How To Spot A Ponzi Scheme

(NAPSA)—The promise of guaranteed returns, consistent gains when the rest of the market is volatile, and complex or secret investment strategies—these are all warning signs of a Ponzi scheme. Learning to recognize them, and doing a little homework, could help you avoid getting conned.

"It may appear as though new investment scams are invented every day," says Gerri Walsh, president of the FINRA Investor Education Foundation. "But most boil down to a few common patterns."

What changes is the "hook"—the lie a criminal tells to make the scheme believable. For Ponzi schemes, it's often something an investor can't get anywhere else, Walsh said, such as abnormally high returns.

"You have to remember that these are professionals who are very experienced in making 'too good to be true' sound good enough to be real," she said.

How Ponzi schemes work. Rather than investing or managing money as promised, a central fraudster or "hub" con collects money from new investors and uses it to pay earlier-stage investors. This is the strategy Charles Ponzi used for his infamous postage-stamp scam of the 1920s.

As with the original, all Ponzi schemes require a steady stream of incoming cash to stay afloat. They fall apart when new investors can't be found or when too many investors attempt to get their money out at the same time.

Here are the key warning signs of these scams:

• **Guarantees**: Be suspect of anyone who guarantees that an investment will make money. All investments carry some degree of risk.

• **Unregistered products or sellers**: Many investment scams involve unlicensed individuals selling unregistered securities—ranging from stocks, bonds, notes, hedge funds, oil or gas deals or fictitious instruments, such as prime bank investments. Before investing, ask if the seller is registered with the Financial Industry Regulatory Authority (FINRA), your state securities regulator or the U.S. Securities and Exchange Commission (SEC). Also ask if the investment is registered with your state or the SEC. Then, independently verify the information.

• **Consistent returns—no matter what**: Any investment that consistently goes up month after month should raise suspicions, especially during turbulent times. Even the most stable investments can experience hiccups once in a while.

• **Complex strategies**: Legitimate professionals should be able to explain clearly what they are doing. It is critical that you fully understand any investment you're seriously considering.

• **Missing documentation**: If someone tries to sell you a security with no documentation—that is, no prospectus in the case of a stock or mutual fund, and no offering circular in the case of a bond—he or she may be selling unregistered securities. The same is true of stocks without stock symbols.

• **Adviser as custodian**: Be sure you know who holds your assets. For instance, is the investment adviser also the custodian of your assets? Or is there an independent third-party custodian? It can be easier for fraud to occur if an adviser is also the custodian of the assets and keeper of the accounts.

For more information on spotting and avoiding investment fraud, visit the FINRA Foundation's fraud-fighting website, www.SaveAndInvest.org/LearnMore.