

## **What is a Ponzi Scheme? Your New Jersey Tax Lawyer Explains**

You've probably heard a lot about Ponzi schemes recently in the news — about people becoming unimaginably wealthy through fraud, only to watch their empires, built on dishonesty, collapse about them — but how many people who are not NJ tax attorneys truly understand what a Ponzi scheme is and how it works? Grasp the fundamentals of a Ponzi scheme, and you too can keep yourself from being victimized by perpetrators of this [white collar crime](#). You can also learn how to keep yourself from being implicated in a Ponzi scheme investigation if you suspect someone you know or work with is involved in a scheme or trying to involve you in one.

### **Ponzi Scheme Basics**

A Ponzi scheme is a fraudulent investment scheme that uses the money from new investors to pay off the old investors. Although Ponzi schemes are subtly different from pyramid schemes, a pyramid is a good way to understand it. Like a pyramid, you need to get continually bigger groups of investors at the bottom in order to support the people above them. Sometimes a con artist will get people to reinvest in the Ponzi scheme, which limits the number of new investors they need to recruit. However, if they don't continually get new investors, they are liable to fall apart.

There are a few common signs of Ponzi schemes. In general, it will attempt to attract new investors by offering returns that are bigger and/or more consistent than those offered by legitimate investments. It is always important to remember that return is a function of risk, and if someone is offering you a “guaranteed” way to make a 10- to 20-percent return annually, it's probably a scam. Ponzi schemes tend to use vague, meaningless terms such as “high-yield investment program” to describe their investment strategy. Ponzi schemes will try to minimize the amount that they have to pay out, so they can just issue statements that say that the person has more money without actually having to give the person any more money (which might cut down on the time the scheme can run). Therefore, they encourage reinvestment or freeze the income for a certain period of time.

### **End Game for Ponzi Schemes**

Ponzi schemes collapse by their nature. Eventually, they won't get enough people in to pay off all the investors. There are a couple different ways a Ponzi scheme can end. If the con artists are clever, they may disappear, their money invested overseas. If the investments slow down, the scheme may collapse because the con artist doesn't have enough money to pay off the investors. A slowdown in the economy will cause investors to remove their money, which can cause the scheme to fall apart.

Some Ponzi schemes end when someone reports them to the government as a suspected Ponzi scheme, for selling unregistered securities, or through an [IRS criminal tax investigation](#). It is always good to report suspected Ponzi schemes to the government. You can ask a [NJ tax lawyer](#) about the proper channels to go through, especially if you are concerned about protecting yourself from suspicions of any involvement in the fraud. The key is to talk to an experienced New Jersey tax lawyer early on, to understand your options and rights.