Fund scandal clips JB Oxford

By Edward Iwata, USA TODAY

As the summer heat hit 90 degrees, FBI agents stormed the Beverly Hills, Calif., offices of JB Oxford, a small brokerage that was under investigation for its ties to Irving Kott, a Canadian with a long history of securities fraud problems.

J.B. Oxford's troubled history involves a stock promoter with a checkered past.

By Bob Riha Jr., USA TODAY

According to former employees who were there at the time, some JB Oxford (JBOH) workers thought it was a joke. But stern agents flashed their badges and drilled them with questions. They demanded trading records and address books. They hauled away boxes of files and computers.

For some, the government raid in August 1997 typifies JB Oxford's legal troubles over the past decade. Although the firm has never been charged with a crime, federal investigators have scrutinized the brokerage, and irate investors have accused it of securities fraud. In the 1990s, JB Oxford cleared stock trades for some of the most notorious brokerages on Wall Street, according to court filings, regulators and prosecutors. Last year, JB Oxford was ordered to pay $3 million to investors after a judge found it liable for another brokerage's fraudulent conduct.

New York State Attorney General Eliot Spitzer charged, in a complaint filed in September, that hedge fund Canary Capital Partners made illegal mutual fund trades. The complaint named JB Oxford as one of several firms that processed trades for Canary.

State and federal investigations into mutual fund trading also are exposing the back-office roles of intermediary firms such as JB Oxford, which are little-known to the public but play crucial roles in handling investors' money. While JB Oxford is an online brokerage, it also works as a "clearing" firm for other brokerages, overseeing customers' accounts and processing the paperwork and payments on stock and mutual fund trades.

Brokerage has links to firms implicated in '90s

Brokerage JB Oxford's name surfaced in state and National

Association of Securities Dealers investigations of micro-cap stock fraud during the 1990s. Prosecutors did not charge the firm with wrongdoing, but JB Oxford provided services to brokerages that were implicated, records show.
Among them:

- Greenway Capital, one of several defunct boiler rooms run by Philip Abramo — a capo, or captain, in the DeCavalcante crime family, according to a grand jury indictment and an FBI agent's testimony in a case involving Abramo.
  This year, a New York jury convicted Abramo, 58, of racketeering, loan sharking and securities fraud in a trial that brought down the DeCavalcantes, believed to be the inspiration for The Sopranos television drama.
- Stratton Oakmont and Biltmore Securities, used by organized crime to manipulate the stock prices of micro-cap companies, according to congressional testimony by regulators.
- The New York boiler room of Euro-Atlantic Securities, a defunct brokerage based in Boca Raton, Fla. It was run by the late Colombo crime family captain William "Wild Bill" Cutolo and associates Dominick "Black Dom" Dionisio and Enrico Locasio, according to indictments. Dionisio and Locasio are serving prison terms for securities fraud.

By Edward Iwata

Canary agreed to a $40 million settlement with prosecutors, but JB Oxford has not been charged. The complaint does not say whether JB Oxford knew Canary's trades were fraudulent.

Brad Maione, a spokesman for Spitzer, said "an investigation is ongoing" into JB Oxford.

On another front, JB Oxford disclosed recently that the Securities and Exchange Commission sent it a Wells notice, warning that civil charges and penalties for securities fraud may be brought against the firm. JB Oxford has replied to the SEC and hopes to resolve the legal issues, the company said.

Last month, Spitzer's office and the SEC went after Security Trust, another back-office firm, charging three former executives with grand larceny and securities fraud. The Office of the Comptroller of the Currency plans to dissolve Security Trust.

JB Oxford is drawing attention because of its agreement with Canary to clear the hedge fund's paperwork on after-hours trades. JB Oxford got compensation equaling 1% of assets traded, according to Spitzer's complaint against Canary.

Christopher Jarratt, 41, CEO of JB Oxford, said New York prosecutors and the SEC subpoenaed the company last summer and that the company is cooperating with investigators. JB Oxford has given the agencies documents and testimony on several unnamed mutual funds that used JB Oxford to process trades in 2002-03, according to the firm's recent SEC filings.

"We feel we're excellent corporate citizens," Jarratt said. "We're following all rules and regulations."

Jarratt added that JB Oxford is investigating the role of JB Oxford employees in the late-trading agreement with Canary. The firm has not decided whether to discipline them.

In the mid- and late-1990s, JB Oxford was a major clearing firm that processed the brokerage trades of micro-cap stocks, the tiny, obscure companies with little market value. The stocks often were sold by "boiler-room" brokerages, also called "bucket shops," which used high-pressure telephone sales tactics to run investment scams on unwary customers.

Even though JB Oxford and other clearing firms typically did paperwork on the stock trades, they were called prime contributors "to the explosion in micro-cap fraud" in a 1997 report on securities crime by the New York attorney general's office.

The report found that clearing firms were "accomplices" and "knowing lubricants" in the boiler-room scams, which included bogus trades, unauthorized trading in customers' accounts and other frauds.

JB Oxford cleared trades for Stratton Oakmont, Biltmore Securities, Monroe Parker Securities, Greenway Capital and other brokerages that were barred from the industry by regulators in recent years.

Before authorities shut them down, some of the firms were run or influenced by organized crime, according to government officials, investors' attorneys, grand jury indictments, lawsuits and other sources.

"Clearly, JB Oxford is a firm with a checkered past," said Gerald Baldwin at Frost Brown Todd, a Cincinnati law firm that won a case for investors against JB Oxford last year.

Investors in recent years filed scores of lawsuits — and arbitration claims with the National Association of Securities Dealers — against JB Oxford and the boiler rooms, alleging they lost billions of dollars in bogus trades and initial public offering scams.

JB Oxford has been fined $216,000 by the NASD in 10 cases from 1996 to September, NASD records show. The NASD accused the firm of charging excessive commissions, failing to report Nasdaq trades and failing to supervise trading.

In one case, several hundred Ohio investors charged they lost $100 million to "pump-and-dump" trades run by Monroe Parker and cleared by JB Oxford. In such scams, stockbrokers talk up a stock and rapidly trade shares back and forth to artificially jack up its price. When the stock peaks, they sell it to the public, which is left holding shares that quickly sink.

The investors alleged that JB Oxford knew Monroe Parker was taking companies public at $7 a share, inflating the price to $15, then dumping the stock on investors at a steep profit, according to the judge's review of the case. "All of the transactions were rigged," said Joseph Dehner, a Frost Brown Todd attorney for the investors. "There was no market activity at all" to boost prices.

At the NASD hearing, Howard Berg, a securities expert who testified for the investors, said he had never seen a clearing firm that had "participated as actively in a fraud as here," reads a legal summary by federal Judge Arthur Spiegel, who reviewed the case.

JB Oxford argued it did not know Monroe Parker was engaging in illegal conduct.

The judge disagreed, writing that "the pump-and-dump scheme orchestrated by (Monroe Parker) could not have occurred without (JB Oxford)" and that "a great number of investors were harmed repeatedly."

Spiegel last year approved a $6.2 million NASD award for the investors and ordered JB Oxford to pay $3 million.

Today, nearly all the boiler rooms from the 1990s that had ties to organized crime are closed. JB Oxford, which cleared trades for some of them, was not charged.

Until recently, attorneys say, it has been difficult to bring cases against clearing firms, because securities laws have long protected clearing firms from liability for frauds committed by their brokerage clients.

Clearing firms have been "relatively bulletproof and gotten away with making a lot of money," said Jeffrey Feldman, a securities lawyer in San Francisco.

However, reporting rules for clearing firms were toughened by the SEC, the NASD and the New York Stock Exchange after a scandal involving investment giant Bear Stearns. In 1999, Bear Stearns paid $39 million to settle charges alleging that it aided boiler room A.R. Baron in illegal trades.

"Clearing firms can no longer say they thought it was (the brokerage's) responsibility," said former prosecutor Joel Cohen, an attorney at Greenberg Traurig.

Behind the scenes

Much of JB Oxford's history involves Kott, a Canadian stock promoter in his 70s. The tall, slender Kott, a former clothing designer partial to Italian suits, is well known among prosecutors and regulators.

In 1976, he pleaded guilty in Ontario of scheming to defraud investors. Two years later, he survived a murder attempt by mobsters after a bomb exploded under his car in Montreal. In 1990, he paid Dutch authorities $4 million to settle a case involving First Commerce Securities, a vast boiler room in Amsterdam that allegedly sold bogus stocks to investors worldwide.

Through much of the 1990s, Kott worked quietly behind the scenes to control JB Oxford, according to an investors' lawsuit against the brokerage. The report by New York prosecutors called Kott "the unregistered control person" of JB Oxford and "an undisclosed criminal element" at the brokerage.

JB Oxford and Kott's attorney have denied in media reports and interviews that Kott secretly controlled the firm, saying he was a consultant with his Canadian firm, Turret Consultants. "We would vigorously dispute the notion that he was a control person as defined under securities laws," says Brian Sun, an attorney for Kott at the Jones Day law firm.

But Kott clearly ran the show, say three former JB Oxford employees, a government official and two private attorneys familiar with boiler-room cases who requested confidentiality.

Kott negotiated JB Oxford's biggest deals, including an agreement with Stratton Oakmont founder Jordan Belfort to clear trades for Stratton Oakmont and several other boiler-room outfits, according to the government official and Baldwin, the attorney for the Ohio investors. Belfort was sentenced last year to four years in prison on fraud charges.

At one point, Kott pumped $1.9 million of badly needed capital into JB Oxford in a secret deal with Felix Oeri, a Swiss financier and former JB Oxford director, according to a lawsuit against JB Oxford. The lawsuit was filed by EBC Trust, a Monaco firm that federal investigators believed was an agent for Kott, according to the lawsuit.

Oeri's attorney, Thomas Green of Sidley Austin Brown & Wood, said Oeri "withdrew from the JB Oxford scene" years ago and still lives in Switzerland.

In 2000, three years after the FBI raid, JB Oxford agreed to pay $2 million to settle the Justice Department investigation into its relationship with Kott.

According to a copy of the confidential settlement obtained by USA TODAY, JB Oxford agreed to cut all business ties to Kott and 19 other people and entities linked to him, including his wife, Rhoda Davis Kott; his sons, Ian and Michael Kott; business associate Dominique Schittecatte; Walter E. Senior, a former Hollywood executive; EBC Trust, a Monaco firm; Arabella, a Luxembourg firm; and Oeri Finance, run by Oeri.

Meanwhile, Kott and some of his family and business associates were under investigation by the Justice Department and the SEC for their roles in 1990s stock-trading schemes involving micro-cap companies, according to JB Oxford's SEC filings and a Justice Department document on JB Oxford. Kott's attorney, Sun, declined to comment.

Kott, who once lived in a Beverly Hills mansion that had been owned by film legend Cary Grant, left the USA after the FBI raid and is living in Canada, according to a lawsuit involving JB Oxford and people familiar with him.

Assistant U.S. Attorney Gregory Weingart and SEC enforcement official Sandra Harris, both in Los Angeles, declined to comment on JB Oxford or Kott.

Good years and bad

New management took over JB Oxford in 1997, when a Nashville-based investment firm, Third Capital Partners, bought 47% of the brokerage.

JB Oxford did fine during the dot-com boom. It posted record revenue of $104 million in 1999. It had offices in Beverly Hills, New York, Miami and Basel, Switzerland. It ran a $10 million advertising campaign with former *M*A*S*H* television star Wayne Rogers, who once owned 1% of JB Oxford.

In a 2001 annual report, Jarratt crowed, "We have made it through ... the darkest hour and have established JB Oxford as a fierce, long-term competitor."

But behind the white JB Oxford neon sign outside its corporate headquarters, the firm was in turmoil, say seven former employees, who spoke on condition of anonymity. They described its offices as rough-and-tumble "sweatshops," where stockbrokers and customer-service workers toiled grueling hours, making cold calls and fielding complaints from furious customers. Bosses berated workers in front of others.

Jarratt, President James G. Lewis and others who took over JB Oxford in the late 1990s had little experience in the brokerage business. They were attorneys, real estate investors and corporate turnaround specialists who worked with ailing firms.

JB Oxford was bloodied when the stock market tanked and the recession hit. In 2001 and 2002, it suffered $20 million in losses. The firm slashed jobs. By 2001, barely 100 employees were left.

Struggling to grow, JB Oxford has spent $7 million since 2001 buying 36,000 customer accounts from several online brokerages, including Mr. Stock, Wall Street Equities and Stockwalk.com.

"It's been a difficult two years for us, but we think we've made the turn operationally," Jarratt said. "We're cautiously optimistic."

That's little comfort for John O'Malley, 46, owner of a construction firm in Dallas. He lost $400,000 on bogus, pumped-up stocks sold to him by a Monroe Parker stockbroker and cleared by JB Oxford, NASD records show.

O'Malley was hopeful when an NASD panel ruled in 2000 that Monroe Parker owed him $327,000. But then Monroe Parker went broke, and the panel found JB Oxford was not liable. O'Malley's claim, among others, is pending before a court-run restitution fund.

"I haven't received a dime," he said, "and I may never get my money back."

Contributing: Thomas Ankner, Pamela Fiawoo and Raymond Hicks

Ilya Barabanov, the guy who wrote the article about Dvoskin laundering money for the SVR.
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