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Ponzi Schemes

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The Fraudulent World of Schemers

In today's financial world, Ponzi schemes are more prevalent. What is a Ponzi scheme? By definition, "A Ponzi scheme is an investment fraud that involves the payment of purported returns to existing investors from funds contributed by new investors".[1] As often as this case may seem, many people become involved in Ponzi schemes only to lose more and more money. However, the investor of a scheme is usually unaware of what it is he or she is investing in. The investor only hears and then sees big return, but soon he or she comes to realize their entire life savings has vanished. The people that fall to Ponzi schemes also perceive the scheme in a way that he or she is looking to maximize return. Naïve people in fall to many types of these schemes. In interviews of those victimized, Ponzi scheme stories are usually told through the investor's point of view, but what about the view of the schemer himself. The creator or developer of a fresh Ponzi scheme, in doing so, most certainly envisions opportunity as well. Projecting money in return, he or she works creatively towards achieving the monetary status he or she has always wanted. Nonetheless, how does the schemer make the Ponzi scheme look so attractive?

Many investors over look the red flags of Ponzi schemes. These red flags make investments look overly incredibility attractive to the investor. Instructing the naïve to investor in the scheme, the creator of the scheme makes these red flags interesting and tells investors that the return cannot be found elsewhere.

So, what are the red flags of a Ponzi scheme? The red flags of schemes include: "high return with little of no risk, overly consistent returns, unregistered

[1] https://www.sec.gov/answers/ponzi.htm

investments, and complex strategies etc".[2] High return with little or no risk is virtually impossible. In order to obtain a high return, the risk is much greater. This is the theory of risk versus return: the higher the risk the higher the return. The lower the risk the lower the return. An overly consistent return is a red flag because the risk is high and the market is bound to change more frequently making the return more volatile. Complex strategies in an investment, the shear complexity of the workings of the investment, are something an investor should stay well clear of especially if the investor does not understand the investment itself. The schemer makes an abnormal return this way, making the investment sound and look attractive. The schemer does not care that the investor is losing money because the schemer is only concerned about him or herself. Most investors caught in the complexity of investment, are naïve: "He (the schemer) is counting on other people's gullibility or blindness so that he can profit from his dishonesty. In other words, he is shifting his primary focus away from the facts relevant to the conduct of his business and towards the deception of others".[3] This is an ethical issue, which is the case in many schemes in today's investment world. Business Ethics is completely lost in the schemers philosophical thinking and beliefs concerning himself and the people he seeks to involve. The schemer is looks towards self, first, and is caught up in self-interest, selfishness, rather than seeking the best of the investor; Rather than seeking the best for the investor and subsequently earning a larger fee. Ethically, delaying gratification and selfishness seems to be the problems on the part of the

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[2] https://www.sec.gov/answers/ponzi.htm

[3] Locke, Edwin A., and Jaana Woiceshyn. *Why Businessmen Should Be Honest: The Argument from Rational Egoism*. Vol. 16. Wiley, 1995. Accessed March 12, 2016. Jstor.

schemer. The fiduciary responsibility in a business ethics point of view is lost in self-interest: "The problem with cynical egoism is that its advocacy of self-interest is only a pretense…To act in one's own actual interest requires that one identify the actions necessary to attain one's long range happiness and survival".[4] In the view of Christianity, there is a loss of morality regarding the schemer against the gullible investor. In the face of morality, even if one is Christian or not, it requires a well-developed conscience, which in some cases take a lifetime. However, not having a well-developed conscience is not an excuse for stealing people's hard earned money. A schemer's thinking is skewed. He believes himself to be above others. He reasons that he deserves the money simply because of "who he is". His confidence that the scheme is, in a criminal sense not a crime, and that of I could never commit a crime, and if discovered, there would be no repercussions.

The sense of not getting caught criminally is called the *Not me Fallacy Theory:* "The false image of crime and criminals leads to something worse: a false image of oneself. … It is the illusion that we could never do crime".[5] The schemer continually tells himself that he is a good person. In telling himself this, he persuades himself overtime, inducing a mental state that encourages an altered mindset. He soon perceives himself as a "do-gooder" above the law; This helps him sleep at night. This mind-set convinces him that he is helping people with their investments, but in all reality he is stealing the investors entire life savings. "Some think they will never get

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[4] Locke, Edwin A., and Jaana Woiceshyn. *Why Businessmen Should Be Honest: The Argument from Rational Egoism*. Vol. 16. Wiley, 1995. Accessed March 12, 2016. Jstor.

[5] http://www.sagepub.com/sites/default/files/upm-binaries/32121_1.pdf

caught because he or she could never commit the crime, therefore since they are not "committing a crime" they cannot get caught.

Interestingly, Ponzi schemers do worry about getting caught when the scheme is first started. In fact, it is known that and they can't live with themselves for the first few weeks because they know what they have conceived is wrong. Sleep, something our bodies need, becomes illusive and daily habits become altered. The schemer is left awake at night wondering and worrying about getting caught. It is this gradual progression as the scheme continues, that the schemer's mindset becomes transformed. Until gradually they come to believe they are not committing a crime. This is when the *Not-Me Fallacy c*omes into play. At this point, schemers believe they can never be caught.

However, there is a portion of schemers that are different. These schemers almost hope to get caught because they are tired of the lies. The lies must continue in order for the scheme to continue. That is when they mentally tire. Lies upon lies are difficult to keep up with and the lying takes a toll on the mind. One must remember every single lies that was told to each individual person." [6]It almost becomes a point where the schemer has to write down every lie that was told to each person. With this being said, there are two types of schemers.

One type of schemer is one that comes from a family owned business or owns his or her own business. This person implements schemes into the business plan. Schemers with their own business are usually afraid of failure. When the business they have begins to fail, they will do anything possible to keep the business going.

[6] Chris Vernon phone call on 3-17-16

This is where the schemes start. The scheme and lies become so much of the schemers' priority, that the business becomes secondary; They can no longer keep the two separate. Since usually these are people with family businesses and are family oriented, trust runs high. Customers, especially regular customers, entrust money to these businesses. Yet, the scheme that was created to keep the business going will eventually crash and burn and immediately lose customer's trust.

The second type of schemer is the narcissistic schemer. He or she is usually out to please someone. These schemers love attention and want to have many friends. They also have bold personalities and appear somewhat cocky, but loveable. Social and confident, they think very highly of themselves. Their thinking involves no self-doubt and they rarely admit that there are any areas in which improvement is needed. Rather, they feel they are above every other person they encounter. Ponzi schemers, in general, are incredibly different than normal criminals. Although these people steal thousands, even billions of dollars, they emphatically believe they are doing good acts.

In considering this gradual progression and change of mindset, it appears to lead to a type of addiction. With the growing number of people involved and the number of dollars generated, a certain euphoria or Adeline high may be. People creating these schemes are addicted to the feelings of acceptance socially, and emotionally. They see the growing numbers and their eyes turn into dollar signs, literally. The more money the scheme creates, the more they become addicted to the scheming and the more damage they inflict; Investors are pilfered out of their entire life savings. This addictive behavior is reinforced and leads to assuming the role of the big shot in the family or in a group of friends; They become addictive to the lifestyle it brings. Since they are always seen to have money, their egos are large and they do not wish to disappoint anyone. The addiction causes schemers to become fiercely competitive to remain in this position, because it becomes their definition of self.

Living the lifestyle of a Ponzi scheme requires luxurious living. Although, monetarily, the Bernie Madoff scam occurring in the northern United States, is presently the most well-known and far reaching scheme, Florida reports the highest number of Ponzi schemes in the nation at this time.[7] This is to be believed because there are more retired people in the state than another other in the country. Older people are thought of as gullible and naïve because they will trust most anyone. Grandma and Grandpa think every person they encounter is a nice person: "As is evident, the most popular group targeted by Ponzi scheme artists is the elderly or retired individual. In some cases, elderly victims were also members of the other target groups, such as religious faction or ethnic group. Religious affinity groups were targeted nearly as much as the elderly, followed by various ethnic groups".[8] The schemer's personality also reinforces this "nice person" fallacy. In addition, Florida supports the lifestyle of a schemer, especially wealthy areas such as Naples, Miami, and parts of Tampa. In addition to the elderly population, there is also a large number of younger people living and working in the tourist industry in Florida. Young people with young families are gullible and naïve as well. Young people are

[7] http://www.ponzitracker.com/ponzi-scheme-map/

[8] Marquet International. "Marquet Report on Ponzi Schemes." June 2, 2011, 1-34. Accessed March 22, 2016.

also fall for schemers due to gullibility. Gullibility is a quality that the crook most depends upon for the scheme to succeed.

“Based upon the Marquet Report on Ponzi Schemes, which was published in 2011, the most common types of schemes involve hedge funds, then real estate, followed by promissory notes. Since Ponzi schemes promise investors a higher rate of return, it is evident one must wonder what rates Ponzi schemes offer. The Marquet reported that the shorter the duration of the scheme, the higher the rate of return; therefore, the longer the duration of the scheme, the lower the return. However, returns were still abnormally high compared to the market. This bring up age groups. At what age is a schemer likely to create a Ponzi scheme? The average age that one is likely to begin a scheming career is 45 years old. The Marquet reportedly tested 329 cases and out of all of them the perpetrator was between 45 and 50 years of age: “As the chart demonstrated, the 50-59 age group accounted for the greatest number of Ponzi schemes cases. However, the 70-79 age group accounted for the greater total fraud and the highest average Ponzi scheme. This fact is clearly due to the inclusion of the Madoff case, which skews everything higher in the 70s age group”.[9] Much of the data is skewed in this report because of the Madoff case. The youngest out of all the cases was 21 and the Ponzi scheme was located in Athens, GA. The young man stole over $42 million dollars. Lastly, the gender of the scheme artist, out of all 329 cases the Marquet Report found that women started 24 of the schemes. “The largest alleged scheme perpetrated by a

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[9] Marquet International. "Marquet Report on Ponzi Schemes." June 2, 2011, 1-34. Accessed March 22, 2016.

female involves 66-year-old St. Augustine, Florida based Lydia I. Cladek, who convinces at least 1,000 apparent victims to invest more than $113 million in fraudulent promissory notes by offering a "guaranteed" return of as much as 20% ... Cladek's scheme allegedly spanned an approximate five year period until shortly before she was indicted on 14 felony counts including wire fraud, mail fraud, conspiracy to commit wire fraud and mail fraud in November 2010".[10]"[11]

Based on the study by the Marquet report in 2011, in the state of Florida, there are forty-eight schemes reported. These schemes comprise a total loss of $1,698,560,000. 00. Just recently on April 20, 2015 in Naples, Florida, a man named Dorian Garcia ran a 4.7 million dollar Ponzi scheme. He involved 80 investors in a scheme disguised as three different companies; "Garcia persuaded investors by showing them falsified documents suggesting his companies had large cash reserves, the commission said. On two separate occasions, Garcia sent E-Trade account balance sheets to potential investors claiming reserves of $13 million and $8.7 million, respectively. In reality, Garcia only had one E-Trade account, which had a balance of $25.31, according to the complaint".[12] Garcia falsified documents such as financial statements and sent them to his investors showing his companies falsified inflated worth. The money he obtained from investors was deposited neatly into his personal accounts, which he used to purchase jewelry and art. In addition,

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[10] Marquet International. "Marquet Report on Ponzi Schemes." June 2, 2011, 1-34. Accessed March 22, 2016.

[11] Marquet International. "Marquet Report on Ponzi Schemes." June 2, 2011, 1-34. Accessed March 22, 2016.

[12] http://www.naplesnews.com/news/crime/feds-naples-man-ran-47-million-ponzi-scheme-ep-1046638809-338032781.html

money from investors was traced to personal cash transfers. Garcia obtained degrees in Florida in the finance field. He claims he allegedly wanted to be part of a hedge fund. He began his own company and added, "several characteristics he infuses into the company, including "loyalty," "morality," and "ethicality."[13] His claims of loyalty, morality, and ethics were added his company's founding mandate. Physiologically, this was a lie from the beginning. Garcia lost a form of conscience and morals when he started stealing people's money. He also falsified financials to show that his companies were making money, when in actuality he was pocketing it. He wanted to make his investors believe that the company was solvent and growing, when in reality the companies were plummeting. Garcia had no right saying he added ethics to his business practices because stealing money from investors was unethical from the beginning. He relied on investor's vulnerability regarding investments and investment opportunity. In the end, Garcia did not face any criminal charges, however all of his assets were frozen, he can never trade on the futures market again, and he was ordered to stop falsifying financial statements. In my opinion, he should have reimbursed all 80 investors fully. Although approximately 2.1 million dollars was returned, large portions of the funds were not recovered. Garcia's behavior should have landed him in prison for he started an illegal investment fund, stole millions from people, and lied on many financial statements. Garcia was ethically and morally corrupt from the beginning. He was afraid he would not succeed and stole money from people to create success. He was completely selfish.

[13] http://www.naplesnews.com/news/crime/feds-naples-man-ran-47-million-ponzi-scheme-ep-1046638809-338032781.html

Over all, the psychology of a Ponzi schemer is corrupt. The schemer trusts in the vulnerability and naiveté of the people who invest their hard earned money. Schemers rely on these peoples' lack of perception to perceive the red flags of a scheme. Schemers are usually extraordinary people. They have strong, bold personalities, and are exceptionally nice and convincing. Targets for typical Ponzi schemes are the elderly, those on fixed incomes who are intrigued with the possibility of abnormally high returns, and religious groups, both trusting and vulnerable. Teaching the red flags of these schemes and instructing people to stay away from abnormal returns, complex strategies, and schemes with virtually no risk is necessary. There has to be a point where the scheme will collapse. At this point, the schemer gets caught. Some of which hope the point comes so the lies can come to an end. Lying continuously takes a toll on the schemer's life because they know they are wrong, and what they are doing is wrong. The craving of social, emotional, and financial recognition feed Ponzi schemers. Psychologically, schemers evolve, becoming financial liars and most eventually are brought to justice; Ultimately the schemer cannot keep up with the lies and hopes to be caught. Continuing to educate the vulnerable group of society seems the best course of action at this time. Ponzi schemers will always be in the world. Understanding the nature of schemers and their schemes, assist in avoiding victimization. Avoiding Ponzi schemes at all costs is the best course of action.