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### *Luxury Vehicle*

# An 18% Return? It Sounded Good To Rich Investors

**Four Star Did Pay Off Well  
For Years -- Then Stopped;  
'Factoring' Phone-Sex Bills**

**Talk of a Big Arbitrage Play**

By **ROBERT TOMSHO**

Staff Reporter of THE WALL STREET JOURNAL

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LOS ANGELES -- Morton Turndorf's friends bragged for years about their investments in Four Star Financial Services. They told the 66-year-old retired apparel maker about annual returns of up to 18%, paid out in monthly checks.


Finally, Mr. Turndorf visited Four Star's offices in a pink granite high-rise on Wilshire Boulevard to hear for himself how the firm turned investments in 900-number operators, their unpaid receivables and other telecom ventures into steady profits. "They explained to me what they did and said everything was fine," recalls Mr. Turndorf, who invested \$100,000 in July 2002.

A month later, he got his first income check from Four Star. It turned out to be his last.

Now Four Star faces liquidation by a federal bankruptcy court here. Its trustee warns that as much as two-thirds of the \$200 million that 500 investors put into the company is gone. Federal prosecutors and the Federal Bureau of Investigation are in the early stages of looking into how that money was raised and what happened to it, say attorneys familiar with the matter. An attorney for two of the three founders of Four Star said he doesn't believe his clients are targets of the probe. As for the third founder, San Francisco attorney Mark Cohn, his lawyer said the U.S. attorney's office in Los Angeles "has made it pretty clear that that he is a target of this investigation."

For nearly a decade, Four Star and a predecessor company made promised payments to investors, and former employees and business associates say many of the early financing ventures were profitable. But lawyers who recently have dug through company records say they found few liquid assets and a tangle of interests in assets ranging from dubious Argentinean securities to X-rated bedroom videotapes of actress Pamela Anderson. "You have to scrape around pretty deep to find any real value," says Martin Zohn, a Los Angeles lawyer who represents one group of investors.

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Four Star's fall reflects a growing risk to affluent investors, who are increasingly putting their money into thinly regulated investments like hedge funds and private-equity offerings. About 44% of the 650,000 American households with a net worth of at least \$5 million had such investments in 2003, up from 20% in 2001, according to Spectrem Group, a Chicago consulting firm.

The air of high risk that once surrounded such investments has dissipated as major financial concerns have begun marketing them. Meanwhile, at a time when interest rates are low and the stock market unpredictable, many people are looking for investments with higher returns.

Securities regulators say the complexity of many alternative investments makes due diligence tough for even a sophisticated investor. It also "provides the ocean that fraudsters can swim in and not stand out as curiously unbelievable," says Mark Knops, an assistant Arizona attorney general specializing in financial fraud.

Investors lost \$1 billion in private-placement bonds bought from National Century Financial Enterprises, an Ohio company that saw two executives plead guilty to fraud charges in Columbus last year. Venture capitalists and high-tech entrepreneurs were among the losers of \$240 million invested with Reed E. Slatkin. He pleaded guilty in 2002 to federal fraud, conspiracy and money-laundering charges after using falsified financial statements to convince investors he was a successful investment adviser.

For years, Four Star portrayed itself as a thriving financial-services firm. It made loans to small businesses and tried to profit by collecting through phone companies on the unpaid receivables of 900-number firms that offered premium priced pay-per-call telephone access to everything from phone-sex operators to psychic hotlines.

Doctors, accountants and investment advisers put money into the closely held firm, as did the likes of Sir Arthur Gilbert, a Los Angeles philanthropist and art collector who died in 2001, and Donald Passman, an entertainment attorney who represented singer Mariah Carey and the rock band R.E.M. Mr. Passman, through a spokeswoman, declined to comment. He filed a lawsuit against Four Star in state court in California last year.

#### **In the Dark**

Four Star's troubles began with a downturn of the 900-number industry in the late 1990s, which left the firm scrambling to keep payouts to investors flowing. As its difficulties worsened, investors largely were left in the dark, except for occasional letters promising a complex multinational "arbitrage" transaction that would save the company.

Four Star investors heard little about one venture until it was too late -- a Baltimore telemarketing scheme financed by the company. Last year, Four Star and Mr. Cohn were convicted of fraud and conspiracy in a federal court in Baltimore for their roles in the scam, which bilked 27,000 consumers with weak credit out of \$3.3 million by promising them a new credit card. Four Star's other two founders, Los Angeles accountants Ronald I. Anson and Jack E. Garrett, who weren't charged in that or any other case, have acknowledged in interviews and letters to investors that some investments on their books are at least partially fictitious.

#### **BUYER BEWARE**

Significant events in the history of Four Star:

All three Four Star founders deny any wrongdoing. In a telephone interview, Mr. Garrett, 51 years old, a former Deloitte & Touche tax specialist, says he and Mr. Anson

- **October 1991:** Launch of 900 Capital Services Inc.
- **April 1996:** Formation of Four Star Financial Services LLC.
- **January 2001:** Federal investigators question Four Star co-founder Mark Cohn about Baltimore telemarketing scam.
- **July 2001:** Four Star, Mr. Cohn and others indicted in Baltimore on multiple federal fraud and conspiracy counts.
- **Fall 2002:** Four Star stops making payments to investors.
- **June 2003:** Four Star and Mr. Cohn found guilty in Baltimore case.
- **October 2003:** Investors force Four Star into federal bankruptcy proceedings.

Source: WSJ research

relied on Mr. Cohn to find, manage and provide information about Four Star's investments. "He was the guy who did all the deals and we believed what he told us," says Mr. Garrett.

Mr. Cohn, in a phone interview before he recently began serving a 57-month prison sentence in the Baltimore case, acknowledged the company had made some bad deals. He also said his partners were apprised of the details of all major ventures and wrote the checks to fund them. "I did not control the money," said Mr. Cohn, 49, who has an economics degree from Stanford University and a law degree from the University of California, Davis.

The son of a wealthy San Francisco developer, Mr. Cohn played the role of a hard-charging entrepreneur, former employees and associates say. Around the office, he juggled multiple phone calls and didn't hesitate to dress down subordinates. He favored luxury cars like Lexuses and Infinitis, though he often came to work wearing the same dark pants and old black leather jacket.

In the years after his father's death in the late 1970s, Mr. Cohn largely gave up his law practice to try to expand his family's holdings, which included a scattering of office, retail and hotel properties. Beginning in the late 1980s, local officials in Burlingame, Calif., and Phoenix complained publicly about delinquent tax and utility payments from Cohn-family-owned hotels. In 1991, a family-controlled partnership that owned a historic Tennessee hotel filed for bankruptcy-court protection in Chattanooga. Two years later, Mr. Cohn personally filed for bankruptcy-court protection in San Francisco.

Mr. Anson met Mr. Cohn through a mutual acquaintance in the savings-and-loan industry in the 1980s. Mr. Anson says he was aware of some of Mr. Cohn's business setbacks but his own early investments with Mr. Cohn routinely paid off as promised. "The symphony sounded like the music that was written," says Mr. Anson, who is 61.

In 1991, the two accountants, who had formed a partnership, teamed up with Mr. Cohn on a new venture. Dubbed 900 Capital Services Inc., it aimed to provide financing to small businesses, primarily 900-number providers. Sometimes 900 Capital made them short-term loans with high interest rates. Other times, 900 Capital engaged in "factoring," deals in which it would buy a cash-hungry 900 company's accounts receivable for as little as 60 cents on the dollar. Then it would try to profit by recovering the receivables' full value through major phone carriers such as AT&T Corp. and MCI Inc., which actually billed and collected from consumers.

Former employees and associates say many early factoring deals were profitable. To raise capital for expansion, Messrs. Anson and Garrett invited accounting clients to lend money to 900 Capital. In return, the clients got notes bearing annual interest rates of up to 18%, payable in monthly installments.

There was no advertising to attract new investors, but 900 Capital offered commissions to outside investment advisers who brought in more money. Meanwhile, early investors often boasted of their returns, at dinners and more-casual gatherings at Mr. Anson's Country French-style mansion in the tony Brentwood Park section of Los Angeles.

A 1997 private-placement memo offered those who had lent money to 900 Capital a chance to trade in their notes for ownership units in a new company, Four Star Financial Services. The memo warned that the units weren't registered securities and that holders might lose all of their money.

Many investors say they relied on assurances from Four Star executives that their money was safe. Colin Gilbert, son of Sir Arthur, says Mr. Garrett served as his late father's accountant for years. "I was always informed by Mr. Garrett that, although the interest rate may fluctuate, principal would be sacrosanct," says Mr. Gilbert, a real-estate developer who is now suing Messrs. Anson, Garrett and Cohn, alleging fraud and negligence, in a state court in Los Angeles.

Los Angeles investment adviser Ken Widelitz met Mr. Cohn in 1998. He says Mr. Cohn used a blackboard to give a polished explanation of Four Star's factoring business and showed him a computer system that seemed capable of tracking 900-number-company receivables by area code and past payment problems of individual callers. "It was, I thought, extremely sophisticated," says Mr. Widelitz, who encouraged 18 clients and several members of his own family to invest.

By then, Four Star had diversified far beyond factoring and loans. Around 1996, it paid about \$2 million to acquire a 50% stake in Seattle-based Internet Entertainment Group, described in Four Star's financial statement for that year as "a corporation that provides entertainment via the Internet."

IEG was soon garnering coverage by publications including Time and The Wall Street Journal. Fronted by a brash young entrepreneur named Seth Warshavsky, IEG marketed adult fare, such as videos of actress Pamela Anderson having sex with her then-husband, Motley Crue drummer Tommy Lee.

In published interviews in the late 1990s, Mr. Warshavsky claimed as much as \$50 million in annual revenue, but some former IEG employees say this was exaggerated and the company was heavily reliant on Four Star's financial help. "When IEG wanted to make payroll and people were screaming because there was no money in the payroll account, Seth had to pick up the phone and call Four Star," says Eric Blank, a former lawyer for IEG. Mr. Warshavsky, who is said by former associates to be living in Thailand, couldn't be reached for comment.

At its peak, IEG was yielding \$500,000 a month in payments to Four Star, says Ronald Nessim, the accountants' lawyer. But, hit by lawsuits from creditors, ex-employees and others, IEG was out of business by 2002, leaving Four Star to defend itself in various lawsuits because it was one of IEG's major investors.

Four Star's factoring business was in trouble by the late 1990s. Consumer complaints about rip-offs by 900-number outfits had sparked stiffer regulation. Some phone companies canceled charges for those who complained, making it harder for companies like Four Star to collect on receivables.

#### **Mounting Legal Costs**

Suzanne Tikkanen, Four Star's former senior vice president of finance, says that by 2000, the company was increasingly desperate to raise money to make monthly payments to investors and pay mounting legal costs. She says she and others in the San Francisco office frequently overheard Mr. Cohn and Mr. Anson shouting at each other over the speaker phone. Ms. Tikkanen

testified against the company and Mr. Cohn in the criminal trial in Baltimore. She is suing Four Star's founders, alleging harassment and breach of contract, in a state court in Redwood City, Calif.

Four Star's financial statement for 2000 showed \$143 million in assets. In a Jan. 4, 2001, letter to investors, Mr. Garrett wrote of the company's "steady growth and profitability."

Three weeks later, Mr. Cohn was in the U.S. attorney's office in Baltimore, being questioned about a telemarketing scam Four Star had taken over from a borrower who'd fallen behind on a loan. For prices ranging up to \$199.95, the business offered consumers with poor credit histories a package that was said to include a preapproved credit card. Consumers complained when, instead of a credit card, they got coupons, credit-card applications and other goods of little value, according to court records. On July 10, 2001, a federal grand jury in Baltimore indicted Four Star, Mr. Cohn and five others on multiple related counts of fraud and conspiracy in connection with the scheme.

Four Star's investors heard little about the company's troubles. In a letter to them dated July 3, 2001, the company said it was the subject of a criminal investigation. But it didn't tell investors that it or Mr. Cohn had been indicted until after they were convicted, nearly two years later. Meanwhile investor money continued to flow in. Mr. Anson and Mr. Garrett say Mr. Cohn assured them that he would prevail in court.

In the fall of 2002, with Mr. Cohn awaiting trial, Four Star stopped making monthly payments to investors. It told them its funds were temporarily tied up in a huge transaction involving what was to be a highly profitable sale of assets.

In ensuing months, more letters told of a series of "arbitrage" transactions involving the purported purchase and resale of long-distance time. Investors who asked for details say they were told about transactions involving a Georgia broker, Saudi banks and certificates of deposit, purportedly valued at as much as \$250 million. The CDs' release to Four Star, the company said, had been delayed by the failure of the Argentine bank that held them.

After a six-week trial last year, Mr. Cohn and Four Star were found guilty in Baltimore on 50 fraud and conspiracy charges. Mr. Cohn soon resigned from Four Star. He has appealed his conviction.

Four Star was eventually hit with a \$1 million criminal fine.

Facing pressure from investors who finally had been told about the convictions, Messrs. Anson and Garrett in July last year hired Stutman, Treister and Glatt, a Los Angeles law firm, to look into the long-delayed Argentine deal. In December, they sent investors a letter indicating that, based on their attorneys' investigation, they believed the Argentina transaction and certain related Four Star ventures to be "wholly or partially fictitious," adding that Mr. Cohn had been their source of information. "The fraud was on all of us," the accountants wrote.

In interviews and in letters to investors, Mr. Cohn has maintained that he was misled by lawyers and executives for other parties in those deals, and that the Argentina transaction wasn't big enough to cause all of Four Star's problems.

Richard Marshack, a bankruptcy trustee managing Four Star's assets, says he is investigating

whether, in recent years, the company operated a Ponzi scheme, using money from new investors to pay existing ones. He estimates investors lost between \$89 million and \$134 million but says a precise calculation is still impossible, given the disarray of records and a lack of information from the founders.

Kurt Wolff, who is 78, hopes there is something left to salvage. The retired pastry chef married Mr. Cohn's widowed mother, Ethel, in 1992 and said in an interview he had about \$1 million in his Four Star account when the company collapsed. Mr. Wolff says he and his wife are selling their sprawling Tudor mansion north of San Francisco, both to cut costs and to help finance an appeal of Mr. Cohn's conviction.

"My gut tells me some money will be coming," he said, as his wife cleaned the patio to prepare for a real-estate photographer. "There has to be something there."

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