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December 18, 2008 – VIA EMAIL

## Thoughts about the Bernie Madoff Scandal

*Let me start this e-mail by letting you know that none of our client's investment accounts are expected to be impacted by the alleged fraudulent activities at Maddoff Investment Securities.*

***What exactly did Bernard Madoff do?*** He allegedly collected money to invest from clients, made up false statements to show that they were doing well, and used new clients' money to pay interest and withdrawals to existing clients. This is known as a Ponzi scheme and is estimated to involve more than a \$50 billion loss for his investors – some of who are local philanthropists and members of our community. His investors say that they didn't see this coming. Could they have?

Here are three key tips that can prevent this from happening to you.

**Know what you own.** Stick to using investment products that use securities such as stocks, bonds, and Exchange Traded Funds (ETF's) that trade daily on major exchanges like the New York Stock Exchange or the NASDAQ. Each of these securities is priced daily, if not minute-by-minute, while the exchange is open. You can check the values and the returns easily. **WARNING -** *If you can't look up the prices and performance in the newspaper or on the Internet - that's a potential red flag - ask a lot more questions.*

**Use an independent custodian.** At our firm, our clients have an independent broker/dealer – LPL Financial, [www.lpl.com](http://www.lpl.com) who serves as custodian of your assets, performs due diligence on the quality of investments, and provides ongoing oversight and compliance. They are subject to regular audits by both the Securities and Exchange Commission (SEC) [www.sec.gov](http://www.sec.gov) and by the Financial Industry Regulatory Authority (FINRA) [www.finra.org](http://www.finra.org). In turn, LPL Financial then audits our offices at least twice each year.

**WARNING –** *Madoff considered himself "custodian" for his client's money. He held his client assets, managed them, and priced them, too. See any conflicts of interest? Investment performance could look like whatever he wanted it to look like. If Madoff gets to decide on the values of each investment, that's called*



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*price manipulation. This is allegedly how Madoff showed winning performance year after year despite market turmoil.*

**Check on investment insurance protections.** As a client of LPL Financial, in the event of securities fraud, you can make claims to recover your lost funds through the Securities Investor Protection Corp (SIPC) on securities up to \$500,000 per account. In addition LPL carries "Fraud Insurance" on each advisor via LPL's Financial Institution Bond held with Chubb Insurance. A copy of this policy is held at our office. You may stop by any time to view it. In addition, your monthly statements reflect information on SIPC insurance. It's important to note, though, that fraud insurance does not protect against market declines; but it does protect against items such as dishonesty, forgery and/or related fraudulent transactions.

*WARNING – Statements issued by Madoff's firm did not include disclosures of any types of securities insurance protection. Thus, Madoff's clients appear to have little recourse to recover funds through traditional methods within an Investment Advisory Firm. When Madoff's clients go to find their assets, which have allegedly been fraudulently paid out over the years, will there be insurance in place? No one can be certain.*

**Final Thoughts.** If an investment strategy sounds too good to be true, it probably is. Reportedly Madoff claimed consistent annual returns of 10-12% (even this year) with little volatility and no annual losses. Money is a very emotional issue and when someone of high regard insists that they could deliver these consistent positive returns to you, (without any fees) it would surely be tempting. And in reality, had it not been for Madoff's investors seeking redemptions from his company during this difficult market environment, this illegal activity could have continued much longer. My heart goes out to those people who have lost their jobs, their life savings and the continued benefits from well minded charitable organizations. Hopefully, some restitution will be delivered to those who have been impacted, but it's likely that the amounts will be in the "pennies on the dollar" area. Without insurance and consumer protections in place, investors should be cautious about working with Registered Investment Advisors who choose to...

- 1. Custody client assets on behalf of their clients – and not through a registered broker/dealer (such as LPL Financial, Charles Schwab, Morgan Stanley, etc)*



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2. *Misrepresent the pricing of securities in accounts*
3. *Create statements that are unaudited, and not compliant with regulatory bodies*
4. *Make it difficult for investors to understand what they own, how it is allocated and the liquidity of each investment.*

...should tread very carefully.

Think about it. With markets down between 35% and 65% worldwide this year, can you name any legitimate financial advisor or money manager who through this year has delivered positive double digit returns? If so, I bet they have a waiting list of people wanting to do business with them. And I'd also bet that the minimum investment needed to hire them is reserved exclusively for a select group of well-to-do people. Wait a second...wasn't that one of the requirements to work with Madoff's team?

But seriously, if you know someone who may be wondering about the integrity, business practices or their current financial advisor's overall desire to place the interests of their client first, we'd be happy to meet with them and explain the consumer protections and transparency of business practices that we've offered to clients since 1968. These have undoubtedly become humbling times for those of us in the financial advisory world; and I assure you that we've all learned lessons that have allowed us to become more efficient, more diligent and more responsive to those we serve.

Have a happy holiday and a wonderful new year. We look forward to seeing you next year in 2009.

Marc

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