withdrawn by that participant. Lofgren misappropriated the funds for a period of time and then eventually repaid the participant. Hannigan requested documentation on the transfer of the \$300,000. In response to Hannigan's request, a Melrose employee sent a letter from a participant requesting the funds.

22. In his review of the \$300,000 withdrawal, Johnson simply accepted the letter referred to in paragraph 21 as sufficient competent evidence and failed to either obtain copies of the wire transfer documents for the transaction or contact the participant to confirm the withdrawal. If Johnson had obtained either the wire transfer documents and reviewed the documents or contacted the participant to confirm the withdrawal, he would have learned 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. As a result, pursuant to GAAS principles, Johnson would not have been able to issue an unqualified report for the 2000 audit. Johnson failed to exercise due professional care when he failed to obtain the wire transfer documents or contact the participant to confirm the withdrawal in his review of the \$300,000 withdrawal. Johnson's failure to obtain the wire transfer documents or contact the participant to confirm the withdrawal was reckless.

23. The participant's letter described in paragraph 21 stated that he was withdrawing funds from the pool because he was unhappy with Lofgren's inability to provide him with reliable information regarding his investment. Johnson failed to contact the participant and inquire about Lofgren's unreliability. This failure was reckless.

Johnson's Review of the "Audit Program for Partnership Capital"

24. In or around December 2001, AMG was engaged to audit the pool's financial statements for the period ending December 31, 2001 ("the 2001 audit"). Johnson was the engagement partner responsible for planning, supervising and reviewing the 2001 audit. Hannigan was the lead or in-charge auditor for 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, Johnson and Hannigan performed this test by selecting three additions and three withdrawals for testing. The withdrawals tested included the January and February 2001 misappropriations.

25. In performing the tests described in paragraph 24 above, Hannigan traced the January and February 2001 misappropriations to the Sentinel statements but did not obtain copies of the wire transfer documents. Hannigan did not obtain copies of the wire transfer documents because Melrose could not produce copies. Hannigan noted in the audit work papers that Melrose “did not keep adequate records regarding withdrawals.”

26. In his review of Hannigan’s work on the audit program, Johnson simply accepted Melrose’s excuse about the absence of essential documentation and failed to obtain copies of the wire transfer documents for the transactions from the entities involved in the transactions. If Johnson had obtained the wire transfer documents for these transactions, and reviewed these documents, he would have learned that the transactions did not occur as represented. As a result, pursuant to GAAS principles, Johnson would not have been able to issue an unqualified report for the 2001 audit. Johnson failed to exercise due professional care when he learned that Melrose did not maintain adequate records regarding the withdrawals and then failed to obtain the wire transfer documents in his review of these transactions. Johnson’s failure to obtain the wire transfer documents in his review of these transactions was reckless.

Johnson's Review of the \$750,000 Misappropriation

27. On or about March 27, 2002, AMG issued its auditor's report for the 2001 audit. AMG issued an unqualified report that the financial statements were free from material misstatement. Johnson signed the auditor's report on behalf of AMG. 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 2002 misappropriation described in paragraph 10 above.

28. In his review of the \$750,000 withdrawal, Johnson 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 had obtained either the wire transfer documents and reviewed them or contacted the participant to confirm the withdrawal, he would have learned 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. As a result, pursuant to GAAS principles, Johnson would not have been able to issue an unqualified report for the 2000 audit. Johnson failed to exercise due professional care when he failed to obtain the wire transfer documents or contact the participant to confirm the withdrawal in his review of the \$750,000 withdrawal. Johnson's failure to obtain the wire transfer documents or contact the participant to confirm the withdrawal was reckless.

The Pool's Financial Statements Were Materially Misstated

29. The 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.

30. The December 31, 2001, financial statements were materially misstated because January and February 2001 misappropriations were included in the equity computations as withdrawals by the non-managing participants and, therefore, the financial statements 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.

AMG's Departures From GAAS

31. Johnson recklessly failed to obtain sufficient competent evidence about material assertions made in the pool's financial statements. Specifically, he failed to obtain sufficient competent evidence on the January and February 2001 misappropriations and the February 2002 misappropriation noted as withdrawals in the subsequent event reviews for the 2000 and 2001 audits and for the January and February 2001 misappropriations when they were tested in AMG's equity analysis for the 2001 audit.

IV.

VIOLATIONS OF THE ACT AND THE REGULATIONS

COUNT I

**JOHNSON VIOLATED SECTION 1.16(d)(1)
OF THE COMMISSION'S REGULATIONS**

32. The allegations contained in paragraphs 1 through 31 are realleged and incorporated herein by reference.

33. Johnson failed to conduct the audits of Melrose's December 31, 2000 and December 31, 2001 financial statements in accordance with GAAS by recklessly failing to obtain sufficient competent evidence and exercise due professional care in performing the audits, in violation of Commission Regulation 1.16(d)(1).

34. AMG is liable for Johnson's violations of Commission Regulation 1.16(d)(1) by virtue of Section 2(a)(1)(B) of the Act.

COUNT II

**JOHNSON ENGAGED IN IMPROPER UNPROFESSIONAL CONDUCT
UNDER TO SECTION 14.8(c) OF THE COMMISSION'S REGULATIONS**

35. The allegations contained in paragraphs 1 through 31 are realleged and incorporated herein by reference.

36. Johnson engaged in improper unprofessional conduct by failing to conduct the audits of Melrose's December 31, 2000 and December 31, 2001 financial statements in accordance with GAAS. Johnson's reckless failure to obtain sufficient competent evidence and exercise due professional care in performing the audits constituted improper unprofessional conduct under Commission Regulation 14.8(c).

37. AMG is liable for Johnson's improper unprofessional conduct by virtue of Section 2(a)(1)(B) of the Act.

V.

By reason of the foregoing allegations, the Commission deems it necessary and appropriate, pursuant to its responsibilities under the Act, to institute public administrative proceedings to determine whether the allegations set forth in Parts I-IV above are true and, if so, whether an appropriate order should be entered in accordance with Sections 6(c) of the Act, 7 U.S.C. § 9 (2002) and Part 14 of the Commission's Regulations, 17 C.F.R. § 14.1 et seq. (2004):

- a) Directing that the Respondents cease and desist from violating the provisions of the Act and Regulations set forth in Parts I-IV of the Complaint;
- b) Assessing against the Respondents a civil monetary penalty in an amount of not more than the higher of \$120,000 or triple the monetary gain to the Respondents for each violation of the Act and Regulations; and
- c) Denying the Respondents, temporarily or permanently, the privilege of appearing or practicing before the Commission.

VI.

WHEREFORE, IT IS HEREBY ORDERED that a public hearing for the purpose of taking evidence on the allegations set forth in Section I-IV above be held before an Administrative Law Judge, in accordance with the Commission's Rules of Practice under the Act (the "Commission's Rules"), 17 C.F.R. §§ 10.1 et seq. (2004), at a time and place to be set as provided by Section 10.61 of the Commission's Rules, 17 C.F.R. § 10.61

(2003), and that all post-hearing procedures shall be conducted pursuant to Sections 10.81 through 10.107 of the Commission's Rules, 17 C.F.R. §§ 10.81-10.107 (2004).

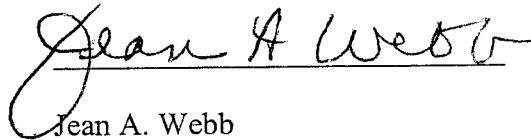
IT IS FURTHER ORDERED that the Respondents shall file an Answer to the allegations contained in this Complaint within twenty (20) days after service, pursuant to Section 10.23 of the Commission's Rules, 17 C.F.R. § 10.23 (2004), and shall serve two copies of such Answer and of any documents filed in these proceedings upon Rosemary Hollinger, Regional Counsel and David A. Terrell, Senior Trial Attorney, Division of Enforcement, Commodity Futures Trading Commission, 525 W. Monroe, Chicago, Illinois 60606 or upon such other counsel as may be designated by the Division. If the Respondents fail to file the required Answer, or fail to appear at a hearing after being duly served, Respondents shall be deemed in default and the proceedings may be determined against Respondents upon consideration of the Complaint, the allegations of which shall be deemed to be true.

IT IS FURTHER ORDERED that this Complaint and Notice of Hearing shall be served upon the Respondents personally or by registered or certified mail, pursuant to Section 10.22 of the Commission's Rules, 17 C.F.R. § 10.22 (2004).

In the absence of an appropriate waiver, no officer or employee of the Commission engaged in the performance of investigative or prosecutorial functions in this or any factually related proceedings will be permitted to participate or advise the

decision in this matter except as a witness or counsel in a proceeding held pursuant to notice.

By the Commission.

A handwritten signature in cursive script that reads "Jean A. Webb". The signature is written in black ink and is positioned above a horizontal line.

Jean A. Webb
Secretary to the Commission
Commodity Futures Trading Commission

Date: September 30, 2004