UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION, Plaintiff, -against- WG TRADING INVESTORS, L.P., WG TRADING COMPANY LIMITED PARTNERSHIP, WESTRIDGE CAPITAL MANAGEMENT, INC., PAUL GREENWOOD, and STEPHEN WALSH, Defendants, ROBIN GREENWOOD and JANET WALSH, Relief Defendants.	No. 09 CV 1750 (GBD)
COMMODITY FUTURES TRADING COMMISSION, Plaintiff, -against- STEPHEN WALSH, PAUL GREENWOOD, WESTRIDGE CAPITAL MANAGEMENT, INC., WG TRADING INVESTORS, L.P., WGIA, LLC, Defendants, WESTRIDGE CAPITAL MANAGEMENT ENANCEMENT FUNDS, INC., WG TRADING COMPANY, L.P., WG LLC, K&L INVESTMENTS and JANET WALSH, Relief Defendants.	No. 09 CV 1749 (GBD)

QWEST ASSET MANAGEMENT CO. AND QWEST PENSION TRUST'S
PROPOSAL FOR DISTRIBUTION OF FUNDS HELD BY THE RECEIVER

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Pursuant to this Court's August 5, 2009 and September 11, 2009 orders and Robb Evan

& Associates LLC's (the "Receiver") September 1, 2010 notice, Qwest Asset Management

Company and the Qwest Pension Trust (collectively, "Qwest") respectfully submit this proposal

for distribution of funds held by the Receiver. In addition to this submission, Qwest also

provides the Receiver with the expert opinion of Dr. Thomajean Johnsen and joins with a group

of other investors in submitting the expert opinion of Peter Salomon, C.P.A.

QWEST'S PROPOSAL

Qwest proposes that the Receiver distribute the estate *pro rata* to all investors based on

each investor's net investment amount calculated in constant dollars to neutralize the effects of

inflation and to equalize the vast loss differences experienced between short and long-term

investors. This net investment approach treats all investors fairly and similarly, maximizes and

simplifies the Receiver's ability to recoup funds, and recognizes the impact of inflation on funds

over time—without giving any investor any fictitious profits or earnings, or even any real return

on its investment.

FACTUAL BACKGROUND ON QWEST'S INVESTMENT AND LOSS

The Qwest Pension Trust provides benefit funding for the Qwest Pension Plan. The

Qwest Pension Plan, in turn, provides retirement benefits for Qwest Communications

International Inc. ("QCII") employees. QCII is an international telecommunications company

that employs more than 30,000 people dedicated to providing innovative products and services.

Twenty-eight thousand employees are currently covered by the Qwest Pension Plan, and 63,000

retirees receive benefit payments from the Qwest Pension Plan. Telephone company retirees

across the United States rely on the Qwest Pension Plan to help fund their living expenses.

Qwest Asset Management Company ("QAM") is the investment fiduciary responsible for

managing the Qwest Pension Trust's investments. QAM's senior management team averages 25

years of investment experience and actively manages two QCII trusts, of which the Qwest

Pension Trust is the largest.

Qwest was introduced to defendants Westridge Capital Management Company

("Westridge Capital") and WG Trading Company ("WGTC," and collectively with Westridge

Capital and other entities controlled by Paul Greenwood and Stephen Walsh, "Westridge") in

1998. Over a two-year period, QAM conducted diligence on a potential investment with

Westridge. Qwest became a noteholder of WGQ, LLC—an entity created by defendants Paul

Greenwood and Stephen Walsh specifically for Qwest's Westridge investment—in 2000. Qwest

loaned money to WGQ at various times for WGQ to invest in WGTC. Qwest's promissory notes

provided that Qwest would receive interest in the same amount that would have been earned if

the loan proceeds were invested directly in WGTC limited partnership interests.

Qwest was a long-term investor in Westridge, making its first investment in 2000. Over

the next nine years, Qwest made several withdrawals and contributions, received monthly

account statements, and obtained funds when requested. After nine years of investment, Qwest

continued to have a substantial sum invested with Westridge. Because Qwest was a long-term

investors, if investors' contributions and withdrawals are not adjusted to constant dollars to

neutralize affects of inflation, Qwest stands to lose roughly 95% of its investment. To ensure the

fair and equitable treatment of all investors, therefore, the distribution plan must calculate each

investor's net investment in constant inflation-adjusted dollars.

SUPPORT FOR QWEST'S DISTRIBUTION PROPOSAL

The Receiver and Court have broad equitable authority to approve fair and reasonable

distribution plans as remedies for federal securities violations. *See S.E.C. v. Byers*, 637 F. Supp.

2d 166, 174 (S.D.N.Y. 2009). When distributing funds to victims of fraud, courts and receivers

should be guided by the maxim that "'equality is equity.'" *Id.* at 176 (quoting *Cunningham v. Brown,* 265 U.S. 1, 13 (1924)).

To achieve equity, all investors should be treated similarly irrespective of their investment structure and timing. Limited partners in WGTC should not be treated differently than note holders in WG Trading Investors, LP ("WGTI") or shareholders in the Westridge off-shore British Virgin Island investment funds. And long-term investors should be treated the same as recent investors. To accomplish this goal, the Receiver should determine each investor's claim by calculating each investor's net principal amount in constant dollars and then distribute the estate to all investors on a *pro rata* basis.

I.   A *pro rata* distribution plan is most equitable.

Pro rata distribution plans are "the most fair and most favored [plans] in receivership cases." *Byers,* 637 F. Supp. 2d at 176. In a *pro rata* distribution plan, each investor receives a portion of the estate equal to the percentage of the investor's claims measured against total claims, regardless of investment form. For example, if investor A's claim is 25% of the total claims against the estate, then investor A would receive 25% of the available estate.

Pro rata distribution is always proper when investor funds are commingled and victims are similarly situated to the defrauders. *See S.E.C. v. Credit Bancorp,* 290 F.3d 80, 88–89 (2d Cir. 2002). *Pro rata* distribution schemes are also "especially appropriate for fraud victims of a Ponzi scheme." *Id.* at 89. As detailed in the Receiver Reports[1] and Mr. Salomon's declaration, in this case investor funds were indisputably commingled, investors are similarly situated to the defrauders under the relevant criteria, and unbeknownst to investors, Westridge operated with

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[1] The "Receiver Reports" consist of the Report of Temporary Receiver's Activities for the Period from February 25, 2009 through May 22, 2009 (the "Receiver's First Report") and the Report of Receiver's Activities for the Period from May 25, 2009 through May 28, 2010 (the "Receiver's Second Report").

classic elements of a Ponzi scheme. A *pro rata* distribution plan is therefore appropriate, fair, and reasonable.

A.   The Westridge funds were commingled.

Because money is fungible, commingling of funds warrants treating all funds as tainted and supports distributing those funds on an equal, *pro rata* basis to all defrauded investors. *See Byers,* 637 F. Supp. 2d at 177. Any amount of commingling is sufficient to support a *pro rata* distribution scheme, even where that commingling is not "systematic." *Id.* at 178. Indeed, even where a party argues that certain funds are "not attributable to any illicit activity," a showing that the tainted funds were commingled with the allegedly untainted funds taints *all* funds. *Id.*

There is ample evidence of commingling here. The Receiver has conducted a lengthy and thorough investigation and has demonstrated that WGTC and WGTI commingled funds and operated with utter disregard for corporate governance. (*See* Receiver's First Report at 2, 13–17; Receiver's Second Report at 1–3.)

Peter Salomon, a managing director in Navigant Consulting, Inc.'s Disputes and Investigations Practice and a Certified Public Accountant with twenty years' forensic accounting experience, reached the same conclusion following a thorough review of the documents collected and provided by the Receiver. (*See* Declaration of Peter A. Salomon ("Salomon Decl.") at 7–13.) Mr. Salomon is eminently qualified for this type of analysis, as demonstrated by his past engagements. For example, Mr. Salomon has been appointed an accounting Referee or Special Master by courts on four occasions, has been retained by the SEC as an expert witness, and has assisted a number of public companies, audit committees, and individuals under investigation by the SEC with their own investigations. (*Id.* at 3–4.) Mr. Salomon and his associates have reviewed the Receiver's reports and thousands of pages of documents related to Westridge accounting and bookkeeping that the Receiver has provided. (*Id.* at 6–7.) After a detailed

review, Mr. Salomon concludes that: there was significant commingling of investor funds between WGTC and WGTI and neither WGTI nor WGTC could survive without financial support or funds from the other entity at various points in time. (*See* Receiver's Second Report at 3; Salomon Decl. at 7.)

As the Receiver has explained and Mr. Salomon has confirmed, this commingling was extensive and pervasive. (*See generally* Receiver's First and Second Reports; Salomon Decl. at 7–13.) For example:

- WGTC received payments from WGTI investors when there was no valid business purpose for these payments (*see* Salomon Decl. at 9, 13);

- WGTI paid WGTC limited partner investors directly on many occasions when there was no valid business purpose for these payments (*id.* at 11–12);

- WGTC improperly accounted for losses in its Signal investment and employee advances as reductions in WGTI's capital (*id.* at 22–23); and

- WGTC advanced and received margin payments on behalf of WGTI investors (*id.* at 13).

Indeed, WGTC treated WGTI's capital account as a piggy bank rather than a true limited partnership interest, simply giving any losses or remaining incoming to WGTI each month. (*See* Receiver's First Report at 9–10; Salomon Decl. at 22.) In at least 100 months, this resulted in negative monthly earnings for WGTI. (Salomon Decl. at 22.) Assigning remaining or negative earnings to WGTI was the only way WGTC was able to maintain the capital accounts of the limited partners. (*See, e.g., id.* at 21–22.)

Qwest understands that investors who purchased limited partnership interests directly from WGTC (the "limited partners") will argue that any commingling of funds between WGTC and WGTI was limited, traceable, and easily unwound so as to allow investors in separate entities to recoup funds allegedly attributable to that entity. For example, the limited partners have argued in the past that they are entitled to the first $550 million of the $800 million estate

because there was limited commingling between WGTC and WGTI and the limited partner

capital accounts were intact at the time of the asset freeze. (*See* Joint Submission of Information

by Seven WG Trading Company, L.P. Limited Partners, at 2, 4–5, *S.E.C. v. WG Trading*

Investors, L.P. et al., C.F.T.C. v. Stephen Walsh, et al. (S.D.N.Y. filed June 1, 2009) (Dkt. No.

118) (hereinafter "LP Submission").) In essence, this would provide fewer than 10 investors

with a full recovery of their final account statement balances—including their fictitious, inflated

earnings—and leave the remaining 25 or so investors with pennies on the dollar.

The limited partners' argument is directly contradicted by the findings made by the

Receiver and the evidence. WGTC and WGTI had a "long history . . . of commingling funds"

and were "financially inseparable." (Receiver's Second Report at 1.) Any impression that

limited partner accounts were "intact" at the time of the asset freeze and that the amount of these

accounts represented a true accounting of limited partner investments in WGTC is belied by the

forensic accounting analysis of both the Receiver and Mr. Salomon. This analysis shows that

WGTC treated its limited partner WGTI differently than all other limited partners, repeatedly

shortchanging WGTI to preserve the fiction that other limited partners were receiving earnings at

the rates created by Greenwood.

Qwest also understands that the limited partners have hired an accounting firm to

recreate the books and records of WGTI and WGTC for the last dozen or more years and to

opine that the commingling of funds can be unwound to show what might have happened to all

investors but for the defendants' fraud or commingling. This exercise, however, misses the

point. The question is whether there was commingling, not whether that commingling can be

untangled. *See Byers,* 637 F. Supp. 2d at 178; *Bancorp,* 290 F.3d at 88–89. Likewise, even if

there were some limited ability to trace an individual investor's funds or funds invested with a

particular Westridge entity, a tracing analysis "has been almost universally rejected by courts as inequitable." *Byers,* 637 F. Supp. 2d at 177. This is because the ability to trace any particular investor's assets "is a result of the merely fortuitous fact that the defrauders spent the money of the other victims first." *Credit Bancorp.,* 290 F.3d at 89. Regardless of any investor's or accountant's attempts to untangle the Greenwood-Walsh fraud or to trace funds to a particular contribution or withdrawal, the Receiver's detailed evidence of commingling here supports a *pro rata* distribution plan that treats all investors equally.

B. All investors were similarly situated to the defrauders.

A *pro rata* distribution plan is also appropriate when investors are similarly situated to the defrauders. *See Credit Bancorp,* 290 F.3d at 89; *Byers,* 637 F. Supp. 2d at 177. Investors are similarly situated when there is a "'reasonably close resemblance of facts and circumstances.'" *Byers,* 637 F. Supp. 2d at 180 (quoting *Lizardo v. Denny's, Inc.,* 270 F.3d 94, 101 (2d Cir. 2001)). Investors' circumstances need not be identical to fulfill this requirement. *Id.* The evidence shows that all Westridge investors are similarly situated.

Byers provides a detailed analysis of the "similarly situated" test. The court held that distributing funds *pro rata* among real estate fund, commodity fund, and diamond investors was fair, reasonable, and appropriate. 637 F. Supp. 2d at 169–71, 178–81. Despite the different funds and investments, investors were similarly situated to the defrauders because: i) the role played by the defrauders in managing the entities in exchange for fees was common to all investments; ii) the offering materials for all investors stated that all investments had a high level of risk; iii) the offering materials for all investors highlighted the management and investment roles of certain personnel; iv) cash from the various entities was pooled for operating expenses and distributions; and v) the offerings were backed by guarantees. *Id.* at 180.

The Receiver and Mr. Salomon have shown that under a *Byers* analysis, all Westridge investors are similarly situated to the defrauders, Greenwood and Walsh.

- First, Greenwood and Walsh played the same role vis-à-vis each investor in the fraud. They formed and controlled WGTC, WGTI, WGQ, and Westridge Capital. Through Westridge, Greenwood and Walsh marketed and sold limited partnership interests, fund shares, and promissory notes. (*See* Salomon Decl. at 14–15.)

- Second, all investors received the same marketing materials. (*See* Receiver's First Report at 4–5; Salomon Decl. at 15.) These materials represented that every contribution was, regardless of investment form, ultimately invested in WGTC for index arbitrage. They also showed that all investors received the same rate of return regardless of the method of investment and that all investors benefitted from the protections provided by the same comprehensive regulatory oversight. (*See* REA 177858; Salomon Decl. at 15.) There is no suggestion that investors would be treated or situated differently based on their choice of investment structure.

- Third, the offering materials highlighted the roles played by Greenwood and Walsh and other senior personnel, regardless of investment form. (*See* Salomon Decl. at 15.)

- Fourth, the receivership documents reveal that the accounting and internal controls for both WGTC and WGTI were performed by the same employee. (Receiver's Second Report at 1; Salomon Decl. at 15.) Indeed, WGTC and WGTI "had to be operated as a single entity to support the myth that they were stand-alone entities." (Receiver's Second Report at 1.)

As in *Byers,* any argument that WGTC investors are not similarly situated to WGTI investors because WGTC allegedly was not engaged in fraud, was less risky, or produced "legitimate" returns must also be rejected here. In *Byers,* the commodity fund investors argued that they were not similarly situated to the real estate fund investors because the commodity fund investors exercised more control over their investments and the entity that controlled their investments was not part of the fraud. *See Byers*, 637 F. Supp. 2d at 180–81. The court rejected this argument because the defrauders had transferred money between the various funds, "exercised control over the Commodity Funds and . . . used the [Commodity] Funds as part of one overarching scheme to defraud investors." *Id.*

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Greenwood and Walsh operated similarly, transferring money between Westridge investors, WGTI, and WGTC. (*See* Salomon Decl. at 16.) Also like *Byers,* Greenwood and Walsh exercised control over all investors' funds through their positions as managers and managing partners of the various Westridge entities. (*See, e.g.,* Receiver's First Report at 5–6 (85% of an investor's funds were to be invested in index arbitrage with WGTC regardless of investment form).) Once an investor's funds were allegedly invested in the index arbitrage strategy, Westridge personnel, not investors, controlled the selection, timing, and execution of the index arbitrage trades. (*See, e.g.*, *id.* at 7.)

Other arguments that the WGTC limited partners are not similarly situated are likewise unsupported by the evidence. For example, the limited partners might argue that they had greater rights to receive corporate documents under Delaware law, but as the Receiver is well aware other investors had contractual rights to those same documents. (*See, e.g.*, REA 044784–85.) Greenwood and Walsh stood in the same relationship with *every* investor. Investors are similarly situated to the defrauders and a *pro rata* distribution plan is appropriate here.

C.   *Pro rata* distribution plans are particularly appropriate in Ponzi schemes, and the Westridge scheme has elements of a classic Ponzi scheme.

The Receiver has characterized Greenwood's and Walsh's actions as fraud with classic Ponzi scheme elements. (*See* Receiver's First Report at 24; Receiver's Second Report at 1, 18–20.) Mr. Salomon has likewise determined that Greenwood and Walsh operated WGTC, WGTI, and related entities as a Ponzi scheme. (Salomon Decl. at 16–21.) In Ponzi-type schemes, a *pro-rata* distribution plan is "especially appropriate." *Credit Bancorp,* 290 F. 3d at 89.

The limited partners have at times attempted to characterize WGTC as a legitimate business enterprise that produced legitimate returns and therefore was not engaged in a Ponzi scheme. The limited partners are wrong. Even if Westridge did generate investment returns

through some genuine index arbitrage trading, that does not mean that WGTC was a legitimate

business enterprise that should be carved out from the estate. Ponzi schemes often involve *some*

amount of legitimate investment.[2] The Receiver's investigation has demonstrated, and Mr.

Salomon has confirmed, that funds from later WGTI or WGTC investors were utilized to pay

earlier WGTC or WGTI investors. (*See, e.g.*, Receiver's Second Report at 19–20; Salomon

Decl. at 19–20 (WGTC actual earnings were $300 million less than purported earnings, not

including $400 million in earnings that should have been allocated to note holders).) That means

Greenwood and Walsh operated WGTC and WGTI as a Ponzi scheme, and a *pro rata*

distribution is appropriate.

D.   The limited partner investment structure did not carry lower risk, and any differences in investment form are immaterial to the distribution scheme.

The limited partners have also argued that there was a lower risk of fraud at WGTC

because it was a regulated and audited entity, while WGTI was not. They claim that these audits

and regulations were the reason that the limited partners chose to invest directly with WGTC and

therefore the limited partners should be treated more favorably than other investors—even

though Greenwood and Walsh's fraud went undetected by regulators and auditors for more than

a decade. (*See* LP Submission at 9.) The evidence does not support the limited partners.

As detailed above, all investors received the same marketing materials, and those

materials represented that all Westridge entities and investors were protected by the regulations

governing, and audits of, WGTC. (*See, e.g.*, REA 177858.) Indeed, Westridge explained that it

offered different forms of investment because of the tax considerations that potentially impacted

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[2] Indeed, Charles Ponzi himself invested some of his investors' assets in mail coupons as advertised. *See* Ponzi Schemes, Frequently Asked Questions, http://www.sec.gov/answers/ponzi.htm#PonziName (last visited October 13, 2010). In *Byers*, the defrauders used investor funds to "actually . . . buy specific pieces of property" in some instances, 637 F. Supp. 2d at 169, and to make "real trades with real assets" and real returns, *id.* at 170. Despite these real investments and returns, the court characterized the action as a Ponzi scheme. *See id.* at 173.

different types of investors. The fact that different investors chose different investment forms for

tax reasons or other independent reasons has no relation to whether investors were defrauded.

All investors were victims here, and all investors should receive a distribution on a *pro rata*

basis.

Furthermore, any investor that chose WGTC over WGTI because it was concerned that

Westridge might be engaged in fraud should not have invested in the first place. Indeed,

investors with knowledge of fraud may be subject to clawback actions for their principal. *See,*

e.g., In re Bayou Group, LLC, 2010 WL 3839277, at *18–20 (S.D.N.Y. Sept. 17, 2010) (noting

in bankruptcy context that where transferee was on notice of debtor's fraud or insolvency, it must

demonstrate it undertook diligent inquiry to establish good-faith defense to protect its principal

investment); *In re World Vision Ent., Inc.* 275 BR 641, 658 (M.D. Fla. 2002) (good faith

standard under Florida UFTA requires transferee to show that it had no actual or imputed

knowledge of fraud); *In re Jacobs,* 394 BR 646, 659 (Bankr. E.D.N.Y. 2008) (New York UFCA

offers protection only to an innocent purchaser's principal). If the limited partners chose to

invest through WGTC rather than WGTI because they were concerned that Greenwood and

Walsh were engaged in fraud, they should make that evidentiary showing and other investors and

regulatory agencies can evaluate the limited partners' possible acquiescence in this fraud.

II.   Calculating investor's net principal in constant dollars treats all investors equally.

In order to treat investors equally, any distribution plan should recognize that a dollar in

2000 was worth more than a dollar in 2009. (Declaration of Dr. Thomajean Johnsen ("Johnsen

Decl." ¶¶ 5–6, 22.) The Westridge fraud has been ongoing since 1996. Some victims began

investing in 1996, while others did not make investments until 2008. (*See* Receiver's First Report

at 2, 8; Receiver's Second Report at 3.) Dr. Thomajean Johnsen, Associate Professor at the

Reiman School of Finance at University of Denver and an authority on risk/volatility in equity

portfolios, portfolio management, and risk assessment has reviewed the Receiver's First and

Second Reports and has determined that early and late investors would be treated inequitably if

their net principal investment is not calculated in constant dollars to neutralize the impact of

inflation. (Johnsen Decl. ¶¶ 1, 5–6, 22.)

Acknowledging inflation when calculating investors' net investments does not provide

investors with illusory profits or fictitious earnings. In fact, as finance-expert Dr. Johnsen put it:

"compensation at an acceptable rate of inflation would return investors to their original position

in terms of their purchasing power, *without giving them any real rate of return*." (*Id.* ¶ 24

(emphasis added).) An inflation adjustment—which is standard practice in financial analysis—

simply equalizes the numbers across investors. (*See id.* ¶¶ 11, 22.) It therefore achieves the

underlying goal of the receivership proceeding: equity through equality.

A.   **The law recognizes that a dollar in 2000 is worth more than a dollar in 2009.**

1.   *Federal and state laws recognize the time value of money.*

Many areas of the law recognize that a dollar in 2009 is worth less than a dollar in 2000.

For example, a standard rate of pre- and post-judgment interest is applied to any judgment in

recognition of the fact that when a party is deprived of the use of his money, he is also deprived

of the value he could have gained from the use of his money. As one Second Circuit court

explained, an "award of prejudgment interest is . . . compensatory, and is customary in cases

involving a breach of fiduciary duties. [Plaintiff] has not had the use of the principal sum in the

nine years since [defendant] defrauded him . . . . In view of the high inflation rates that beset this

period, a damage award without prejudgment interest (or, indeed, even one that does include it)

would not give [Plaintiff] full compensation for the losses he suffered at the hands of his

fiduciary." *Rolf v. Blyth, Eastman Dillon & Co.*, 637 F.2d 77, 87 (2d Cir. 1980).

Though equity receiverships do not typically compensate victims for pre- or post-judgment interest, receivers obtain it in their clawback-claims against over-withdrawn investors. *See, e.g.*, *Donnell v. Kowell,* 533 F.3d 762, 772 (9th Cir. 2008). In these situations, courts recognize that such interest "is simply an ingredient of full compensation that corrects judgments for the time value of money." *Id.*

Tax law also recognizes the principle that a dollar in 2009 is not equal to a dollar in 2000 by adjusting tax brackets to avoid inflation-induced increases in tax rates. *See, e.g.,* Press Release, 2009 Inflation Adjustments Widen Tax Brackets and Expand Tax Benefits, http://www.irs.gov/newsroom/article/0,,id=187825,00.html (last visited Oct. 16, 2008). Social Security benefits and federal and state employee salaries are likewise adjusted for inflation through cost of living increases. *See, e.g.,* Latest Cost-of-Living Adjustment, http://www.ssa.gov/OACT/COLA/latestCOLA.html (last visited October 13, 2010). It would be unreasonable not to recognize that inflation has also affected Westridge investors.

> 2.   *The government has acknowledged the use of constant dollars to distribute funds in Ponzi-like cases.*

Recently in the *Bernard Madoff* litigation the SEC has advocated accounting for inflation by adjusting to constant dollars because it is a more equitable approach to distributing funds to defrauded investors under the Securities Investor Protection Act ("SIPA"). The SEC recognized that this area of Ponzi-scheme law has received little attention, but speculated that this may be because "many Ponzi-type schemes are of relatively short duration, and the inequity among those who invested at different points in time is less striking." Hearing before the Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises of the House Committee on Financial Services, 111th Cong., 2009 WL 4647561, at *9 (Dec. 9, 2009) (statement of Michael A. Conley, Deputy Solicitor, U.S. Securities and Exchange Commission) (hereinafter "SEC

Hearing Statement"). When a fraud is long-term, ignoring inflation creates inequity in the valuation of short- and long-term investor funds.

The SEC's recent distribution proposal in *Madoff* makes this point clear. There the government has proposed valuing claims on a cash-in/cash-out—or net investment—basis calculated in "constant dollars to account for the effects of inflation (or deflation)." Memorandum of Law of the Securities and Exchange Commission Supporting Trustee's Determination that Net Equity Should Not Be Based on Securities Positions Listed on Last Statements, and Supporting in Part Trustee's Determination that Net Equity Should Be Based Upon Amounts Deposited Less Amounts Withdrawn, *In re Bernard L. Madoff Invest Secs. LLC*, No. 08-1789 (Bankr. S.D.N.Y. Dec. 11, 2009) (Dkt. No. 1052) ("SEC Brief") at 1. The SEC advocated such an approach in *Madoff* because it recognizes "the economic reality that a dollar invested in 2008 has a different value than a dollar invested twenty years earlier." *Id.*

In testimony before the House Committee on Financial Services, the SEC explained its recommendation in *Madoff* more fully. *See generally* SEC Hearing Statement. There the SEC noted that an account balance valuation "favors earlier customers at the expense of later customers," while an unadjusted net investment approach "favors later customers at the expense of earlier customers by treating a dollar invested in 1987 as having the same value as a dollar invested in 2007." SEC Hearing Statement at *9. The SEC determined that valuing investments in time-equivalent or constant dollars was the best way to "achieve a fair and economically accurate allocation among Madoff customers who invested and withdrew funds in different historical periods." *Id.*

The SEC distinguished SIPA cases from Ponzi-scheme cases in its briefing and in a recent letter to the Receiver. *See* SEC Brief at 10 (noting that some Ponzi scheme cases indicate

that claims should be valued on a pure net investment basis); Letter from Thomas P. Smith, U.S.

Securities and Exchange Commission, to Brick Kane, Robb Evans & Associates, LLC (Oct. 15,

2010). But SIPA does not mandate the SEC's proposal in the *Madoff* litigation; it was

appropriate there because the long-term nature of the fraud meant not adjusting for inflation

would be inequitable to long-term investors. The same is true here.

Typical Ponzi schemes are of relatively short duration and do not have enough funds to

return significant portions of victims' investment. *See, e.g.,* SEC Hearing Statement, at *9. In

contrast, the Westridge fraud took place over at least 13 years (*see* Receiver's First Report at 1),

and the Receiver has significant funds to return to investors—indeed, the receivership *already*

holds more than $850 million in cash and assets for sale (*see* Receiver's First Report at 2).

Through clawback actions, the value of the estate will likely grow to exceed the value of

unadjusted principal claims. The substantial available funds means that all investors stand to

receive a significant distribution under *either* a constant dollars approach or an unadjusted

principal approach.

B.   **Normalizing contributions and withdrawals to constant dollars achieves an equitable result in theory.**

It is a fundamental economic principle that a dollar in 2000 was worth more than a dollar

in 2009. (Johnsen Decl. ¶ 5.) This is because someone who had a dollar in 2000 could have

invested that dollar to generate returns until he received a dollar in 2009. (*Id.*) Meanwhile,

inflation has eroded the purchasing power of the 2000 dollar, so that it purchases much less in

2009. (*Id.*) As a result, it is inequitable to treat dollars invested ten or 15 years ago equally with

dollars invested a year or two ago. (*Id.* ¶ 22.) Based on years of experience and training, Dr.

Johnsen concludes that distributing funds here on a net investment basis without normalizing for

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the impact of inflation would be inequitable because it would treat recent investors more

favorably than earlier investors. (*Id.*)

Dr. Johnsen concludes that adjusting withdrawals and contributions to constant dollars by

applying the Consumer Price Index ("CPI") to each investor's net principal investment is a

conservative and reasonable way to normalize investments for inflation and return investors to

their original position in terms of purchasing power. (*Id.* ¶¶ 22, 27.) The CPI is a measure of the

average change over time in prices paid by urban consumers for a market basket of goods, and is

the most widely used measure of inflation. (*Id.* ¶ 25.) Calculating investors' net investment in

this way treats early and late investors more fairly and is more equitable than distributing funds

on an unadjusted net principal basis. (*Id.* ¶¶ 22, 27.) Overall, calculating net principal in

constant dollars according to the CPI will result in a distribution to each investor that is

equitable, fair, and reasonable.

C. Normalizing contributions and withdrawals to constant dollars achieves an equitable result in practice.

Qwest is not the only investor who suffers an unfair loss if net investments are not

adjusted for inflation. According to various calculations, eleven out of twenty-five investors

achieve a better outcome than they would on a pure net investment basis.[3] Two investors have

an essentially equal outcome under an unadjusted-net investment or an adjusted-net investment

approach.

Comparing potential recoveries to statement value—which is, of course, how the

charitable organizations and pension funds that invested in Westridge carried the investment on

their books—highlights the unfairness in not adjusting figures for inflation. For example, an

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[3] For these purposes multiple investments by related entities are considered separately, Fund A is
treated as one entity, and James Carder's investment is not considered.

unadjusted principal distribution of $800 million would provide the Qwest pension fund with roughly 6% of its statement value, while a more recent investor like the Iowa pension fund would receive approximately 85% of its statement value. This does not treat similarly situated investors equally. In contrast, a distribution based on contributions and withdrawals adjusted for inflation would still provide the Iowa pension fund with approximately 75% of its statement value, yet give Qwest a more reasonable yield of roughly 40% of its statement value. Another long-term investor, the collective 3M entities, would obtain only approximately 17% of its statement value on an $800 million net-cash distribution and a more reasonable 40% of its statement value if figures are adjusted for inflation. A distribution scheme that requires one investor to record a 94% or 83% loss while another investor records only a 15% loss is not equitable—particularly when an equally acceptable alternative requires no investor to take more than a 60% loss.

> D. **Giving effect to inflation simplifies and maximizes recovery.**

Adjusting for constant dollars simplifies the Receiver's ability to collect funds. The Receiver is charged with maximizing the estate by pursuing suitable clawback litigation. (*See* Preliminary Injunction and Order Freezing Assets and Granting Other Relief Against Relief Defendants, at 7–9, S.*E.C. v. WG Trading Investors, L.P. et al.*, *C.F.T.C. v. Stephen Walsh, et al.* (S.D.N.Y. filed May 22, 2009) (Dkt. No. 100).) Given the assets currently in the estate and the availability of clawback actions against other investors, the Receiver has a realistic opportunity to recover more than the unadjusted net principal of all current investors. But limiting a distribution plan to unadjusted net principal inhibits the Receiver's ability to argue that the estate should be allowed to recoup funds in clawback actions once all unadjusted net principal claims have been satisfied. The clawback defendants would claim that any recovery from them would constitute gains for the current investors. But if the Receiver recognizes the

undisputed principle that inflation erodes purchasing power for both current and cashed-out

investors, the clawback defendants would not have this defense. And all investors—both current

and fully-withdrawn—would be better off.

In contrast, accounting for inflation increases the value of current-investor claims and

provides the Receiver with a reasoned basis to seek approval of settlements with clawback

targets. If current investors' net investments are measured in constant dollars, the Receiver can

reach the same agreement with fully withdrawn investors, and the Court would be able to

approve such settlements as reasonable. Implementing a distribution plan that accounts for

inflation by adjusting all funds to constant dollars therefore maximizes and simplifies the

Receiver's ability to increase the estate and return funds equitably to *all* victims.

III.   A rising tide approach to distribution does not treat investors equally and is inappropriate here.

Some investors have proposed a rising-tide distribution plan.[4] But a rising tide

distribution would give many investors no distribution at all—hardly a fair or equitable

approach.

Distributions under a rising-tide approach are calculated by subtracting 100% of an

investor's withdrawals from a *pro rata* portion of an investor's contributions. For example,

depending on the size of the estate, 100% of an investor's withdrawals could be subtracted from

70% of that investor's contributions. This approach can mean that victims who made

withdrawals over the life of the investment will receive no distribution. Because some victims

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[4] Interestingly, Fund A investors have suggested a rising-tide distribution, even though it leads to far less recovery for them than a net investment approach. This is because Fund A fails to acknowledge that under a rising tide theory it needs to be treated like the single investment fund it is. *See, e.g., C.F.T.C. v. Equity Fin. Group, Inc.*, 2005 WL 2143975, at *15, *26–27 (D.N.J. Sept. 2, 2005). That means that *all* of its contributions and withdrawals would be counted, not just those of current investors.

receive nothing under such an approach, courts have held that a rising tide approach is less

equitable than a *pro rata* approach. *See, e.g., Byers,* 637 F. Supp. 2d at 182.

A simple example illustrates the inequity of this approach. Assume investor A made a

$150 investment but later withdrew $50, and investor B made an investment at the same time of

$100 and never withdrew anything. If the estate consists of $30, both investors receive 32% of

their contributions minus 100% of their withdrawals. This leaves investor A with no distribution

while investor B receives all $30. This is the case even though both investors have lost the same

$100 principal. Under a *pro rata* net-investment plan, however, each investor would get $15.

See, e.g., Byers, 637 F. Supp. 2d at 182.[5]

Furthermore, a rising tide approach is inappropriate here because Westridge's

bookkeeping is unreliable. This means that the Receiver's calculations of some investors'

contributions and withdrawals are inaccurate, even if the net number is correct. For example,

using Westridge's books, the Receiver calculated that Qwest contributed $766 million and

withdrew $728 million. This is incorrect, though Qwest and the Receiver agree on Qwest's final

account balance and unadjusted net principal amount. Qwest's counsel believes that other

investors may face similar accounting inaccuracies. Such inaccuracies have no effect on a

distribution plan based on adjusted net principal but have significant effect on a distribution plan

that requires investors to subtract 100% of inaccurate withdrawals from some as yet

undetermined percentage of inaccurate contributions.

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[5] One justification for a rising tide distribution is that it does not penalize investors based on the timing of their investment—*i.e.*, it recognizes the time value of money. *See, e.g., Equity Fin. Group*, 2005 WL 2143975, at *25. Qwest agrees that a distribution should recognize the time value of money—*i.e.*, recognize that recent investors had the value of their money for several years while the long-term investors did not.

CONCLUSION

A *pro rata* distribution plan that accounts for inflation by applying the CPI to each

investor's contributions and withdrawals is an equitable plan that maximizes and simplifies the

Receiver's ability to recover funds for the estate. Qwest respectfully requests that the Receiver

implement Qwest's proposed distribution plan.

Date: October 22, 2010

Respectfully submitted:

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/s/Abby F. Rudzin

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Qwest Asset Management Company and
Qwest Pension Trust

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION, Plaintiff, -against- WG TRADING INVESTORS, L.P., WG TRADING COMPANY LIMITED PARTNERSHIP, WESTRIDGE CAPITAL MANAGEMENT, INC., PAUL GREENWOOD, and STEPHEN WALSH, Defendants, ROBIN GREENWOOD and JANET WALSH, Relief Defendants.	No. 09 CV 1750 (GBD)
COMMODITY FUTURES TRADING COMMISSION, Plaintiff, -against- STEPHEN WALSH, PAUL GREENWOOD, WESTRIDGE CAPITAL MANAGEMENT, INC., WG TRADING INVESTORS, L.P., WGIA, LLC, Defendants, WESTRIDGE CAPITAL MANAGEMENT ENANCEMENT FUNDS, INC., WG TRADING COMPANY, L.P., WG LLC, K&L INVESTMENTS and JANET WALSH, Relief Defendants.	No. 09 CV 1749 (GBD)

**DECLARATION OF THOMAJEAN JOHNSEN, PH.D.,
IN SUPPORT OF QWEST ASSET MANAGEMENT CO. AND QWEST PENSION
TRUST'S PROPOSAL FOR DISTRIBUTION OF FUNDS HELD BY THE RECEIVER**

I, THOMAJEAN JOHNSEN, hereby declare:

QUALIFICATIONS

1.   I am an Associate Professor at the Reiman School of Finance at the University of Denver, from which I received my MBA in 1983. I have recently been appointed as the Co-Chair at the Reiman School with a 4 year term to begin in July 2011. I have a Ph.D. from the University of Colorado, and my consulting firm, Portfolio Research Solutions, has been a Registered Investment Advisor in the state of Colorado since 1999. I teach in the areas of capital markets; portfolio management and performance analysis; financial applications of econometrics; and quantitative models of security selection. My research focus and expertise include the sources of risk/volatility in equity portfolios; portfolio management and risk assessment. I have written twenty-three articles on these and related topics. I am a member of the Financial Management Association and regularly attend academic and practitioner research conferences. My curriculum vitae is attached as Exhibit A to this declaration.

2.   I am being compensated at $250 an hour for my work on this matter. My compensation is not contingent upon the opinions that I render or the outcome of the litigation.

3.   Attached as Exhibit B is a list of the materials I considered in reaching the opinions expressed in this report.

ASSIGNMENT

4.   I have been retained by Qwest Asset Management, Co. and the Qwest Pension Trust to offer expert testimony regarding what would be an equitable distribution plan for investors in the Westridge entities fraudulently operated by Paul Greenwood and Stephen Walsh.

STATEMENT OF OPINION

5.   It is a fundamental economic and financial principle that there is a time value associated with money. The concept of the time value of money holds that a dollar received

today can be reinvested immediately to generate additional dollars. At the same time, inflation operates to weaken the purchasing power of that dollar in the future. These combined forces make today's dollar more valuable than a dollar received in a future period. In finance, this principle means that there is always a preference for early money over deferred money.

6.   It is my opinion that funds invested over time in Westridge entities cannot be equitably valued and compared unless the funds are adjusted to constant dollars by applying the Consumer Price Index (the "CPI"). Using the CPI to adjust investors' net principal to constant dollars reduces the difference between the much greater losses that long-term investors have suffered relative to more recent investors. It is the most equitable approach here.

BASES FOR OPINION

The Theoretical Basis for the Time Value Concept

7.   In 1907, Irving Fisher published *The Rate of Interest* (which was revised in 1930 under the title *The Theory of Interest*), which presents the classic economic treatment of the time value of money. In the well-known Fisher equation, the time value of money is expressed as a nominal rate of return or interest and used in time value calculations. The nominal rate of return or interest is the sum of the real rate of return plus an expected inflation premium. In this way, the nominal rate of interest both reflects the growth rate of money and compensates investors for the loss of purchasing power. As a result, both the real rate of return and the inflation rate have an additive effect on the rates included in time value calculations.

8.   The Fisher equation shows that the concept of inflation is central to the calculation of the time value of money. Inflation is generally considered to be caused by an increase in the volume of available money in relation to available goods and services. As the money supply increases within the economy and the availability of goods remains constant or declines, the inflation rate increases. All other factors held equal, without an inflation

adjustment to income, one's purchasing power will decrease. In an economic environment where inflation has not been zero, the result is that a dollar today purchases less than a dollar did in the past. From the investor's point of view, an investment should return a rate sufficient to compensate the investor for loss of purchasing power over the life of the investment.

9.   For example, in 2000 the inflation (CPI) rate was 1.746% and by the end of 2009 it was 2.172%. The average inflation rate over this 10-year period was 1.952%. Thus, while at the beginning of 2000 one gallon of milk cost approximately $2.88, today in 2010 it would cost approximately $3.50.[1] The U.S. government acknowledges inflation by providing judges and other federal employees cost of living pay increases. *See, e.g.,* Memorandum from John Berry, Director of the United States Office of Personnel Management (Dec. 23, 2009) (available at http://www.chcoc.gov/Transmittals/TransmittalDetails.aspx?TransmittalID=2653); Press Release, Administrative Office of the U.S. Courts, Federal Judges' Treatment By Congress Called Unfair (Dec. 12, 2008) (available at http://www.uscourts.gov/news/NewsView/08-12-12/Federal_Judges_Treatment_By_Congress_Called_Unfair.aspx) (explaining that lack of 2009 cost of living adjustment for federal judges was "starkly unfair"). Many corporations and colleges and universities, as well as other employers, do the same.

10.   If one assumes that a real rate of return is zero, then the Fisher equation provides that the time value of money should be calculated at a nominal rate equal to inflation in order to preserve purchasing power. To do this, money should be adjusted into constant dollars of a selected year.

11.   Adjusting to constant dollars is standard practice in economic studies or financial analyses. This is done because it is often useful to cast valuation problems in terms of the same

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[1] Of course, other market forces also affect the price of goods.

kind of dollars, thus eliminating the influence of inflation. Constant dollars are generally defined

relative to a given reference year. These constant dollars are the dollars that continue to have the

same purchasing power as the dollars in the reference year.

12.   An investment analysis may be carried out in real or nominal terms. Whether an

analyst chooses to evaluate an investment in real or nominal terms, she must be consistent in her

treatment of the cash flows and rates of return. Investment cash flow forecasts in nominal terms

must be adjusted with a nominal rate in time-value calculations. Likewise, cash flow forecasts in

real terms must be adjusted with a real rate.

The Concept of the Time Value of Money Is Well-rooted in History and Serves as a Bedrock Finance Principle.

13.   The concept of the time value of money has been recognized for more than eight

hundred years. Mathematician Leonardo Fibonacci developed the concept in 1202, though some

believe it was recognized long before that by the Arabs or the Indians. *See A History of the*

Theory of Investments: My Annotated Bibliography, by Mark Rubenstein.

14.   Today, the time value of money is a fundamental principle of graduate and

undergraduate finance curriculums as well as the curriculum for the Certified Financial Analyst

Institute. For example, all corporate and investment finance textbooks explain and apply the

concept. Examples of such finance textbooks are *The Theory of Finance*, by Fama and Miller;

Investments and *Essentials of Investments,* by Bodie, Kane, and Marcus; *Intermediate Corporate*

Finance, by Brigham and Daves; *Contemporary Financial Management,* by Moyer, McGuigan

and Kretlow; *Financial Markets and Institutions*, by Madura; *Fixed Income Mathematics*, by

Fabozzi, *International Financial Management,* by Eun and Resnik; and *Fundamentals of Futures*

and Option Markets, by Hull, among others.

15.   The application of the concept of the time value of money is widespread. Individuals regularly take the time value of money into account when determining the desirability of investing in the capital markets, in determining mortgage payments, or evaluating various consumer-related financial contracts. Investment managers utilize time-value-of-money calculations to determine the economic or intrinsic value of equity securities when selecting securities to include in actively managed portfolios and to calculate the yield to maturity on bond securities. Portfolio managers use time-value concepts to measure portfolio returns and to evaluate the performance of mutual funds, hedge funds, and other investment vehicles. Corporations utilize the time value of money in making capital budgeting decisions by calculating the net present value or internal rate of return for various plant, property, and equipment purchases. Corporations also take the time value of money into account when making decisions to issue commercial paper for their short term funding needs or to purchase the commercial paper of other corporations in order to earn a return that is both short term and of high credit quality. Investment banks and analysts working in the area of mergers and acquisitions utilize the concept to value potential takeover companies. Even state lotteries apply the time value of money, recognizing that a full payment to winners over many years is equal to (or in some cases less than) a discounted immediate payment.

16.   A simple example demonstrates the concept of the time value of money. If I deposited $100 in a savings account earning 3% annually ten years ago, it would be worth approximately $134.39 today. If the $100 had been invested in a slightly more risky investment such as a money market account earning 5% annually, it would be worth approximately $162.89 today. And since the S&P 500 has appreciated at 8.79% annually between January 1990 and

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December 2009, if I had invested $100 in January 1990 in an index fund that tracked the S&P 500, that investment would be worth $539.24 at the end of December 2009.

17.   A look at an historical transaction highlights the impact of the time value concept. Legend has it that that the Lenape Indians sold an unimproved Manhattan Island to the Dutch for $24 in 1626. If that $24 had been invested to earn a rate of 6% of interest per year in January of 1626, it would be worth more than $125 billion as of the end of December 2009. After 384 years, the 22 square miles of unimproved land no longer appears to be so "cheap."

An Equitable Distribution Plan Should Be Adjusted to Constant Dollars to Reduce the Greater Harm Suffered by Long-term Investors.

18.   I have reviewed the Report of Temporary Receiver's Activities for the Period from February 25, 2009 through May 22, 2009 (the "Receiver's First Report") and the Report of Receiver's Activities for the Period from May 25, 2009 through May 28, 2010 (the "Receiver's Second Report"). From the Receiver's reports, I understand that Paul Greenwood and Stephen Walsh operated the Westridge entities fraudulently beginning at least as early as 1996. *See* Receiver's First Report at 2, 8; Receiver's Second Report at 3.

19.   The Receiver's reports explain that investors in Westridge entities made contributions and withdrawals between 1996 and February 2009, when the SEC and CFTC discovered the fraud and asked the Court to appoint a receiver. *See* Receiver's First Report at 7-13; Receiver's Second Report at 8.

20.   I understand that the Receiver will review proposals to distribute the significant pool of money (exceeding $800 million) being returned to Westridge investors and ultimately propose a distribution plan to the Court. I have been informed that the Receiver's goal in proposing a distribution plan is to treat investors equitably.

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21.   I have been informed that one method of distribution that has been discussed is distributing funds *pro rata* on a net principal basis. As I understand it, under this proposal an investor's withdrawals would be subtracted from an investor's contributions to determine each investor's net principal investment. The estate would then be distributed among all investors *pro rata*. I have been informed that another method of distribution that has been discussed is distributing funds *pro rata* based on an investor's net principal adjusted to constant dollars using the CPI.

22.   It is my opinion that an equitable distribution plan is one that treats early and late investors fairly. A net-principal distribution plan would treat recent investors more favorably than early investors. Investors that invested money with Westridge in 1996 or 2000 have not only lost the opportunity to invest that money elsewhere, but also lost purchasing power at a higher rate than investors who invested their money more recently. Adjusting net principal to constant dollars using the CPI equalizes the value of contributions and withdrawals made at different points in time. Distributing funds *pro rata* based on an adjusted net principal basis reduces the large disparity between losses suffered by early investors and by late investors. Therefore, distributing funds on the basis of net investment adjusted to constant dollars is more equitable than distributing funds on an unadjusted net principal basis.

The Consumer Price Index Is a Reasonable and Conservative Way to Adjust Principal to Constant Dollars.

23.   The rate in time-value calculations is determined using various methodologies depending on the type of security that is under consideration. For example, in the equity market the discount or time value rate is set using capital market theory. That theory holds that the return demanded by equity investors is a linear function of the market risk of the stock and the equity risk premium. The risk premium has averaged just under 8% over the last 82 years. For

an equity security with average market risk, the rate used in time value calculations to value the security would be approximately 12%. In the case of bonds, the return demanded by bond investors varies with the term to maturity on the bond, its credit quality, and the current term structure of interest rates. Currently, the term structure indicates that a US Treasury bond with a 10-year maturity is priced to return approximately 2.5%.

24.   One very conservative but reasonable way to adjust funds to account for the time value of money is to value funds in constant dollars by applying an accepted rate of inflation to those funds. Since the rate of inflation is embedded in the nominal rates quoted in the capital markets, it represents a minimum rate to reimburse investors. Compensation at an acceptable rate of inflation would return investors to their original position in terms of their purchasing power, without giving them any real rate of return.

25.   The CPI is a measure of the average change over time in prices paid by urban consumers for a market basket of goods. The CPI is the most widely used measure of inflation. It is used to adjust economic series such as retail sales, earnings, and the value of a consumer's dollar for inflation. The CPI is also used to adjust tax brackets for inflation to avoid inflation-induced increases in tax rates. It is publicly available and widely regarded as one of the most credible economic indicators available.

26.   The CPI is often used in calculations designed to decompose nominal rates in the capital markets into their component parts. This is done because it is often useful to cast valuation problems in terms of the same kind of dollars, thus eliminating the influence of inflation. Constant dollars are generally defined relative to a given reference year. These constant dollars are the dollars that continue to have the same purchasing power as the dollars in the reference year.

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27.   The CPI represents a reasonable and generally accepted indicator of the rate of inflation and is an appropriate way to adjust investor's net principal to constant dollars here.

I hereby declare under penalty of perjury that the foregoing is true and correct.

Executed on October 21, 2010

THOMAJEAN JOHNSEN

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EXHIBIT A

VITA

Thomajean Johnsen, PhD

Reiman School of Finance
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Denver, CO 80208
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Education

BA&MA	University of North Carolina, Greensboro
MBA	University of Denver
PhD	University of Colorado

Dissertation   "An Empirical Examination of Wealth
 Effects Associated with Event-Related
 Shifts in Systematic Risk." Selected as Outstanding Paper
in Corporate Finance.
 Midwest Finance Association, 1994.

Current: Associate Professor
Reiman School of Finance
Daniels College of Business
University of Denver

Areas of Expertise

Portfolio Management and Theory
 Multifactor Risk Models of Equity Markets
 Return Attribution and Performance Measurement
 Quantitative Methods in Finance
 Capital Markets

Consulting Relationships

 Qwest Asset Management
 Ziegler Capital Management, LLC
 Standard and Poor's Compustat
 Blueprint Growth Institute
 Blueprint Growth Investors, LLC

Publications

"Equity Collars as an Alternative to Debt in Traditional Asset Allocation", Journal of Financial Services
   Professionals, forthcoming.

"Exploring the Use of Equity Collars in Asset Allocation: A Simulation Approach", Journal of
   Financial Services Professionals, November, 2009.

"A Framework for Factor Return Attribution", Journal of Investing, Spring, 2009.

"Benchmarking Performance Ratios for Oil and Gas Independents, 1999-2000", Petroleum
   Accounting and Financial Management Journal, Summer, 2001.

"Socially Responsible Investing in the Context of Asset Allocation". Journal of Investing,
   Fall, 2000.

"Socially Responsible Investing in the Context of Asset Allocation, published in
   The Investment Research Guide to Socially Responsible Investing, June, 2000.

"Oil and Gas Industry Performance Benchmarks for 1996-97". Petroleum Accounting
   and Financial Management Journal, Spring 1999.

"Analysis of Oil and Gas Stock Returns with Benchmark Ratios", Petroleum Accounting
   and Financial Management, Fall, 1999.

"Socially Responsible Investing: Growing Issues and New Opportunities".
   Business and Society, September, 1998.

"Expanding Socially Screened Portfolios: An Attribution Analysis of
   Bond Performance". Journal of Investing, Fall, 1997.

"Recycling: A Structured Student Exercise". Journal of Management Education,
   May, 1997.

"1994 and 1995 Key Indicators of Performance for Oil and Gas Firms:
   All Sectors and Quartile Benchmarks for Independents". Petroleum
   Accounting and Financial Management Journal,   Fall/Winter, 1996.

"Nuisance OLS Correlations in Market Model Parameter Shift Studies" .
   Quarterly Journal of Business and Economics, Spring, 1996.

"Are Petroleum Market Values a Triumph of Economics and Accounting?".
   Journal of Business Finance and Accounting, March, 1996.

"Do Investors Follow Accounting or Appraised Petroleum Values?"
   March 1995. Petroleum Accounting and Financial Management Journal.

"Key Indicators of Performance for Oil and Gas Firms: A contrast of All Sectors:
   Petroleum Accounting and Financial Management Journal, Summer, 1995.

"Determinants of Oil and Gas Company Valuations". Oil and Gas Investor,
   September, 1995.

"Predicting Corporate Bankruptcy and Financial Distress: Information
   Value Added by Multinomial Logit Models". Journal of Economics
   and Business, 1994.

"Key Indicators of Performance for Oil and Gas Firms: A Contrast of All Sectors".
<u>TIMS - Proceedings 1994 Annual Meeting</u>.

"Earnings Management and Executive Compensation Incentives". <u>Proceedings,
American Accounting Association, Southwest Region, 1994</u>.

"Earnings Management with Early Adoption of a FASB Statement".
<u>Journal of Managerial Issues</u>, Summer, 1993.

"Financial Ratios and Macroeconomic Effects on Firm Bankruptcy: Lender Implications".
<u>Journal of Financial and Strategic Decisions</u>, Vol. 6, No. 2, 1993.

"An Empirical Test of the `Pecking Order' Theory of Capital Structure". <u>Proceedings,
Decision Sciences</u>, November 1990.

All publications are coauthored.

<u>Professional Organizations and Designations</u>

Financial Management Association

Registered Investment Advisor

EXHIBIT B

Materials Considered

1.   Report of Temporary Receiver's Activities for the Period from February 25, 2009 through

May 22, 2009.

2.   Report of Receiver's Activities for the Period from May 25, 2009 through May 28, 2010.

3.   Standard and Poor's Compustat Data.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION, Plaintiff, -against- WG TRADING INVESTORS, L.P., WG TRADING COMPANY LIMITED PARTNERSHIP, WESTRIDGE CAPITAL MANAGEMENT, INC., PAUL GREENWOOD, and STEPHEN WALSH, Defendants, ROBIN GREENWOOD and JANET WALSH, Relief Defendants.	No. 09 CV 1750 (GBD)
COMMODITY FUTURES TRADING COMMISSION, Plaintiff, -against- STEPHEN WALSH, PAUL GREENWOOD, WESTRIDGE CAPITAL MANAGEMENT, INC., WG TRADING INVESTORS, L.P., WGIA, LLC, Defendants, WESTRIDGE CAPITAL MANAGEMENT ENANCEMENT FUNDS, INC., WG TRADING COMPANY, L.P., WG LLC, K&L INVESTMENTS and JANET WALSH, Relief Defendants.	No. 09 CV 1749 (GBD)

DECLARATION OF THOMAJEAN JOHNSEN, PH.D.,
IN SUPPORT OF QWEST ASSET MANAGEMENT CO. AND QWEST PENSION
TRUST'S PROPOSAL FOR DISTRIBUTION OF FUNDS HELD BY THE RECEIVER

I, THOMAJEAN JOHNSEN, hereby declare:

QUALIFICATIONS

1.   I am an Associate Professor at the Reiman School of Finance at the University of Denver, from which I received my MBA in 1983. I have recently been appointed as the Co-Chair at the Reiman School with a 4 year term to begin in July 2011. I have a Ph.D. from the University of Colorado, and my consulting firm, Portfolio Research Solutions, has been a Registered Investment Advisor in the state of Colorado since 1999. I teach in the areas of capital markets; portfolio management and performance analysis; financial applications of econometrics; and quantitative models of security selection. My research focus and expertise include the sources of risk/volatility in equity portfolios; portfolio management and risk assessment. I have written twenty-three articles on these and related topics. I am a member of the Financial Management Association and regularly attend academic and practitioner research conferences. My curriculum vitae is attached as Exhibit A to this declaration.

2.   I am being compensated at $250 an hour for my work on this matter. My compensation is not contingent upon the opinions that I render or the outcome of the litigation.

3.   Attached as Exhibit B is a list of the materials I considered in reaching the opinions expressed in this report.

ASSIGNMENT

4.   I have been retained by Qwest Asset Management, Co. and the Qwest Pension Trust to offer expert testimony regarding what would be an equitable distribution plan for investors in the Westridge entities fraudulently operated by Paul Greenwood and Stephen Walsh.

STATEMENT OF OPINION

5.   It is a fundamental economic and financial principle that there is a time value associated with money. The concept of the time value of money holds that a dollar received

today can be reinvested immediately to generate additional dollars. At the same time, inflation operates to weaken the purchasing power of that dollar in the future. These combined forces make today's dollar more valuable than a dollar received in a future period. In finance, this principle means that there is always a preference for early money over deferred money.

6.   It is my opinion that funds invested over time in Westridge entities cannot be equitably valued and compared unless the funds are adjusted to constant dollars by applying the Consumer Price Index (the "CPI"). Using the CPI to adjust investors' net principal to constant dollars reduces the difference between the much greater losses that long-term investors have suffered relative to more recent investors. It is the most equitable approach here.

BASES FOR OPINION

The Theoretical Basis for the Time Value Concept

7.   In 1907, Irving Fisher published *The Rate of Interest* (which was revised in 1930 under the title *The Theory of Interest*), which presents the classic economic treatment of the time value of money. In the well-known Fisher equation, the time value of money is expressed as a nominal rate of return or interest and used in time value calculations. The nominal rate of return or interest is the sum of the real rate of return plus an expected inflation premium. In this way, the nominal rate of interest both reflects the growth rate of money and compensates investors for the loss of purchasing power. As a result, both the real rate of return and the inflation rate have an additive effect on the rates included in time value calculations.

8.   The Fisher equation shows that the concept of inflation is central to the calculation of the time value of money. Inflation is generally considered to be caused by an increase in the volume of available money in relation to available goods and services. As the money supply increases within the economy and the availability of goods remains constant or declines, the inflation rate increases. All other factors held equal, without an inflation

-2-

adjustment to income, one's purchasing power will decrease. In an economic environment where inflation has not been zero, the result is that a dollar today purchases less than a dollar did in the past. From the investor's point of view, an investment should return a rate sufficient to compensate the investor for loss of purchasing power over the life of the investment.

9.   For example, in 2000 the inflation (CPI) rate was 1.746% and by the end of 2009 it was 2.172%. The average inflation rate over this 10-year period was 1.952%. Thus, while at the beginning of 2000 one gallon of milk cost approximately $2.88, today in 2010 it would cost approximately $3.50.[1] The U.S. government acknowledges inflation by providing judges and other federal employees cost of living pay increases. *See, e.g.,* Memorandum from John Berry, Director of the United States Office of Personnel Management (Dec. 23, 2009) (available at http://www.chcoc.gov/Transmittals/TransmittalDetails.aspx?TransmittalID=2653); Press Release, Administrative Office of the U.S. Courts, Federal Judges' Treatment By Congress Called Unfair (Dec. 12, 2008) (available at http://www.uscourts.gov/news/NewsView/08-12-12/Federal_Judges_Treatment_By_Congress_Called_Unfair.aspx) (explaining that lack of 2009 cost of living adjustment for federal judges was "starkly unfair"). Many corporations and colleges and universities, as well as other employers, do the same.

10.   If one assumes that a real rate of return is zero, then the Fisher equation provides that the time value of money should be calculated at a nominal rate equal to inflation in order to preserve purchasing power. To do this, money should be adjusted into constant dollars of a selected year.

11.   Adjusting to constant dollars is standard practice in economic studies or financial analyses. This is done because it is often useful to cast valuation problems in terms of the same

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[1] Of course, other market forces also affect the price of goods.

kind of dollars, thus eliminating the influence of inflation. Constant dollars are generally defined relative to a given reference year. These constant dollars are the dollars that continue to have the same purchasing power as the dollars in the reference year.

12.   An investment analysis may be carried out in real or nominal terms. Whether an analyst chooses to evaluate an investment in real or nominal terms, she must be consistent in her treatment of the cash flows and rates of return. Investment cash flow forecasts in nominal terms must be adjusted with a nominal rate in time-value calculations. Likewise, cash flow forecasts in real terms must be adjusted with a real rate.

The Concept of the Time Value of Money Is Well-rooted in History and Serves as a Bedrock Finance Principle.

13.   The concept of the time value of money has been recognized for more than eight hundred years. Mathematician Leonardo Fibonacci developed the concept in 1202, though some believe it was recognized long before that by the Arabs or the Indians. *See A History of the Theory of Investments: My Annotated Bibliography*, by Mark Rubenstein.

14.   Today, the time value of money is a fundamental principle of graduate and undergraduate finance curriculums as well as the curriculum for the Certified Financial Analyst Institute. For example, all corporate and investment finance textbooks explain and apply the concept. Examples of such finance textbooks are *The Theory of Finance*, by Fama and Miller; *Investments* and *Essentials of Investments,* by Bodie, Kane, and Marcus; *Intermediate Corporate Finance,* by Brigham and Daves; *Contemporary Financial Management,* by Moyer, McGuigan and Kretlow; *Financial Markets and Institutions*, by Madura; *Fixed Income Mathematics*, by Fabozzi, *International Financial Management,* by Eun and Resnik; and *Fundamentals of Futures and Option Markets*, by Hull, among others.

15.   The application of the concept of the time value of money is widespread. Individuals regularly take the time value of money into account when determining the desirability of investing in the capital markets, in determining mortgage payments, or evaluating various consumer-related financial contracts. Investment managers utilize time-value-of-money calculations to determine the economic or intrinsic value of equity securities when selecting securities to include in actively managed portfolios and to calculate the yield to maturity on bond securities. Portfolio managers use time-value concepts to measure portfolio returns and to evaluate the performance of mutual funds, hedge funds, and other investment vehicles. Corporations utilize the time value of money in making capital budgeting decisions by calculating the net present value or internal rate of return for various plant, property, and equipment purchases. Corporations also take the time value of money into account when making decisions to issue commercial paper for their short term funding needs or to purchase the commercial paper of other corporations in order to earn a return that is both short term and of high credit quality. Investment banks and analysts working in the area of mergers and acquisitions utilize the concept to value potential takeover companies. Even state lotteries apply the time value of money, recognizing that a full payment to winners over many years is equal to (or in some cases less than) a discounted immediate payment.

16.   A simple example demonstrates the concept of the time value of money. If I deposited $100 in a savings account earning 3% annually ten years ago, it would be worth approximately $134.39 today. If the $100 had been invested in a slightly more risky investment such as a money market account earning 5% annually, it would be worth approximately $162.89 today. And since the S&P 500 has appreciated at 8.79% annually between January 1990 and

December 2009, if I had invested $100 in January 1990 in an index fund that tracked the S&P 500, that investment would be worth $539.24 at the end of December 2009.

17.   A look at an historical transaction highlights the impact of the time value concept. Legend has it that that the Lenape Indians sold an unimproved Manhattan Island to the Dutch for $24 in 1626. If that $24 had been invested to earn a rate of 6% of interest per year in January of 1626, it would be worth more than $125 billion as of the end of December 2009. After 384 years, the 22 square miles of unimproved land no longer appears to be so "cheap."

An Equitable Distribution Plan Should Be Adjusted to Constant Dollars to Reduce the Greater Harm Suffered by Long-term Investors.

18.   I have reviewed the Report of Temporary Receiver's Activities for the Period from February 25, 2009 through May 22, 2009 (the "Receiver's First Report") and the Report of Receiver's Activities for the Period from May 25, 2009 through May 28, 2010 (the "Receiver's Second Report"). From the Receiver's reports, I understand that Paul Greenwood and Stephen Walsh operated the Westridge entities fraudulently beginning at least as early as 1996. *See* Receiver's First Report at 2, 8; Receiver's Second Report at 3.

19.   The Receiver's reports explain that investors in Westridge entities made contributions and withdrawals between 1996 and February 2009, when the SEC and CFTC discovered the fraud and asked the Court to appoint a receiver. *See* Receiver's First Report at 7-13; Receiver's Second Report at 8.

20.   I understand that the Receiver will review proposals to distribute the significant pool of money (exceeding $800 million) being returned to Westridge investors and ultimately propose a distribution plan to the Court. I have been informed that the Receiver's goal in proposing a distribution plan is to treat investors equitably.

21.   I have been informed that one method of distribution that has been discussed is distributing funds *pro rata* on a net principal basis. As I understand it, under this proposal an investor's withdrawals would be subtracted from an investor's contributions to determine each investor's net principal investment. The estate would then be distributed among all investors *pro rata*. I have been informed that another method of distribution that has been discussed is distributing funds *pro rata* based on an investor's net principal adjusted to constant dollars using the CPI.

22.   It is my opinion that an equitable distribution plan is one that treats early and late investors fairly. A net-principal distribution plan would treat recent investors more favorably than early investors. Investors that invested money with Westridge in 1996 or 2000 have not only lost the opportunity to invest that money elsewhere, but also lost purchasing power at a higher rate than investors who invested their money more recently. Adjusting net principal to constant dollars using the CPI equalizes the value of contributions and withdrawals made at different points in time. Distributing funds *pro rata* based on an adjusted net principal basis reduces the large disparity between losses suffered by early investors and by late investors. Therefore, distributing funds on the basis of net investment adjusted to constant dollars is more equitable than distributing funds on an unadjusted net principal basis.

The Consumer Price Index Is a Reasonable and Conservative Way to Adjust Principal to Constant Dollars.

23.   The rate in time-value calculations is determined using various methodologies depending on the type of security that is under consideration. For example, in the equity market the discount or time value rate is set using capital market theory. That theory holds that the return demanded by equity investors is a linear function of the market risk of the stock and the equity risk premium. The risk premium has averaged just under 8% over the last 82 years. For

an equity security with average market risk, the rate used in time value calculations to value the security would be approximately 12%. In the case of bonds, the return demanded by bond investors varies with the term to maturity on the bond, its credit quality, and the current term structure of interest rates. Currently, the term structure indicates that a US Treasury bond with a 10-year maturity is priced to return approximately 2.5%.

24.   One very conservative but reasonable way to adjust funds to account for the time value of money is to value funds in constant dollars by applying an accepted rate of inflation to those funds. Since the rate of inflation is embedded in the nominal rates quoted in the capital markets, it represents a minimum rate to reimburse investors. Compensation at an acceptable rate of inflation would return investors to their original position in terms of their purchasing power, without giving them any real rate of return.

25.   The CPI is a measure of the average change over time in prices paid by urban consumers for a market basket of goods. The CPI is the most widely used measure of inflation. It is used to adjust economic series such as retail sales, earnings, and the value of a consumer's dollar for inflation. The CPI is also used to adjust tax brackets for inflation to avoid inflation-induced increases in tax rates. It is publicly available and widely regarded as one of the most credible economic indicators available.

26.   The CPI is often used in calculations designed to decompose nominal rates in the capital markets into their component parts. This is done because it is often useful to cast valuation problems in terms of the same kind of dollars, thus eliminating the influence of inflation. Constant dollars are generally defined relative to a given reference year. These constant dollars are the dollars that continue to have the same purchasing power as the dollars in the reference year.

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27.   The CPI represents a reasonable and generally accepted indicator of the rate of

inflation and is an appropriate way to adjust investor's net principal to constant dollars here.

I hereby declare under penalty of perjury that the foregoing is true and correct.

Executed on October 21, 2010

THOMAJEAN JOHNSEN

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EXHIBIT A

VITA

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Education

BA&MA	University of North Carolina, Greensboro
MBA	University of Denver
PhD	University of Colorado

Dissertation "An Empirical Examination of Wealth
Effects Associated with Event-Related
Shifts in Systematic Risk." Selected as Outstanding Paper
in Corporate Finance.
Midwest Finance Association, 1994.

Current: Associate Professor
Reiman School of Finance
Daniels College of Business
University of Denver

Areas of Expertise

Portfolio Management and Theory
Multifactor Risk Models of Equity Markets
Return Attribution and Performance Measurement
Quantitative Methods in Finance
Capital Markets

Consulting Relationships

Qwest Asset Management
Ziegler Capital Management, LLC
Standard and Poor's Compustat
Blueprint Growth Institute
Blueprint Growth Investors, LLC

Publications

"Equity Collars as an Alternative to Debt in Traditional Asset Allocation", <u>Journal of Financial Services</u>
  <u>Professionals</u>, forthcoming.

"Exploring the Use of Equity Collars in Asset Allocation: A Simulation Approach", <u>Journal of</u>
   <u>Financial Services Professionals,</u> November, 2009.

"A Framework for Factor Return Attribution", <u>Journal of Investing</u>, Spring, 2009.

"Benchmarking Performance Ratios for Oil and Gas Independents, 1999-2000", <u>Petroleum</u>
   <u>Accounting and Financial Management Journal</u>, Summer, 2001.

"Socially Responsible Investing in the Context of Asset Allocation". <u>Journal of Investing</u>,
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"Oil and Gas Industry Performance Benchmarks for 1996-97". <u>Petroleum Accounting</u>
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"Analysis of Oil and Gas Stock Returns with Benchmark Ratios", <u>Petroleum Accounting</u>
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"Socially Responsible Investing: Growing Issues and New Opportunities".
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"Are Petroleum Market Values a Triumph of Economics and Accounting?".
  <u>Journal of Business Finance and Accounting</u>, March, 1996.

"Do Investors Follow Accounting or Appraised Petroleum Values?"
  March 1995. <u>Petroleum Accounting and Financial Management Journal</u>.

"Key Indicators of Performance for Oil and Gas Firms: A contrast of All Sectors:
  <u>Petroleum Accounting and Financial Management Journal</u>, Summer, 1995.

"Determinants of Oil and Gas Company Valuations". <u>Oil and Gas Investor</u>,
  September, 1995.

"Predicting Corporate Bankruptcy and Financial Distress: Information
  Value Added by Multinomial Logit Models". <u>Journal of Economics</u>
  <u>and Business</u>, 1994.

"Key Indicators of Performance for Oil and Gas Firms: A Contrast of All Sectors".
TIMS - Proceedings 1994 Annual Meeting.

"Earnings Management and Executive Compensation Incentives". Proceedings,
American Accounting Association, Southwest Region, 1994.

"Earnings Management with Early Adoption of a FASB Statement".
Journal of Managerial Issues, Summer, 1993.

"Financial Ratios and Macroeconomic Effects on Firm Bankruptcy: Lender Implications".
Journal of Financial and Strategic Decisions, Vol. 6, No. 2, 1993.

"An Empirical Test of the `Pecking Order' Theory of Capital Structure". Proceedings,
Decision Sciences, November 1990.

All publications are coauthored.

Professional Organizations and Designations

Financial Management Association

Registered Investment Advisor

EXHIBIT B

Materials Considered

1.   Report of Temporary Receiver's Activities for the Period from February 25, 2009 through

May 22, 2009.

2.   Report of Receiver's Activities for the Period from May 25, 2009 through May 28, 2010.

3.   Standard and Poor's Compustat Data.