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Squandered Futures

The polished CEO at Refco allegedly cooks the books, then enjoys a bang-up IPO--but not for long

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In the often rowdy world of commodities trading, Phillip Bennett, the chief of giant commodities broker Refco, seemed like a cut above. An elegant, Cambridge-educated detail man, he often dressed in three-piece suits, lived on a horse farm in New Jersey and was something of a gourmet. Bennett brought an aura of respectability to a firm that was known for highflying, sometimes sloppy ways, offering a striking contrast with Refco founder Thomas Dittmer, a cattle and oil trader and all-around swashbuckling guy who liked to hand out gold watches when he made a great trade. "They were rough, very street-smart gunslingers at Refco," says Victor Niederhoffer, a hedge-fund manager who had dealings with Bennett in the 1990s. Bennett "was a great counterpart--polished, responsible and diligent."

Appearances may have been deceiving. Just as Bennett was about to take off on a wine-tasting trip to Europe last week, police arrived at his Park Avenue penthouse to put him under arrest. Behind the refined veneer, it appears, Bennett may have been playing loose with the rules. Just two months after Refco raised \$583 million in an initial public offering (IPO), federal prosecutors accused Bennett of hiding \$430 million of uncollectible debt, in so doing propping up Refco's earnings and share price. When the news hit, Refco shares plunged from \$28.56 to \$7.90, wiping out \$2.6 billion of shareholder wealth before the New York Stock Exchange halted trading. It wasn't clear when--or if--trading in Refco would resume.

The commodities markets that Refco had dominated were holding up well last week. But there will be plenty of fallout elsewhere. A source close to Refco's largest shareholder, buyout kingpin Thomas Lee, says Lee figures his remaining Refco stake is worthless. Lee recouped \$175 million in the Refco IPO. But he had invested \$507 million for 57% of Refco in 2004, using funds from dozens of public and private pension systems, including California Public Employees' Retirement System, Pennsylvania State Employees' Retirement System, General Motors and Verizon. As a Refco insider (several Lee executives are on the Refco board), Lee and the underwriters who took the company public may be on the hook for shareholder losses. "We have a history of taking forceful action in response to misbehavior," says Alan Hevesi, New York State comptroller, whose retirement system invested \$36 million in Refco through Lee and others. Lee declined to comment. Bennett's lawyer, Gary Naftalis, reiterated what he had already said in court: "We think the government jumped the gun."

But investors are wondering how so many gatekeepers, including auditors at the accounting firm Grant Thornton and officials at the Securities and Exchange Commission (SEC), missed the company's alleged book cooking so soon after the scandals of Enron, Worldcom and others. "Everybody had a chance to look them over," says Bill Harris, a forensic accountant at the business-services firm CBIZ. "Four hundred thirty million dollars is an awful big number to hide." Those who have dealt with Refco say there was reason to be careful. In 1999 the Commodity Futures Trading Commission levied \$7 million in fines against Refco for order-taking and record-keeping violations. Several times during the '90s, Refco was cited by regulators for violations related to combining account balances and failing to supervise employees.

In recent years Bennett had improved Refco's record, but his handling of Refco's IPO may have been reckless in more ways than one. Not only did Bennett fail to disclose \$430 million--more than double last year's net income--that would never be collected (believed to be the result of hedge-fund clients who didn't pay up after bad trades), but he also went ahead with the IPO even though his top lieutenant, Santo Maggio, was under investigation by the SEC in connection with a stock-manipulation scheme that had driven software firm Sedona into the ground. Refco disclosed the investigation when it went public, saying the case would be resolved. But it never was, raising questions as to whether the IPO should have proceeded with Maggio on board. As for Bennett's debt maneuverings, says futures broker James Mound: "You wonder why someone so wealthy, in such a powerful position, would do something so immoral." Prosecutors aim to find

out, but Refco customers weren't waiting. They scrambled last week to take their business elsewhere in an exodus that may bring down the house of Refco.

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