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## About This Series...

*A periodic update of the tax, due diligence, and business fraud issues for those clients and friends of the firm affected by the alleged fraud of Bernard L. Madoff and his business.*

# MADOFF MATTERS

## A CAT Scan of the Madoff Scandal:

### Diagnosing Fraud Inside The Black Box

While many investors may think the Madoff scheme is unprecedented, rest assured it is not. Over the past ten years the SEC has investigated numerous instances of investor fraud on the scale of a hundred million to a billion dollars. Daily headlines are now revealing fresh examples.

The alleged fraud in the Madoff scheme has set a new and shocking dollar bar, but the financial and operational elements that are the recipe for such a disaster have been around for quite a while and we will likely see more such events in the future.

The complexity of hedge fund strategies combined with investor desire for “above average” returns, along with the elite lure of a private, exclusive investment realm, have resulted in an atmosphere ripe for fraudulent practices. Due diligence, audit statements, and understanding of investment strategy – traditional tools of prudent investors – often have been cast aside in recent years. Instead, whispered social relationships accompanied by regular reports of fund success and individual wealth building were the key attributes of many “sophisticated investors”.

As we now enter a period of more sober consideration, stemming from the economic crisis in general and the Madoff meltdown specifically, it will

be vital that the correct lessons are taken from the current situation.

This article is for investors, advisors and lawyers on the phenomenon of hedge funds and other similar Unregulated Multi-Level Investment Structures (“UMLIS”). The intent is to illuminate the investment pitfalls inherent in this nearly-impenetrable area of investment and what steps can be taken to prudently take advantage of the opportunities as the market is redefined.

In this article we will:

- 1) explain the structure of a typical UMLIS;
- 2) illustrate how Madoff deviated from it;
- 3) explore the difficulty inherent in monitoring and valuing an UMLIS; and
- 4) demonstrate how a more integrated approach to reputational and financial due diligence by forensic experts can help detect a potential for fraud and otherwise provide confidence in making investments in this arena.

**To read the full article, click:**

**<http://www.holtzrubenstein.com/Catscan.pdf>**



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