



U.S. Securities and Exchange Commission

SECURITIES AND EXCHANGE COMMISSION

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Accounting and Auditing Enforcement Release No. 1361 / January 23, 2001

SEC CHARGES MULTI -MILLION DOLLAR FINANCIAL REPORTING FRAUD AGAINST FORMER CHAIRMAN AND OTHER FORMER SENIOR OFFICERS AND EMPLOYEES OF AURORA FOODS INC.

SEC V. AURORA FOODS INC., ET AL., 01 CIV 0554 (AKH) S.D.N.Y.

The Commission announced today that it has brought securities fraud charges against three former senior officers and four employees of Aurora Foods Inc. ("Aurora" or the "Company"), a producer and marketer of branded food products, in connection with a scheme that caused Aurora to under-report trade marketing expenses and substantially inflate reported earnings in 1998 and 1999. In addition, the Complaint charges Aurora and another former employee with corporate reporting and record keeping violations. The Commission further announced that, simultaneous with the filing of the Complaint, it settled the charges against Aurora and two of the individual defendants.

The Complaint alleges that, during 1998 and the first three quarters of 1999, Aurora under-reported trade marketing expenses by more than \$43 million. Aurora's senior management, consisting of defendants Ian R. Wilson ("Wilson"), M. Laurie Cummings ("Cummings") and Ray Chung ("Chung"), was aware that Aurora was not accurately reporting trade marketing expense, which is the expense Aurora incurs to induce grocery stores to purchase its products, for example, a case discount or other similar incentive. Instead of properly booking the expense, Wilson, Cummings and Chung tried to conceal it from the auditors by directing division level officers and employees to make false entries in various accounts on the Company's books. The effect was to falsely and substantially inflate the Company's financial results.

The defendants are as follows:

Aurora is a Delaware corporation with its principal place of business in St. Louis, Missouri. During the relevant time period, Aurora had its principal places of business in St. Louis, Missouri and Columbus, Ohio, and its corporate headquarters at the offices of Dartford Partnership, LLC in San Francisco, California. Aurora's common stock trades on the New York Stock Exchange. At all relevant times, Aurora's business was divided into two divisions, the Aurora Foods division ("AFI") and the Van de Kamp's division ("VDK"). Aurora markets products including Duncan Hines baking mix, Mrs. Butterworth's and Log Cabin syrup, Van de Kamp's and Mrs. Paul's frozen seafood, Aunt Jemima frozen breakfast products and Celeste frozen pizza.

Wilson, age 71, was Chairman of the Board and Chief Executive Officer of Aurora from June 1998 until he resigned on February 17, 2000. Wilson is a resident of San Francisco, California.

Cummings, age 36, was the Chief Financial Officer of Aurora from June

1998 until she resigned on February 17, 2000. Cummings is a resident of San Francisco, California.

Chung, age 51, was the Executive Vice-President of Aurora from June 1998 until he resigned on February 17, 2000. Chung is a resident of Houston, Texas.

Dirk Grizzle ("Grizzle") was the vice-president of finance and principal financial officer of Aurora's AFI division until June 2000. Grizzle is a resident of Westerville, Ohio.

Tammy Fancelli ("Fancelli") was a Senior Financial Analyst at Aurora's AFI division until September 2000. Fancelli is a resident of Columbus, Ohio.

James Elliott ("Elliott") was the Manager of Customer Financial Services at Aurora's AFI division until September 2000. Elliott is a resident of Powell, Ohio.

Timothy B. Andersen ("Andersen") was the vice-president of finance and principal financial officer at Aurora's VDK division until June 2000. Andersen is a resident of St. Louis, Missouri.

Keith Luechtefeld ("Luechtefeld") was the Controller at Aurora's VDK division until June 2000. Luechtefeld is a resident of St. Louis, Missouri.

The Complaint alleges as follows:

During 1998 and the first three quarters of 1999, defendants Wilson, Cummings and Chung systematically understated Aurora's trade promotion expense associated with the marketing of the Company's products. They accomplished this by directing the division-level defendants to (i) make inadequate or no accruals for known trade marketing expenses incurred in connection with sales already booked and (ii) hide these inadequate accruals from the Company's auditors by making false entries in various accounts on the Company's books. The result was materially to understate expenses and liabilities on the Company's publicly filed financial statements. The object of the scheme was to conceal from the investing public the fact that the Company had not met its earnings targets from quarter to quarter.

At the Company's AFI division, the key participant was defendant Grizzle, AFI's principal financial officer. Beginning in or about March 1999, Grizzle and Cummings discussed putting known trade promotion expenses in accounts receivable, rather than simply recording them on the books of the Company. The effect would be to conceal these expenses from the auditors. Thereafter, on a regular basis, Cummings and/or Chung instructed Grizzle to move large portions of the expense to accounts receivable. Grizzle carried out these instructions by directing defendants Fancelli and Elliott to make false entries in the accounts receivable ledgers and subsidiary ledgers. Beginning in about April 1999, Grizzle also prepared, at least quarterly, two versions of AFI's trade promotions reserve analysis, one for the Company's internal use, which showed an ever-growing trade underaccrual, consisting primarily of items of actual, known expense, and the other to be provided to the auditors, which falsely showed AFI in an overaccrued position.

At the Company's VDK division, defendant Andersen, VDK's principal financial officer, carried out Cummings' and Chung's instructions to reduce expenses on the books to enable Aurora to hit "must make" numbers on a quarterly or more frequent basis. In almost every instance, in order to hit these earnings targets, Andersen reduced trade promotion expense and the accompanying trade promotion accrual, even though he knew that VDK had already recorded insufficient trade expense and had underaccrued the trade

promotion reserve.

Andersen accomplished this by directing VDK's Director of Budget and Planning to reduce the trade promotion accrual. Because the division's computers automatically posted accruals to the reserve account as sales were posted, the automated entries had to be adjusted manually. However, as Cummings eventually became concerned that these manual entries would draw audit scrutiny, Cummings directed Andersen to turn off the automated posting system. Thereafter, all accruals were posted by hand at the levels dictated by Cummings.

In order to conceal further the underaccrual from the auditors, Cummings directed VDK's Director of Budgeting and Planning to prepare for the auditors a version of the trade reserve analysis employing incorrect assumptions, which, had they been disclosed, would have immediately revealed the inadequacy of the accruals.

Defendant Luechtefeld, VDK's Controller, was aware of these deliberate underaccruals, and, on at least one occasion, carried out Andersen's instruction to conceal the underaccruals by shifting \$2 million from other liability accounts on VDK's books to the trade promotion reserve. These entries had no purpose other than to make it appear to the auditors that the accrual was adequate, when, in fact, it was not.

Throughout 1999, division officers at both AFI and VDK regularly informed Aurora CEO Wilson of the substantial trade accrual deficit, but Wilson refused to take action to correct the problem and, from time to time, noted his concurrence in actions directed by his subordinates Cummings and Chung to conceal the underaccrual. Wilson also made several public statements in 1999 concerning the Company's financial condition, which failed to disclose the substantial unrecorded trade marketing expense. By January 2000, Wilson actively participated in efforts to conceal the false accounting entries from the auditors and personally directed division employees to lie to the auditors.

The Commission alleges that, as a result of the foregoing, Wilson, Chung, Cummings, Grizzle, Fancelli, Andersen and Luechtefeld violated, or aided and abetted violations of, Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act"), and Rule 10b-5; that all of the individual defendants violated Section 13(b)(5) of the Exchange Act and Rule 13b2-1 in connection with a financial reporting fraud involving Aurora; that Wilson, Chung and Cummings also violated Rule 13b2-2 promulgated under the Exchange Act; that Aurora violated Sections 13(a) and 13(b)(2) of the Exchange Act and Rules 12b-20, 13a-1 and 13a-13; and that Wilson, Chung and Cummings, as control persons of Aurora, are liable for Aurora's violations of Sections 13(a) and 13(b)(2) of the Exchange Act and Rules 12b-20 and 13a-13.

The Commission seeks a Final Judgment (i) permanently enjoining each defendant from future violations of the securities laws; (ii) ordering Wilson, Chung, Cummings and Grizzle to disgorge performance bonuses paid to them on the basis of materially overstated earnings, plus prejudgment interest; (iii) imposing civil penalties against each defendant (except Aurora); and (iv) barring Wilson, Chung, Cummings and Grizzle from serving as an officer or director of a public company.

The Company has consented to the entry of a final judgment that permanently enjoins the Company from further violations of the reporting and internal control provisions of the federal securities law.

Defendant Fancelli has consented to the entry of a final judgment that permanently enjoins her from further violations of the antifraud and

reporting and internal control provisions of the federal securities laws and that orders her to pay a civil penalty in the amount of \$20,000.

Defendant Elliott has consented to the entry of a final judgment that permanently enjoins him from further violations of the reporting and internal control provisions of the federal securities laws and that orders him to pay a civil penalty in the amount of \$10,000.

The litigation is pending in the United States District Court for the Southern District of New York.

The Commission acknowledges the assistance of the United States Attorney's Office, Southern District of New York, in this investigation.

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