

**UNITED STATES OF AMERICA**  
**Before the**  
**SECURITIES AND EXCHANGE COMMISSION**

**SECURITIES EXCHANGE ACT OF 1934**  
**Release No. 61195 / December 17, 2009**

**ACCOUNTING AND AUDITING ENFORCEMENT**  
**Release No. 3086 / December 17, 2009**

**ADMINISTRATIVE PROCEEDING**  
**File No. 3-13724**

<p><b>In the Matter of</b></p> <p><b>THOMAS D. VOGELSINGER, CPA,</b></p> <p><b>Respondent.</b></p>
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**ORDER INSTITUTING PUBLIC  
ADMINISTRATIVE PROCEEDINGS  
PURSUANT TO SECTION 4C OF THE  
SECURITIES EXCHANGE ACT OF 1934  
AND RULE 102(e) OF THE  
COMMISSION'S RULES OF  
PRACTICE, MAKING FINDINGS, AND  
IMPOSING REMEDIAL SANCTIONS**

**I.**

The Securities and Exchange Commission (“Commission”) deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted against Thomas D. Vogelsinger, CPA (“Vogelsinger” or “Respondent”) pursuant to Sections 4C<sup>1</sup> of the Securities and Exchange Act of 1934 (“Exchange Act”) and Rule 102(e)(1)(ii) of the Commission’s Rules of Practice.<sup>2</sup>

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<sup>1</sup> Section 4C provides, in relevant part, that:

The Commission may censure any person, or deny, temporarily or permanently, to any person the privilege of appearing or practicing before the Commission in any way, if that person is found . . . (1) not to possess the requisite qualifications to represent others . . . (2) to be lacking in character or integrity, or to have engaged in unethical or improper professional conduct; or (3) to have willfully violated, or willfully aided and abetted the violation of, any provision of the securities laws or the rules and regulations thereunder.

<sup>2</sup> Rule 102(e)(1) provides, in relevant part, that:

The Commission may censure a person or deny, temporarily or permanently, the privilege of appearing or practicing before it . . . to any person who is found . . .

\* \* \*

(ii) to have engaged in unethical or improper professional conduct.

\* \* \*

## II.

In anticipation of the institution of these proceedings, Vogelsinger has submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission's jurisdiction over him and the subject matter of these proceedings, which are admitted, Vogelsinger consents to the entry of this Order Instituting Public Administrative Proceedings Pursuant to Section 4C of the Securities Exchange Act of 1934 and Rule 102(e) of the Commission's Rules of Practice, Making Findings, and Imposing Remedial Sanctions ("Order"), as set forth below.

## III.

On the basis of this Order and Vogelsinger's Offer, the Commission finds<sup>3</sup> that:

### Summary

1. This matter involves improper professional conduct by Vogelsinger during his tenure as the Area Managing Partner of the Lake Michigan Area of Ernst & Young LLP ("E&Y"). The Lake Michigan Area ("LMA") included the Chicago, Grand Rapids and Milwaukee offices. Vogelsinger engaged in repeated instances of unreasonable conduct in failing to detect problems with respect to a revenue recognition policy of an E&Y audit client, Bally Total Fitness Holding Corporation ("Bally"). Bally's prior accounting policy for the revenue at issue, which E&Y had audited for years, was clearly not in conformity with accounting principles generally accepted in the United States ("GAAP").

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(iv) with respect to persons licensed to practice as accountants, "improper professional conduct" under §201.102(e)(1)(ii) means:

\* \* \*

(B) either of the following two types of negligent conduct:

\* \* \*

(2) repeated instances of unreasonable conduct, each resulting in a violation of applicable professional standards, that indicate a lack of competence to practice before the Commission.

<sup>3</sup> The findings herein are made pursuant to Vogelsinger's Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

2. Vogelsinger did not exercise due care as required by professional standards.<sup>4</sup> Had he done so, he would have discovered that the revenue recognition policy was not in conformity with GAAP.

### **Respondent**

3. Vogelsinger, age 59, was a certified public accountant licensed in Illinois and Iowa during the relevant period. Vogelsinger was the LMA Managing Partner from 2000 until October 2003, and was in charge of E&Y's Chicago, Grand Rapids and Milwaukee offices. He was responsible for overseeing all activities in those offices, including, among others, participating in client continuance decisions and risk management efforts with respect to certain of E&Y's highest risk audit clients. Vogelsinger retired from E&Y in 2009.

### **Other Relevant Entities**

4. E&Y is a national public accounting firm and, during the relevant period covered by this Order, served as the independent auditor for Bally.

5. Bally, a Delaware corporation, purported to be the largest, and only nationwide, commercial operator of fitness centers. At all relevant times, Bally's common stock was registered with the Commission pursuant to Section 12(b) of the Exchange Act and traded on the New York Stock Exchange ("NYSE"). The NYSE delisted Bally's common stock on June 8, 2007. After filing for reorganization under Chapter 11 of the Bankruptcy Code, on September 17, 2007, Bally emerged as a privately held reorganized entity. On February 28, 2008, the Commission filed a settled injunctive action against Bally in the United States District Court for the District of Columbia, charging Bally with violating Section 17(a) of the Securities Act of 1933, Sections 10(b), 13(a), 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act, and Rules 10b-5, 12b-20, 13a-1, 13a-11 and 13a-13 thereunder. The District Court issued permanent injunctions on May 8, 2008.

### **Bally's "Reactivation" Revenue Recognition**

6. The particular revenue recognition policy with respect to which Vogelsinger failed to exercise due care pertained to Bally's "reactivation" revenue.

7. Bally recognized revenue from what it called "reactivations," which were payments from Bally members who had completed their initial contract period, but whose memberships were canceled for failure to pay the monthly dues necessary to maintain their membership. Bally did not attempt to recover those dues because there was no legal obligation to pay dues. Accordingly, for those canceled members who had completed the initial contract

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<sup>4</sup> Article V of the Principles of Professional Conduct (ET Section 56) requires that an accountant exercise due care when discharging professional responsibilities. Due care requires the accountant to discharge professional responsibilities with competence and diligence. Diligence imposes the responsibility to render services carefully, to be thorough, and to observe applicable technical and ethical standards.

period, Bally waited at least six months after receiving their last payment and then began soliciting those canceled members to reactivate. Those who accepted the reactivation offers did so, on average, 36 months after having stopped paying monthly dues. The reactivation offers did not contain claims for or seek payment of "past due" amounts. Instead, they asked for either a nominal reactivation fee or no reactivation fee at all, and the payment of monthly dues for a period of future service.

8. Bally's reactivation revenue recognition policy was to project (as of the balance sheet date) the reactivation payments it anticipated receiving in the coming year and then immediately recognize most of these projected payments by improperly allocating them to past periods. Bally's reactivation accounting was not in conformity with GAAP because use of the method enabled Bally to recognize revenue before it was earned and was realized or realizable.<sup>5</sup> Bally recognized revenue before it was earned because, among other things, it barred canceled former members from the gyms, and therefore, had not provided services to those of its canceled members who might reactivate in the future. Additionally, Bally recognized revenue before it was realized or realizable because it was recognizing revenue for reactivations that had not yet occurred, which it anticipated from canceled former members whom it could not identify individually and who had no legal obligation to reactivate or pay Bally anything at all.

9. In short, Bally violated GAAP by recognizing revenue related to the anticipated future payments before the reactivation transactions occurred. A reasonable accountant who understood Bally's accrual basis of recognizing revenue for "reactivations" would conclude that it was not in conformity with GAAP, because Bally was recognizing revenue that was not realized or realizable, and had not been earned.

10. For at least six years, E&Y had audited Bally's "reactivation" revenue recognition practices. In each of those years, E&Y provided Bally with an unqualified audit opinion in violation of GAAS.<sup>6</sup>

### **Vogelsinger's Involvement In E&Y's Risk Management Efforts**

11. In 2001 and 2002, a series of widely known financial scandals led E&Y to assess its audit risks and the firm took steps to identify and resign from or focus on certain of its riskiest clients. These 18 riskiest accounts -- including Bally -- were so-called "National Focus Accounts" and were monitored by the Americas Executive Board. Bally was not only identified as a National Focus Account, it was identified as the riskiest account in E&Y's Lake Michigan Area.

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<sup>5</sup> See, e.g., Accounting Research Bulletin No. 43, *Restatement and Revision of Accounting Research Bulletins*, Chapter 1A (1953); Accounting Principles Board Opinion No. 10, Omnibus Opinion (1966); Statement of Financial Accounting Concepts No. 5, *Recognition and Measurement in Financial Statements of Business Enterprises* (1985); Staff Accounting Bulletin No. 101, *Revenue Recognition in Financial Statements*, Topic 13.A (1999).

<sup>6</sup> See AICPA's Codification of Auditing Standards AU § 508, *Reports on Audited Financial Statements*.

12. Because of the high risk posed by Bally, and the heightened scrutiny that was warranted for engagements identified as “National Focus Accounts,” as the LMA Managing Partner, Vogelsinger was actively involved in helping manage the risk posed to E&Y by Bally. As discussed below, Vogelsinger participated in multiple internal E&Y meetings that focused on the risks presented by the Area and National Focus Accounts, including Bally, and on the steps taken by E&Y to mitigate those risks. Additionally, he participated in two meetings with Bally executives that were intended to improve Bally’s accounting and mitigate E&Y’s risk.

### **The 2002 Meetings**

13 Beginning in June 2002, Vogelsinger attended meetings with other senior E&Y partners which focused on the risks presented to E&Y by certain audit clients, including Bally, and on the steps taken by E&Y to mitigate those risks.

14 On June 14, 2002, Vogelsinger met to discuss client continuance with, among others, Mark Sever and Kenneth Peterson. Both Sever and Peterson were members of E&Y’s National Office. Bally was one of ten high-risk accounts in the Lake Michigan Area that were discussed in that meeting. Among the risks posed by Bally that were discussed at that meeting was Bally’s management, which was difficult and engaged in aggressive accounting.

15 On July 16, 2002, Vogelsinger attended another meeting with, among others, Sever, Peterson, and John Kiss, who had been the Bally audit engagement partner since 1996. That meeting likewise focused on the risks presented to E&Y by Bally and on the steps taken by E&Y to mitigate those risks.

16 On September 11, 2002, Vogelsinger had another meeting with Peterson to discuss Bally’s risks.

17 On October 28, 2002, Vogelsinger, Peterson, Sever, and Kiss met again to discuss mitigating Bally’s risks. Those risks concerned Bally’s management, which engaged in “aggressive” accounting with respect to accounting policies and estimates. Among the topics discussed was Bally’s accounting for reactivations.

18 By January 2003, E&Y was contemplating resigning from Bally "due to risk issues." Ultimately, Vogelsinger and other senior E&Y partners decided not to resign. That decision was made at a meeting on March 6, 2003.

### **The March 6, 2003 Internal E&Y Meeting**

19. On March 6, 2003, Vogelsinger met with, among others, Sever, Peterson, and Kiss. The subject of the meeting was whether E&Y should resign as Bally's auditor. Kiss prepared a one-page list of the reasons to retain Bally and the reasons to resign. The participants at the meeting discussed the list of reasons to retain and resign and discussed E&Y's exposure.

Under the heading, “Estimates/Complexity in Business Model,” “Reactivations” was listed as one of the reasons to resign.

20. At the end of the discussion, Vogelsinger and the others decided not to resign but to stay on and reduce the firm’s risk.

### **The March 11, 2003 Meeting With Bally’s CFO**

21. On March 11, 2003, Vogelsinger met privately with Bally CFO John Dwyer, who was a former E&Y audit partner, and delivered a one-page document, the “Terms of Engagement,” containing E&Y’s conditions for remaining as Bally’s auditor. During the meeting, Vogelsinger and Dwyer discussed various accounting issues, but Vogelsinger did not request any information about Bally’s reactivation revenue recognition policy.

### **Selection Of A New Engagement Partner**

22. Because Kiss was required to rotate off the Bally account, E&Y needed to designate a new engagement partner for the 2003 audit. Vogelsinger and others identified William J. Carpenter as a suitable successor to Kiss. They selected Carpenter because of his ability to "deliver tough messages."

23. Vogelsinger and the AABS Managing Partner briefed Carpenter about the Bally engagement. They advised him that Bally was considered one of the firm’s highest-risk clients. They instructed Carpenter to “fix this situation to reduce the firm’s risk.”

### **The June 16, 2003 Meeting Regarding Reactivation Accounting**

24. After becoming the new engagement partner, Carpenter focused on reactivations as posing risk to E&Y. Carpenter conferred with other members of the audit team, but remained concerned with Bally’s reactivation accounting and had the view that Bally’s reactivation accounting was more aggressive than he was willing to accept and he was unwilling to sign off on the financial statements that included the reactivation accrual. Carpenter, Sever, Peterson and Vogelsinger planned a meeting with Bally to demand that the Company change its reactivation accounting.

25. In June 2003, Bally was in the midst of refinancing its debt. E&Y called a meeting for June 16, 2003 at Bally's offices. Bally was represented at that meeting by its senior officers. E&Y was represented at the meeting by Vogelsinger, Carpenter, Peterson, Sever, and Kiss. The presence of Vogelsinger, the managing partner of E&Y's Lake Michigan Area office, was unusual, as was the presence of Sever, who was in charge of all of E&Y’s Professional Practice Directors in the United States.

26. Vogelsinger began the meeting by stating that Bally had the most aggressive accounts receivable in E&Y's entire Lake Michigan Area.

27. At that same meeting, E&Y announced that it would not provide Bally with the comfort letter and consent that it needed to complete its debt refinance if Bally continued to recognize reactivation revenue the way it had in the past. Additionally, E&Y offered to permit Bally to write off the reactivation accrual over several quarters, a course of action which is clearly not in conformity with GAAP.

28. By participating in substantive aspects of the engagement, Vogelsinger knew or should have known that the reactivation accounting policy was not in conformity with GAAP; there would be no reason to withhold the comfort letter and consent if such policy was in conformity with GAAP even if it was aggressive; similarly, there would have been no reason to offer to allow Bally to violate GAAP by spreading the write off over several quarters.

29. As discussed above, Vogelsinger did not fulfill his obligation to exercise due care by not requiring the engagement team to take appropriate action concerning E&Y's 2002 and 2003 audits of Bally, despite: (1) having risk management responsibilities; (2) knowing that Bally was one of E&Y's riskiest 18 clients; (3) knowing that Bally's management employed "aggressive" accounting principles and estimates; and (4) knowing that Bally's reactivation revenue recognition policy was one of the issues that led to Bally's identification as one of E&Y's riskiest clients.

### **Findings**

Based on the foregoing, Vogelsinger engaged in improper professional conduct pursuant to Rules 102(e)(1)(ii) and 102(e)(1)(iv)(B)(2) of the Commission's Rules of Practice. Specifically, the Commission finds that Vogelsinger engaged in repeated instances of unreasonable conduct, each resulting in a violation of applicable professional standards that indicate a lack of competence to practice before the Commission.

### **IV.**

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Vogelsinger's Offer.

Accordingly, it is hereby ORDERED, effective immediately, that:

A. Vogelsinger is denied the privilege of appearing or practicing before the Commission as an accountant pursuant to Rule 102(e)(1)(ii) and Rule 102(e)(1)(iv)(B)(2).

B. After 9 months from the date of this order, Vogelsinger may request that the Commission consider his reinstatement by submitting an application (attention: Office of the Chief Accountant) to resume appearing or practicing before the Commission as:

1. a preparer or reviewer, or a person responsible for the preparation or review, of any public company's financial statements that are filed with the Commission. Such

an application must satisfy the Commission that Vogelsinger's work in his practice before the Commission will be reviewed either by the independent audit committee of the public company for which he works or in some other acceptable manner, as long as he practices before the Commission in this capacity; and/or

2. an independent accountant. Such an application must satisfy the Commission that:

(a) Vogelsinger, or the public accounting firm with which he is associated, is registered with the Public Company Accounting Oversight Board ("Board") in accordance with the Sarbanes-Oxley Act of 2002, and such registration continues to be effective;

(b) Vogelsinger, or the registered public accounting firm with which he is associated, has been inspected by the Board and that inspection did not identify any criticisms of or potential defects in Vogelsinger's or the firm's quality control system that would indicate that Vogelsinger will not receive appropriate supervision;

(c) Vogelsinger has resolved all disciplinary issues with the Board, and has complied with all terms and conditions of any sanctions imposed by the Board (other than reinstatement by the Commission); and

(d) Vogelsinger acknowledges his responsibility, as long as Vogelsinger appears or practices before the Commission as an independent accountant, to comply with all requirements of the Commission and the Board, including, but not limited to, all requirements relating to registration, inspections, concurring partner reviews and quality control standards.

C. The Commission will consider an application by Vogelsinger to resume appearing or practicing before the Commission provided that his state CPA license is current and he has resolved all other disciplinary issues with the applicable state boards of accountancy. However, if state licensure is dependent on reinstatement by the Commission, the Commission will consider an application on its other merits. The Commission's review may include consideration of, in addition to the matters referenced above, any other matters relating to Vogelsinger's character, integrity, professional conduct, or qualifications to appear or practice before the Commission.

By the Commission.

Elizabeth M. Murphy  
Secretary