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PONZI SCHEME FREQUENTLY ASKED QUESTIONS **(With Particular Reference To Bernard C. Madoff Investment Securities, LLC)**

Question: *What is a Ponzi scheme?*

Answer: A Ponzi scheme is a form of investment fraud in which the funds obtained from later investors are either diverted to the promoter's pocket or used by the promoter to pay off earlier investors in order to maintain the illusion that the investment is legitimate. The promoter has not merely lost the investor's money; there usually was never any investment at all. The Madoff investments appear to have been a classic Ponzi scheme.

Question: *How do I recover my investment if I have been victimized by Madoff's Ponzi scheme?*

Answer: It is rare for investors in a Ponzi scheme to recover all or even most of their losses, because the funds usually have been dissipated by the time the scheme is revealed. However, there are avenues for victims to recover some of their losses. In the case of Madoff's scheme, it appears that there are several potential sources of recovery:

- (1) Personal assets Madoff has accumulated (expensive homes, artwork, yachts, hidden bank or securities accounts);
- (2) Assets of individuals or companies found to have assisted Madoff in his fraud (the SEC is investigating his employees, colleagues, accounts, etc.);
- (3) Investment advisors, hedge funds, etc. that invested your money with Madoff without disclosing this fact and/or without properly investigating Madoff's operations (lawsuits are already being filed against such third parties, including accounting firms that failed to properly audit Madoff's performance reports);
- (4) Funds distributed to earlier investors (see discussion of such redistributive activities below), as well as Securities Investment Protection Corporation (SIPC) payouts analogous to the type of insurance provided by the FDIC for bank account losses (see discussion below).

Question: *Some news articles have reported that investors who made money with Madoff may be required to return that money. Is that correct?*

Answer: Yes. Under certain circumstances, courts have required investors who innocently profited from a Ponzi scheme or *who simply recouped their investment* to put those funds back in the pot to be divided among all those who were defrauded. It is still too early in the process of untangling the Madoff fraud to determine whether such remedies will be adopted and how far back in time they might reach.

Question: *Will SIPC insurance cover any of my losses?*

Answer: SIPC covers losses for securities unlawfully removed from a customer's account up to \$500,000. The maximum includes losses for cash unlawfully removed up to \$100,000. SIPC, unlike FDIC, is a non-profit, industry-funded insurer with limited funds relative to the size of the Madoff fraud, so it could not satisfy the anticipated claims even if it wanted to. Beyond that, most lawyers report that the SIPC has been highly resistant to paying claims, and recovery usually involves costly and time consuming litigation. Until more is known about the methods Madoff employed in his fraud, it is impossible to predict whether there will be any meaningful relief from the SIPC.

Question: *Can I get a tax deduction for the losses I have incurred in the Madoff Ponzi scheme?*

Answer: The tax laws allow a deduction for theft losses that is different from and more favorable than the rules governing regular investment losses. Whether and when you qualify for this tax treatment is something that is important to investigate. If your tax advisor is not familiar with the theft deduction rules as they have been applied to embezzlement, Ponzi schemes and the like, you should ask him or her to consult with a lawyer or accountant who is familiar with the rules and the type of evidence that must be gathered to support the deduction.

Question: *How long will it take to resolve my claim to recover investments with Madoff?*

Answer: A receiver has been appointed recently to oversee the liquidation and recovery process. The steps involve roughly: gathering and making an inventory of the remaining Madoff assets and liabilities; tracking the history of the investments; seeking recovery of funds from third parties who may have liability; establishing a claims filing process; reviewing; challenging and allowing the claims on a case-by-case basis; and finally making a prorata distribution to those entitled to a recovery—assuming there are funds to distribute. Each of these steps involves its own delays and pitfalls for the investor/fraud victim.

It is likely to be years before investors recover funds left from the Madoff scheme, and there will be many legal twists and turns along the way. There will also be important deadlines during the process, such as the deadline for filing claims in the receivership proceedings. These need to be monitored and adhered to carefully.

Question: *What can I do now to protect my rights in connection with the Madoff Ponzi scheme?*

Answer: Individuals and institutions that invested substantial funds directly or indirectly with Madoff should seriously consider obtaining legal counsel. Advice, systematic monitoring of the proceedings and aggressive participation at key points can significantly affect the likelihood and size of your recovery.