

BROKING BAD

How Russell Wasendorf Sr. built a \$200 million fraud on a simple lie

The big man of Cedar Falls

SECRET LIFE: Wasendorf, founder of Peregrine Financial, used forgeries and a post-office box to hide his theft. REUTERS/RICK CHASE/WATERLOO COURIER

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First of two parts

A small-town Iowa boy, raised in hard times by a widowed mother, starts a business in the back room of a barber shop before setting out to the big city. He strikes it rich and returns years later to local glory, spending lavishly and savoring his role as the big man in a little town.

It's a real story, but as became clear this summer, a dark thread ran through it. For most of the two-decade life of Peregrine Financial Group, a leading independent futures brokerage, founder and chief executive Russell Wasendorf Sr. was taking hundreds of millions of dollars of his customers' money to cover losses and live large.

BROKING BAD THE BIG MAN OF CEDAR FALLS



PASTORAL CARE: The house of pastor Linda Livingston in Marion, Iowa, where Wasendorf hopes to stay if he is released from federal custody.

REUTERS/JEFF HAYNES

His dual life came to light after Wasendorf, 64, tried to commit suicide outside his headquarters in July. Authorities discovered a four-page confession letter describing how he used a post-office box, a scanner and basic software to hide his theft for years. The Commodity Futures Trading Commission accused him of making off with more than \$200 million of customer money. Last week, he pleaded guilty to mail fraud, lying to regulators and embezzling customer funds, crimes that could put him in jail for 50 years.

Interviews with dozens of former employees, colleagues and associates, as well as court filings and company documents seen by Reuters, offer the most complete account yet of Wasendorf and his career. He is a man who came from little, made it big and then dipped ever deeper into customer

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longtime counsel to Peregrine

accounts to finance a facade of seemingly unlimited wealth.

Part of Wasendorf's life was an open book: He brought celebrity speakers such as Ted Koppel to industry events and wrote columns for a glossy magazine he owned. Toward the end of last decade, he relocated his headquarters from Chicago back to Cedar Falls, bought a private jet and built a \$24 million state-of-the-art office, touting the move as a template for revitalizing small-town America.

Less known were the personal tensions he faced, including a split with a brother, two divorces, a last-minute mystery wedding in Las Vegas and seething resentment against establishment rivals in Chicago. His pastor says Wasendorf knew his ruse was doomed several years before it unraveled. A rift emerged with his only son, Russ Jr., who warned the Iowa shift was an expensive folly - and prepared this summer to move to Australia.

“Russ Jr. told him it was a mistake - that it was a mistake to spend \$24 million on the building and a mistake to buy that jet,” said Nicholas Iavarone, Russ Jr.'s lawyer and a longtime counsel to Peregrine. “It didn't matter.... He wanted to go back to Cedar Falls to be the big man.”

Today, Wasendorf sits in solitary confinement, and under suicide watch, at Linn

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County Correctional Facility in Cedar Rapids, Iowa. Authorities have found only \$181 million of an estimated \$400 million in customer funds Peregrine was supposed to have on hand.

Wasendorf and his lawyer, a public defender, didn't respond to requests for comment. Beyond the confession letter and the plea agreement, neither has made any public comments to the media.

The youngest son of a meatpacking plant foreman, Russell Ralph Wasendorf was born in 1948, named after a pastor and his son who offered the Wasendorfs shelter in their attic when money grew tight.

Arthur Wasendorf died when his son was in kindergarten. Russell's widowed mother, Ida, landed a job in marketing for a local securities broker to keep the family fed.

Wasendorf gravitated toward the arts. At high school in Marion, Iowa, he performed in plays at local churches. While at the University of Northern Iowa, he joined a local artist collective, learned to use audio-visual equipment and worked on documentaries about New Mexico's Pueblo Indians. That led to "a short, but successful career in the motion picture business" prior to entering the futures industry, according to a note he published in the glossy magazine he later founded, *Stocks, Futures and Options*, or SFO.

GROWING GOLD

The peak came in 1974, two years after he left university: a 20-minute documentary on soybeans titled "The Gold That Grows," which later won an award from the Council on International Non-Theatrical Events.

At the time, Wasendorf was in an early job as an advertising and production manager for the American Soybean Association. The film was made to tell farmers how their dues were being spent to bolster exports, including shots of soybean meal being fed to chickens in Japan.

His first marriage was brief. He married Susan Richardson in 1969 while both



SUICIDE WATCH: The University of Iowa Hospital and Clinics. Wasendorf was taken here after he tried to kill himself in July. **REUTERS/STEPHEN MALLY**

were students at the University of Northern Iowa, according to an announcement in the *Cedar Rapids Gazette*.

The couple had one son, Russell Jr., and later divorced. Richardson, who has since remarried and lives in Florida, declined to comment.

It was one of several family splits. Wasendorf maintained little contact with his siblings in recent years, including older brother Lewis, who lives just 80 miles from Cedar Falls.

"Russ chose to kind of divorce himself from the rest of the family. We respect his wishes," said one family member. "He was always flying around the country, around the world... We didn't want to live that lifestyle."

In 1976, Wasendorf married Connie

Brandhorst. Russ Jr. was the ring bearer. Connie, who worked at a John Deere plant, became a second mother to young Russell, say people who know the family.

Wasendorf was now working in the advertising and sales department of a local commodities magazine owned by Merrill J. Oster, a futures-industry newsman whom the Peregrine founder admired. He worked on promotional videos and trader-education programs. The position offered entry to a world Wasendorf longed for: the Chicago commodities trading floor.

By 1980, Wasendorf left to start up a rival advisory firm and newsletter. Co-workers believed that Wasendorf and another staffer had taken a copy of Oster's client list with them, according to a former employee. Oster declined to comment.

His new consulting business, which provided research and futures-trading advice, began in the back room of a local barber shop. "He was in my chair one day, saying that



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he was starting up a business and needed space,” said barber Ron Welper, who owned Hair Unlimited on Main Street. Wasendorf moved in a couple of desks, a computer and a phone, and got to work contacting would-be clients. A year or so later, he moved out and up.

Wasendorf bought a small brokerage, Dana Futures of Iowa, in 1985. As an “introducing broker,” he was responsible for rustling up business, helping arrange commodity-futures trades by farmers or small-scale speculators. Futures allow a seller or buyer to lock in a price for, say, soybeans at an agreed future date. Wasendorf would pass along those trades to futures commission merchants – the regulated middlemen responsible for executing deals on exchanges.

The business was launched as many farmers were looking to protect their operations amid plummeting corn prices and a sharp downturn in the farm economy. Wasendorf later bragged on his company’s website that he made his customers rich by anticipating the 1987 stock-market crash and advising them to sell ahead of it.

By the early 1990s, he began moving staff to offices on LaSalle Street, a block from the Chicago Board of Trade, center of agricultural futures trading for 150 years. Soon, Wasendorf moved upmarket to broker his clients’ trades as a futures-commission merchant, collecting fees and earning interest on their collateral. He opened Peregrine Financial Group in 1992. The company became commonly known as PFG, or PFGBest.

The firm, with offices in Cedar Falls and Chicago, had just \$2 million in customer funds for its first few years. Yet the fraud commenced soon after PFG Best opened, according to Wasendorf’s confession letter.

In the winter of 1993, after a routine audit, a Commodity Futures Trading Commission investigator named Robert Agnew began inquiring into a possible violation of rules on how Peregrine was investing customer money – something that took Wasen-

“You could not have sent me a more clear message of the low regard you hold me and my firm.”

Russell Wasendorf Sr.

in a letter to Jack Sander, former chairman of the Chicago Mercantile Exchange in Oct. 2000

dorf by surprise, he wrote in his letter.

What specifically caught Agnew’s attention isn’t known. Agnew could not be reached for comment. A CFTC spokesman declined to comment.

Wasendorf said Agnew gave him a copy of the rules Peregrine was allegedly violating; the broker replied by saying the rules were outdated, making the investigator “livid,” according to the letter.

Agnew and his team then “harassed” Wasendorf, conducting six audits over five months until the agency found a “technical violation” that forced Peregrine to raise more capital.

CHEATING FATE

Legal fees mounted, according to his confession letter, and the need to keep more cash on hand sparked financial trouble.

“I had no access to additional capital and I was forced into a difficult decision: Should I go out of business or cheat?” the letter states. “I guess my ego was too big to admit failure. So I cheated, I falsified the very core of the financial documents of PFG, the Bank Statements.”

Peregrine got a big break in 1995. Regulators at the National Futures Association found that managers had used bad checks to falsely bulk up capital at brokerage First Commercial Financial Group. The NFA forced First Commercial to move its customers to other firms with a history of working with small independent brokers.

It was a common move: help clients of a troubled brokerage quickly resume trading by simply shifting their accounts to a similar shop.

Peregrine was one of at least two firms entrusted with the clients. It kept some of First Commercial’s brokers, too. But trouble followed. In 1996, the NFA fined these brokers and Peregrine for using “false and deceptive” promotional material.

The NFA also discovered that Peregrine failed to properly calculate how much money was in its customer accounts and to keep them properly segregated. The brokerage settled the matter by paying a \$75,000 fine without admitting or denying the allegations.

It was a pattern that Peregrine would follow at least twice more: take over a troubled firm that the NFA later penalized for lax oversight.

The NFA declined to comment on why it did not consider such acquisitions and violations to be a possible red flag.

By the late 1990s, Peregrine was a family affair. Connie worked in the personnel department. Russ Jr. graduated from the University of Iowa with a finance degree, studied Spanish and worked as a liaison between the Chicago Mercantile Exchange and regulators in Mexico over the development of Mexican peso futures. Then, in 1998, he joined Peregrine as head of the computer team. His job: build and launch the company’s online trading system.

Wasendorf Sr. was launching or building up a variety of different companies – a securities brokerage in 2001, a hedge fund in 2004, a publishing house and a construction company in 2007. Some were flops. All, Wasendorf said later in his confession letter, were part of his attempt to bring in new revenue to repay the money he had been stealing from customers.

His strangest bet ultimately became the most profitable, at least on paper.

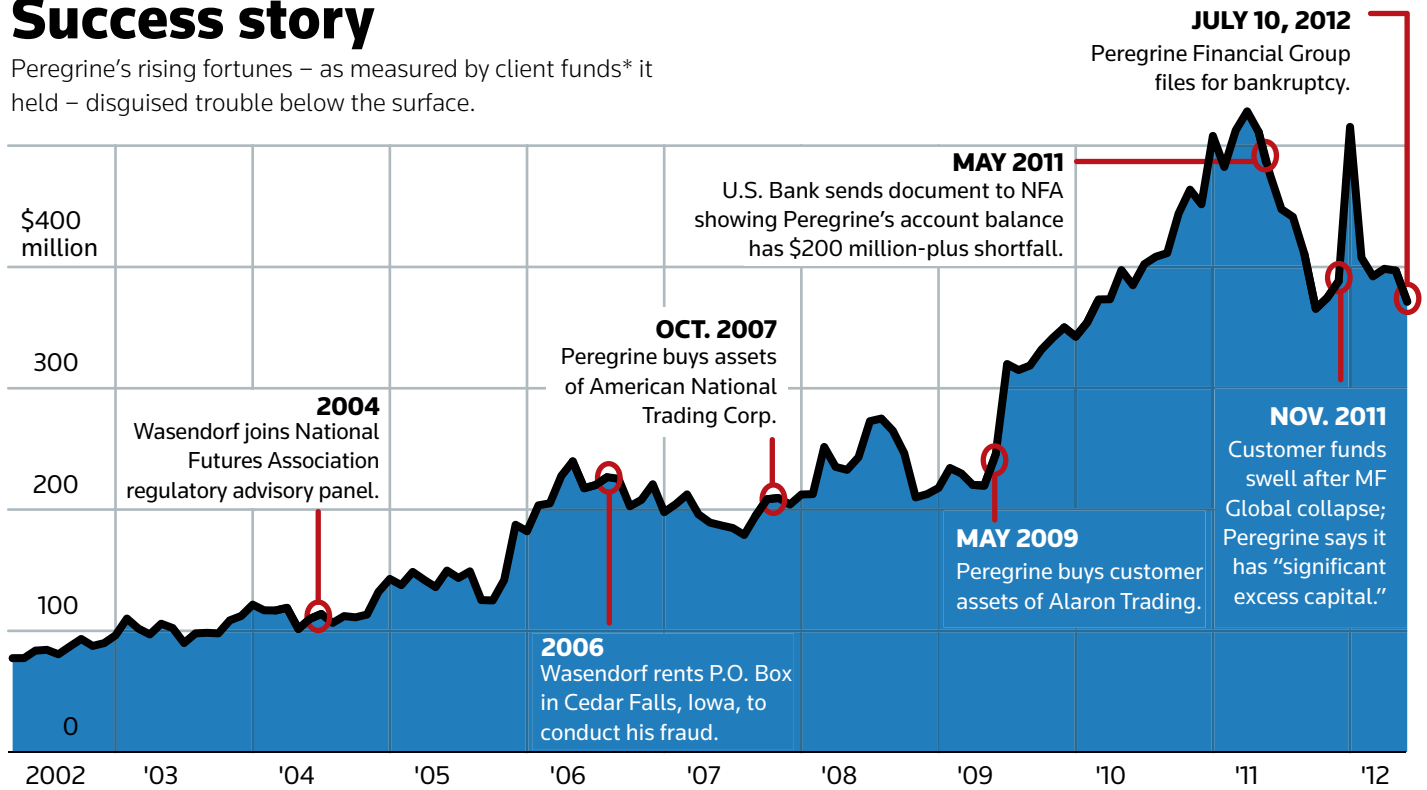
Alexander Hergan, a founding member of the Chicago Board Options Exchange, ap-



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Success story

Peregrine's rising fortunes – as measured by client funds* it held – disguised trouble below the surface.



*Segregated funds

Source: Commodity Futures Trading Commission data

proached Wasendorf in 1998 with a proposition: become a largely silent partner in a Romanian real estate venture. They knew each other from Chicago trading circles, according to Hergan. Wasendorf invested half a million dollars in the property development firm, Avrig 35 Group, and it flourished.

Peregrine rose into the ranks of the country's biggest independent brokers. According to data Peregrine submitted to regulators, customer funds nearly tripled from around \$70 million in 2002 to over \$200 million in 2006 – less than a tenth as much as the big Wall Street banks, but enough for Wasendorf to achieve prominence.

He became an outspoken proponent of a merger between the two biggest Chicago futures exchanges. His magazine sponsored big-name speakers at industry events, including General Tommy Franks and former First Lady Barbara Bush.

But in Chicago, where Peregrine was

now based, Wasendorf was still seen as something of an upstart next to decades-old family-owned brokers. And he was not always granted the respect he felt he deserved.

"You could have not sent me a more clear message of the low regard you hold me and my firm," Wasendorf wrote in a letter seen by Reuters, dated October 20, 2000, to Jack Sandner, a former chairman of the Chicago Mercantile Exchange who was running a brokerage that had cleared PFG's trades. "I guess I should have taken the hint when you refused to take my phone calls or when you refused to write a foreword in my latest book."

Wasendorf felt Sandner's firm was overcharging him, according to the letter. Sandner told Reuters that the letter speaks for itself, and declined to comment further.

Wasendorf also joined, in 2004, an advisory panel at the NFA, tasked with giving feedback to the regulator about pro-

posals that affect the industry.

The agency, which regulates smaller brokers like Peregrine, would later be faulted for having missed two decades of fraud. The post would have offered him a first-hand look at – and a say in – rule changes that could impact his business. It isn't clear whether this vantage point abetted the alleged fraud, however.

BOX OF SECRETS

An NFA spokeswoman declined to comment on Wasendorf's role on the panel. The association sought to distance itself from Wasendorf in a July 30 letter from its president, Dan Roth, to U.S. Sen. Tom Harkin of Iowa. Roth wrote that the panel had no decision-making power, and that Wasendorf had never attended any NFA board meetings or interacted with board members in their official capacities.

It was in 2006 that Wasendorf first rent-

ed Post Office Box No. 706 in Cedar Falls. Wasendorf began forging monthly bank statements that Peregrine received from U.S. Bank for an account it held there, and replacing the bank's real return address with the address of Box 706. The aim, according to his plea agreement, was "to deceive auditors into believing PO Box 706 was US Bank's mailing address."

When the regulator sent requests to U.S. Bank to verify the funds held in Peregrine's accounts, Wasendorf simply picked up the letters from Box 706, forged bank statements and sent them to the regulator with the PO Box as the return address. The regulator doesn't appear to have recognized the ruse.

In 2007, trading volume was rising and the firm was earning healthy interest income on the funds it held for clients. Wasendorf scooped up another wounded firm, American National Trading Corp., a Los Angeles-based foreign-exchange brokerage with some \$25 million in client funds. The Avrig 35 Group in Romania was valued by investment bank UBS at more than \$1 billion ahead of an expected public offering. On paper, Wasendorf's stake in the real estate venture was worth at least \$150 million.

Emboldened, Wasendorf made a decision that he hoped would cement his legacy: moving his headquarters, and dozens of staff, back to the town where he had founded it, Cedar Falls (pop. 40,000).

Iowa was home for Wasendorf. Though he bought a \$1 million condominium in Chicago in 2003, he never sold his house in Cedar Falls, more than 250 miles away. He expanded it instead. He would host summer barbecues for the staff there, featuring steak and sweet corn.

At a jungle-themed party, the Wasendorfs drove workers' children around the property so they could grab stuffed animals dangling from trees, said Jackie Reitz, who ran a one-woman wealth-management branch for the brokerage in Arizona.

Back home

Wasendorf planned a \$24 million headquarters in his hometown of Cedar Falls, Iowa.



"I thought that they were an amazing company," Reitz said.

Wasendorf found the perfect site for his new headquarters a short walk from the greens at Beaver Hills Country Club. But the 22.2-acre wooded grove wasn't zoned for the kind of use Peregrine sought. Wasendorf sent his architects to the county to get that changed. He was rebuffed.

"You know how sometimes there are people from the city who come in and think they own everything and can do anything? It was like that," said Grant Veeder, Black Hawk County's auditor.

Wasendorf held public meetings at the country club and library, hinting he'd take his 100 new jobs to friendlier environs. He told local media he would build a small airline to serve nearby Waterloo Regional Airport, so his executives could easily travel cross-country.

At a Black Hawk County Board of Supervisors hearing on April 27, 2007, supporters turned out in droves. Area economic development officials sported "Say Yes to PFG!" buttons and waved a petition bearing more than 1,300 signatures and a letter of support from six state lawmakers.

Think about the boon to the community,

Wasendorf urged the crowd, with dozens of new residents buying homes and shopping on Main Street. The board voted in favor of the rezoning, 5 to 0.

Privately, Peregrine executives and Russ Jr. were skeptical about the move, according to Iavarone, Russ Jr.'s attorney.

The airport in Waterloo had only two direct flights a day to Chicago and none to New York. Chicagoans were reluctant to uproot. Wasendorf shrugged off such concerns, said Iavarone, who represented Peregrine in legal matters for almost 20 years. The CEO bought a jet with a long-time friend in Cedar Falls and hired private pilots.

Wasendorf had held out hope that he could make good on the money that he had pilfered, according to his pastor, Linda Livingston of the Ascension Lutheran Church. But the American financial crisis changed that.

"In 2008, he thought that would still be possible. And then the crash happened," said Livingston. "And that was the last time that it appeared that there would ever be a possibility that he could actually replace and repay everything that has been misappropriated."

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Next: Peregrine falls

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