

Financially Speaking

With Trisha Arndt, CFP®

The Ponzi Scheme is Alive and Well

Unless you were hiding under a rock somewhere last fall you likely heard about the Bernard Madoff scandal that shook the financial industry (an industry that was already in the midst of a firestorm of bad news). Through direct investments and various feeder entities Bernard Madoff managed to abscond with literally billions of dollars from investors. Even the Overture Center had significant money “invested” with Mr. Madoff – and, despite having closed the account before the scandal broke, may still lose some of it.

As hard as it is to believe, Bernard Madoff pulled off one of the oldest, most simplistic scams in the book with some of the most sophisticated investors in the world. He was running a basic Ponzi scheme.

In simplest terms, a Ponzi scheme is based on the idea of robbing Peter to pay Paul. It earned its name from Charles Ponzi, who, in the 1920s, stole millions from more than 40,000 people in New England in what is believed to be the first and most well-known of these crimes. The elements of Ponzi’s original scam are markers for similar swindles today.

Ponzi told investors that he could take advantage of the differences in U.S. and foreign currencies used to buy and sell international mail coupons. He claimed that he could provide a 40-percent return in only 90 days, which was dramatically greater return than the 5-percent return investors could earn in a bank savings account. Investors jumped on the idea, inundating Ponzi with funds. He became a well-known Boston millionaire within six months.

Unfortunately, even the simplest financial analysis would have illustrated that his operation was running at a large loss. While new investors kept money coming in, that new money was the only source Ponzi had to pay off existing investors, as he made no effort to generate legitimate profits. Indeed, he only purchased \$30 worth of the international mail coupons he said he was working with, and he paid off a handful of early investors to make his scheme appear legitimate.

There are signs to watch for and steps that all investors should take to try to avoid becoming a victim of the next Ponzi imitator.

Common sense is the best defense that you can have. If it sounds too good to be true, it probably is. And if the person “introducing” you to the opportunity is using high pressure sales tactics with the hope of rushing you into a decision then you should walk away. Be wary of “once-in-a-lifetime” opportunities that are only “available for a very limited time”. Remember that legitimate investment opportunities are rarely that fleeting

and take the time to do your research and be comfortable with where your money is going.

You should avoid writing investment checks payable directly to an investment advisor or a small, unknown company. Most legitimate investment professionals are going to custody client assets with an institution that you would recognize and/or be able to easily obtain information about. Investment checks should generally be made payable to that institution so that the money can be properly invested in the segregated account established for you.

Make sure to research who you are investing with as well. Check out the websites of the parties you are working with and know what various credentials stand for so that you can recognize if they are really meaningful or just a series of letters that someone is paying to put behind their name. AARP offers a resource that explains various financial designations; find it by going to www.aarp.org and typing “understanding financial credentials” into the Search field.

Ultimately I’m still old fashioned when it comes to issues of trust and I believe that the best way to find a financial professional to work with is by relying on recommendations from friends, family and other professionals, especially if they have a long-standing relationship with the individual or firm you are considering. Feel free to bring a trusted friend or professional to the initial interview meeting with you – I personally find that beneficial for both prospective clients and myself as it helps to make sure that everyone is on the same page with goals and objectives.

Your financial future is in your control—you decide who gains access to your hard-earned dollars—so be sure to choose wisely. You’ll find that most financial professionals not only want to assist you with your needs, but they also want to educate you so you can make the right decisions for your situation. The time you put into vetting potential professional partners is one investment that can legitimately promise a great return.

Have a financial question or a topic that you’d like to see a column on? Email me at Trisha@wealthstrategies.biz.

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