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Ponzi Schemes and its Prevention: Insights from Malaysia

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ABSTRACT

A Ponzi scheme is a fraudulent investing scheme which promises high rates of return with little risk to investors. The scheme has led to a substantial amount of financial leakages in recent years. Despite warnings by the law enforcement agencies and regulators, many have unfortunately fallen victim. Hence, the current measures are limited in preventing the fraudulent schemes. Therefore, the present study aimed to identify the influencing factors for joining Ponzi schemes by examining the modus operandi used, profile of victims and fraudsters and to investigate the current measures in preventing Ponzi schemes in Malaysia. This study employed a qualitative methodology with semi-structured interviews and document reviews to collect data. Interviews involving eight interviewees with regulators, enforcers, and victims revealed that prevention of Ponzi schemes should be addressed holistically by examining the modus operandi used, profile of victims and fraudsters. Findings further indicated that the prevention measures are led by three core elements consisting of education, regulations and enforcement. Additionally, education is the best approach to ensure an effective preventive strategy which needs to be supported by a specific regulations on Ponzi schemes. This study provides recent evidence on Ponzi schemes and valuable insights for future development of preventive measures.

Keywords*:* Ponzi scheme, pseudo-investment, fraud, prevention measures, regulation, enforcement

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INTRODUCTION

A Ponzi scheme is an investment fraud which lures its investors by promising abnormally high rates of returns with little risk to investors (Interpol, 2019; Wells, 2010). Ponzi schemes, also known as pseudo-investments, have caused huge financial leakages in history. It earned its name when Mr Charles Ponzi, an Italian immigrant to the United States in the early 20th century, started a scheme that promised a return of 50% of the investment to investors within 45 days or 100% return within 90 days by buying discounted postal reply coupons in other countries and redeeming them at face value in the United States (Azim & Azam, 2016). Instead of using the money on actual investments, Ponzi merely used it to pay his earlier investors and took some for his own interest. The cycle continued for some duration but when there were no longer new investors contributing to the scheme it eventually collapsed. It was reported to cause financial losses amounting to USD7 million (Wilkins, Acuff & Hermanson, 2012). A similar tactic was employed by modern day Ponzi schemer, the infamous Bernie Madoff, who swindled USD65 billion worth of money (Jacobs & Schain, 2011). Unlike Ponzi, Madoff was an influential figure in Wall Street with various key positions held in the financial sector in the US. Using his reputation and credentials, Madoff won the trust of many unsuspecting investors until his fraudulent scheme finally collapsed in 2008.

In Malaysia, a Ponzi-like scheme known as “Skim Pak Man Telo” was publicly discovered in the late 1980s. Led by Pak Man Telo who was a former reporter, the scheme caused an alleged RM90.9 million losses involving nearly 50,000 investors. Another major fraud in Malaysia was the Swisscash Mutual Fund scheme in 2006 with an estimated RM190 million losses (Abdul Ghani & Abdul Halim, 2017). Several other Ponzi schemes have also been reported in Malaysia such as JJ Poor to Rich (JJPTR), MBI, VenusFX Forex and Richway Global Venture (Teo Piaw, Zawawi & Bujang, 2019). In 2017, the Commercial Crime Investigation Department of the Royal Malaysia Police reported 408 recorded cases with RM70.1 million in losses in 2015 which grew to 1,151 cases reflecting RM210.3 million in losses in 2016 (Berita Harian, April 2017). Hence, the incidence of Ponzi schemes have been rising over the years and if left unchecked, this problem will further escalate resulting in adverse consequences to investors, creditors and the public as a whole (Omar, Said & Johari, 2016).

These infamous fraudulent investment scandals and many more similar schemes often share recurring characteristics especially in its modus operandi, profiles of both fraudsters and victims as well as the factors influencing participation in the scheme. Ponzi schemers keep their modus operandi up to date with the latest advanced information technology available in recent years. For instance, according to the Purple Notice of Interpol (2019) most of the advertisements and promotions of Ponzi schemes in recent years are conducted using digital platforms. Past studies also noted that although fraudsters come from all walks of life, their common characteristics include a persuasive nature, good communication skills and have a positive image among the public (Mugarura, 2017).Omar, Said and Johari (2016) found that fraudsters were mostly male and some even held top management positions in their companies. Victims on the other hand are often described as trusting individuals who are usually associated with lack of knowledge in investment and financial matters and were not particularly rich (Lokanan, 2014). The Theory of Gullibility by Greenspan in 2009 proposed four key factors that induced people to enter a Ponzi scheme viz., situation, cognition, personality and emotion. Yet, little evidence which explores these recurring characteristics of current cases of Ponzi schemes is available within developing countries including Malaysia. Therefore, given the adverse impact Ponzi schemes have on the financial market, the economy and society in general, a more thorough investigation on the scheme is timely and highly warranted which would be helpful in assisting the relevant authorities to prevent such fraud.

Presently, in Malaysia there are no specific laws and regulations for dealing with Ponzi crimes which makes it difficult to legally frame a scheme as a Ponzi fraud. Instead, the existing Ponzi cases can be in violation of several laws and monitored by three main authorities: the central bank of Malaysia which is Bank Negara Malaysia, the Securities Commission Malaysia and the Royal Malaysia Police. These authorities act as regulators, monitoring bodies as well as law enforcers. Each entity plays a significant role in warning and educating the public on the danger of Ponzi schemes. For example, BNM continually provides investment fraud and scam notices through its website and mobile applications. Nevertheless, despite the public warnings and various education programmes against fraudsters, the number of Ponzi schemes are still increasing. The amount of financial leakages resulting from Ponzi schemes have also risen over time which potentially pose a risk towards confidence in the integrity of the Malaysian capital market. Hence, the question arises as to whether the public is sufficiently aware of the danger of such schemes and how can the public play a role in overcoming this problem. Therefore, the present study aimed to to identify the influencing factors for joining Ponzi schemes by examining the modus operandi used, profile of victims and fraudsters and to investigate the current measures in preventing Ponzi schemes.

LITERATURE REVIEW

Characteristics and Modus Operandi

Ponzi schemes are often characterised by the promise of higher returns on investment which far surpass the returns offered by licensed financial institutions. The scheme requires a constant flow of new investments to survive, failure of which will lead to the collapse of the schemes. This happens when large numbers of existing investors withdraw their investments and recruiting new investors becomes a challenge (SEC, 2018, as cited in Eren & DiMauro). A review of extant literature reveals that most research focus on modus operandi of schemes, profiles of fraudsters and victims, and the factors influencing investors to get involved in Ponzi schemes.

According to Munisamy (2019), many of the companies offering dubious schemes operate without a license. These companies often camouflage the fraudulent schemes using common types of investments such as forex trading, cryptocurrency (e.g. Bitcoin), gold investment scheme, commodity investment scheme, property investment scheme, multi-level marketing and recreational membership scheme. The Purple Notice issued by Interpol (2019) suggests that Ponzi fraudsters make use of the internet to promote schemes digitally as shown in Figure 1.

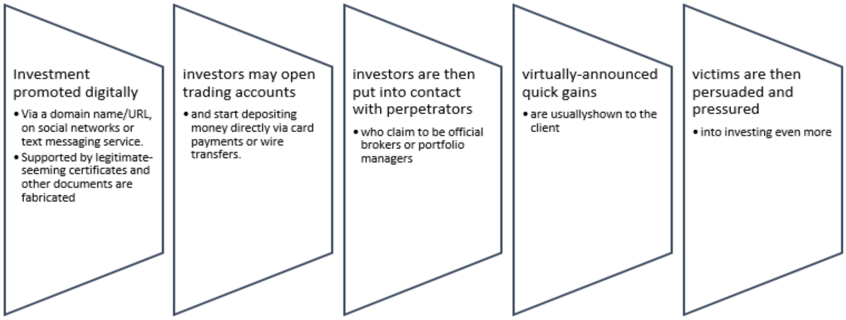

Figure 1: Digital-based modus operandi (Adapted from Purple Notice Interpol, 2019)

Munisamy (2019) further noted that most Ponzi schemes operate as a syndicate by forming a legitimate company which register with the Registrar of Companies. The registration is done to avoid suspicion from the authorities when large sums of money are involved. Apart from that, fraudsters were found to act as company director or in some cases they appoint dummy directors. Past studies suggest that a growing trend of Ponzi schemes is the use of social media and the internet to deceive unsuspecting victims (Abdul Ghani & Abdul Halim, 2017; Mohd Sulaiman, Moideen & Moreira, 2016). Increased surveillance is required to pierce through the legitimate appearance of the crime (Albrecht, Morales, Baldwin & Scott, 2017), as schemers continually find new ways to use the fraudulent scheme to manipulate and take advantage of investors.

Greenspan (2009) in his Gullibility Theory identified four factors that contribute towards participation of victims in Ponzi schemes. These factors are situation, cognition, personality and emotion. According to this theory, victims commonly found themselves in a situation that induces them to join the schemes when everybody else are doing it. It appears to signal to the victims that since others are already involved, then it must be the correct thing to do. Apart from that victims tend to be those who lack knowledge in financial matters and demonstrate a certain personality that is prone to be manipulated. In particular, some individuals are argued to be more trusting than others; such personalities tend to make them a possible victim more than others. Greenspan (2009) also suggest that apart from greed, other emotions such as fear of insecurity in earnings could lead to participation in Ponzi schemes. Murphree (2019) concurs by noting that Ponzi schemes thrive on emotion whereby investors may not always think through their actions before making an investment decision. The Gullibility Theory gained support from various recent studies including George, Teunisse & Case (2020) and Tennant (2011). In their study, George, Teunisse & Case (2020) used the concept of gullibility as the basis in understanding the reasons why some people are more prone to scams than others while Tennant (2011) used the same concept to determine individuals' exposure to Ponzi schemes.

Besides Greenspan (2009), Manning (2018) also found that victims tend to be those of limited financial knowledge. This is consistent with Chariri, Sektiyani, Nurlina and Wulandari (2018) which noted that the level of individual financial literacy positively affects the ability to detect investment scams. Lokanan (2014) added that some victims joined because they are poor and desperate to make ends meet. Schemers prey on individuals with specific characteristics that indicate they are more trusting, and gain trust from victims which makes the victims to be more susceptible to fraud (Baucus & Mitteness, 2016). This type of modus operandi is difficult to prevent and detect as false, mimicry used by schemers can signal trustworthiness to the victims. Schemers rely on investors' ignorance of this investment structure for their continued participation (Almassi, 2017). Past studies also identified victims as people who lack effort in conducting due diligence, fail to make necessary enquiries and conduct information search before investing (Carey & Webb, 2017).

A distinct feature of the fraud involves repeated interaction with an increasingly large number of individuals over a long period of time (Carey & Webb, 2017). The motive for such interactions is commonly to build and maintain an individual's victim's trust. Trusting individuals are less likely to conduct due diligence to detect fraud and hence are prone to become a victim (Carey & Webb, 2017). The building of trust among the victims is closely associated with affinity relation between the fraudsters and the victims. Nevertheless, Mugarura (2017) suggests that many people who fall victims of fraudulent investment schemes such as Ponzi and advance fee fraud are not gullible but lack knowledge of their sophistication and how they operate to defraud unsuspecting victims of their savings. Jacobs & Schain (2011) opined that individuals are vulnerable to Ponzi schemes due to the part of time we live in. The fact that investors often confuse acquaintance with friend, the endless networking has blurred the lines between acquaintance and true friend and allows the Ponzi schemes to succeed.

Prevention Measures of Ponzi Schemes

Murugara (2017) noted that there are no specific measures that can be taken to prevent Ponzi schemes to continue operation. However, preventive measures are still needed to reduce the number of people from becoming victims. Government regulations and internal auditing can prevent fraud from increasing (Albrecht et al., 2017). Baucus & Mitteness (2016) suggested that regulations should also be in place as Ponzi business formation is easy since the fraudsters act to portray their business as legitimate organizations. The Securities Commission Malaysia regulate the legitimate way of investing by consolidating the Securities Industry Act 1983 and Futures Industry Act 1993 in the Capital Market and Services Act 2007. The Act aims to regulate and provide for matters relating to the activities, markets and intermediaries in the capital markets, and for matters consequential and incidental thereto. Similarly, the Financial Services Act 2013 consolidates legislation pertaining to banking, investment banking, insurance and payment system, thus repealing the Banking and Financial Institutions Act 1989, the Insurance Act 1996, the Exchange Control Act 1953 and the Payment Systems Act 2003 (Ali et al., 2018).

Another aspect of preventive measure involves the need for effective enforcement by the relevant authorities. Sulaiman and Moreira (2016) suggested that regulators of the securities market (e.g. the US Securities Exchange Commission) to have specialised training for the staff such as Certified Fraud Examiners and Certified Financial Analysts courses. The authors also suggested severe punishment against schemers as documented in a unprecedented custodial sentence in the Crude Palm Oil Ponzi case. This law shall provide for ways to counter this financial crime as well as the duties of the various financial supervisory bodies. Also, authorities should reconsider and clarify the relevant laws, and business practices and to increase sanctions especially for money scheme frauds (Galasintu, Supanit, Chaiittivej, 2018). At the very least, this will address perception of ineffective enforcement of the law due to the reluctance in imposing custodial sentence for securities law contravention (Sulaiman, Moideed & Moreira, 2016) to be as deterrence for future schemers and to specifically combat Ponzi schemes (Uppiah, 2018). Additional mechanisms must also be carried out in terms of reforms with the recruitment of staff with specialised experience and skills such as financial and accounting experts, as well as conducting risk-based examinations of financial firms.

In ensuring more successful prevention, financial fraud needs to be treated as a social phenomenon and not as circumstantial issue (Reurink, 2016). As social phenomenon, fraud detection mechanisms should be introduced to investors, due diligence experts, regulators and policymakers who seek to determine the genuineness and authenticity of investment schemes (Drew & Drew, 2010). This highlights the importance of education of the public on how they can play their role in preventing Ponzi schemes from occuring. With globalisation, there are a myriad of investment opportunities, but potential investors need to bear in mind when deciding on where to invest and how to invest their money since there are also opportunities for criminal exploitation. The lack of knowledge of the sophistication and how Ponzi schemes operate to defraud unsuspecting victims of their savings requires the regulators of financial markets to intensify education of investors on how to identify and avoid Ponzi schemes (Amoah, 2018). Bosley and Knorr (2018) suggested that the state and federal regulators should allocate resources and to actively engage in preventive education. In a similar line, Galasintu, Supanit, and Chaiittivej (2018) suggested that consumers must be self-regulated by becoming more aware of business fraud and learn to be more protective. The public is urged to be knowledgeable in recognising the signs or red flags of investment fraud such as investments guaranteeing high returns with little risk, once-in-a-lifetime deals, pressure to buy quickly, and overly consistent returns (Baker & Puttonen, 2017).

RESEARCH METHODS

This study aimed to identify the influencing factors for joining Ponzi schemes by examining the modus operandi used, profile of victims and fraudsters and to investigate the current measures in preventing Ponzi schemes in Malaysia. Given the diverse nature of Ponzi schemes, the perceptions and actions of individuals involved in the investment scam field is of paramount importance. Denzin and Lincoln (2008) suggest that as a qualitative researcher, one needs to involve an interpretive and naturalistic approach to the world. It necessitates the researcher to study things in its natural settings while making sense of and interpreting the phenomena in question in terms of the meanings people bring to them. Hence, this study utilized the interpretive approach adopting a qualitative phenomenology methodology. This research methodology enabled the researchers to gain an in-depth understanding of the Ponzi schemes from both the regulators and enforcers' perspectives. This is consistent with Creswell (2003) who noted that in such contexts the researcher "looks for complexity of views rather than narrow the meanings into a few categories or ideas" (Creswell, 2003:p.20).

The main sources of evidence for this study comprised of semi-structured interviews with the relevant personnel involved with the regulation and enforcement of Ponzi Scheme prevention. The semi-structured interviews consisted of open-ended questions based on the interview protocol as suggested by related literature on Ponzi schemes, investment scams, fraud and financial criminology. The interviews covered context and scopes, as well as the modus operandi employed by the fraudsters. Since the focus of this study was to elicit information from the regulatory and enforcement agency perspectives, three key entities were selected for the purpose of data collection, namely Bank Negara Malaysia, the Securities Commission Malaysia and Royal Malaysia Police. Several attempts were made to contact the key informants in each authority, however, only Bank Negara Malaysia and the Royal Malaysia Police responded and agreed to have the interviews. Hence, it was decided to obtain information from the Securities Commission Malaysia through secondary data. Some information cannot be disclosed due to secrecy and it will only be released if it has become a public document (Abd Ghani, Abdul Halim & Abdul Rahman (2019).

In the present study, interviews were conducted with three BNM officers who were directly involved in complaints and cases regarding illegal investments. Within BNM a formal department was set up for the purpose of receiving complaints, feedback and providing education to fight against Ponzi schemes. Therefore, investigation on BNM allows for good illustrations of key research issues highlighted in the present study. Interviews were also conducted with two key police officers from the Commercial Crime Investigation Department of the Royal Malaysia Police. Theywere chosen based on active involvement in the fight against Ponzi Schemes. Three victims were also willing to be informants to share their experience with Ponzi schemes. Table 1 shows the list of interviewees involved in the study which were conducted between 1 March 2019 until 31 May 2020.

Table 1: List of Interviewees

Interviewee's Position & Department	Total interview hours
Senior Investigator of the Commercial Crime Investigation Department, Royal Malaysia Police	2 hours
Investigator of the Commercial Crime Investigation Department, Royal Malaysia Police	4 hours
Mr A, Bank Negara Malaysia	4 hours
Mr B, Bank Negara Malaysia	
Mr C, Bank Negara Malaysia	
Victim X	45 minutes
Victim Y	30 minutes
Victim Z	30 minutes

The interview data were facilitated using interview protocols and conversations were recorded and later transcribed. Cross-checking of the research findings was done against the website information and archival reports of the BNM, Securities Commission Malaysia and the Royal Malaysia Police. In addition, social media postings of a vigilante group against Ponzi schemes were reviewed. The inclusion of this data source was considered important in examining the role of the public in preventing Ponzi schemes.

The qualitative data analysis involved a thorough examination of the data which was followed by formation of initial codes. These codes are further analysed to establish themes or patterns. Throughout the data analysis process, several rounds of coding were conducted resulting in the final refined coding scheme. The code refinement enabled the researcher to subsequently formulate findings statements. Following the write up of key findings, a procedure called "member checks" was conducted to ensure trustworthiness of the qualitative data already collected. The interviewees were contacted through emails and provided with the draft findings for them to validate. Upon receiving the responses from the interviewees, several key conclusions were drawn. During this stage, the findings were linked to insights and the literature as suggested by Bloomberg and Volpe (2008). Despite the weaknesses in terms of statistical generalizations, this qualitative phenomenology study offered opportunities for in-depth observation and an analysis of the conduct of Ponzi Schemes.

FINDINGS AND DISCUSSIONS

The following sections present key findings on the influencing factors for joining Ponzi schemes and the current measures undertaken to prevent them.

Modus Operandi of Ponzi Schemes

Knowledge on the modus operandi used by Ponzi schemes is an essential requirement in preventing the crime. Various Ponzi schemes use different modus operandi when targeting their victims. However, common features are usually found in most cases. Case facts pertaining to Victim X, a male victim, is used in this paper to illustrate one of the latest and common modus operandi used in Ponzi schemes examined. Victim X joined an "investment" scheme a year ago by depositing RM5,000 withdrawn from the Employee Provident Fund account with the hope of getting an estimated RM100,000 return. X had a history of joining get-rich-quick schemes previously but with a smaller amount of money. X had also joined a multi-level-marketing scheme to sell some products but failed to break even on the cost of investment. X's participation in the current scheme was based on word of mouth suggestion by a trusted friend, M, who was a former co-worker. Prior work relationship with M provided the trust placed by X into the current scheme. X deposited the money to M's personal account with no black and white proof of transaction. X admitted that he was enticed to join when M gave the impression of "exclusivity" of the scheme by mentioning that "only one portion left" for X to join the scheme.

Once X joined the scheme, he was put under the supervision of M who acts as a "leader" and middleperson between X and the so-called investment company. As such X was never in direct communication with the management of the fraudulent company nor with other victims. This approach managed to isolate victims from getting information and updates other than through the "leader". Thus, manipulation of information was quite easy for the fraudsters. When asked the reason why X still keeps his confidence in getting the money in the future, he responded by saying that he trusts M to keep the promise of delivering the returns. Therefore, M relied on this trust for X to maintain his participation in the scheme so much so that X did not question the various excuses given by M for failure to pay the returns. The interview also revealed that M regularly sends motivational messages using religion and ethnic ties as a way to keep X in the scheme.

Consistent with Interpol (2019) and Munisamy (2019), fraudsters resort to digital platforms to promote their schemes. Reviews of postings on popular social media such as Facebook, Instagram, and personal websites revealed a plethora of advertisements of so-called investment schemes. Using the internet for online promotion of their fraudulent schemes has made it much easier to reach out to potential victims in a greater scale than the traditional offline methods. In the past, fraudsters promote Ponzi schemes through face-to-face meetings, seminars, and conferences. The modus operandi using the internet has posed more challenges to regulators and law enforcers partly due to the easy nature and relatively cheaper way for the fraudsters to commit the fraud. As such, the authorities also need to use the internet as a medium of communication for public announcement and warnings purposes. Hence, it is crucial for both regulators and the law enforcers to be up to date with the latest communication technology in implementing their prevention strategies.

As in several other modus operandi, such as in Colombia's DRE and DMFG Ponzi schemes (Hofstetter et al., 2018), this study found that Ponzi crime fraudsters typically do not work solo. Instead, they commonly form a group of individuals with a mastermind behind the scam. It is the mastermind who devises the modus operandi of the Ponzi scheme and hires other people who communicate directly to the investors (Hardy, Bell & Allen, 2020). Thus, the spokesperson or the representative serves as a "veil" by which the fraudster would hide. Similar to earlier Ponzi schemes (see Cross, 2020), the mastermind operates in this way as a back up plan should the scheme fall apart. In some cases, the mastermind will engage in few individuals who would formally form a company and register it with the Registrar of Companies. However, it is often the case that these companies would illegally carry out deposit taking activities without proper registration with Bank Negara Malaysia or the Securities Commission Malaysia. This approach works well with the mastermind since when things go bad, the company would be shut down, investors could do little to recover the cash and the mastermind could escape easily. Even if actions are taken on the company, the puppet management teams would be investigated by enforcers while the mastermind would go free. For example, a senior investigator at Royal Malaysia Police stated:

> *"The problem is when these masterminds create an investment scheme, he has a way, he may make a dummy company, so that the money will go into another account of the company. He will collect money through that company. So, there is no money trail...."*

Furthermore, evidence suggests that it is not uncommon to find that the masterminds could also be victims in the past. Through experience and greed, they themselves turn to become the fraudsters. Another approach often used by fraudsters to gain trust from victims is the engagement of public figures, influential persons, and celebrities as the spokesperson. The spokesperson was part of the Ponzi schemes promotion campaigns to provide testimony on the apparent success of the scheme. In addition, there are also schemes which use religion as an attraction to invest. For instance, there has been occasions whereby there were intentional use of Islamic terms and individuals disguised as "ustaz" or religious figures to deceive the public into the scheme. Such modus operandi has been found to induce individuals to withdraw their retirement savings and pensions to invest in the schemes. All the aforesaid modus operandi are summarised in Table 2.

Table 2: Modus Operandi of Ponzi Schemes

Modus Operandi	Effects
Digital platform to promote scheme	Reach out greater scale of potential victims
Mastermind headed a group of individuals	A spokesperson who is the "veil" will hide the mastermind
Public figures / influential persons / celebrities	Testimonies from the public figures / influential persons/ celebrities will induce victims

Profiles of Fraudsters and Victims

Among the common characteristics of the fraudsters include the personality of a con man, a competent mastermind, person with lavish appearance, eloquent and having good communication skills. In addition, fraudsters have also been found to have an influential and excellent public relationship with the ability to portray a good image of the company they represent. Most of the times the fraudsters often portray themselves as having luxurious lifestyle (Azim & Azam, 2016). These traits represent valuable capabilities that can be harnessed by the Ponzi schemers to commit the fraud. For example, fraudsters used opulence appeal to win the trust of victims by displaying luxurious lifestyles on their social media postings. Common luxury items displayed are expensive cars and houses. Moreover, fraudsters employ persuasive communication skills in luring victims as well as putting pressure to them to join the schemes. A common method used to persuade victims is to give a false impression on the need to act quickly on exclusive offers before it is too late. Not only that the victims are pressured into joining the scheme, they are also enticed by the apparent attractiveness of the once in a lifetime offer.

Victims can also be identified into several profiles. Firstly, victims tend to be among individuals who are expected to or has recently obtained a windfall (Nouri & Kremenich, 2019). Typically, the windfall includes large sums of money received by newly retired employees. In Malaysia, private sector employees receive savings in a compulsory savings plan known as the Employee Provident Fund. Likewise, government pensioners would also get huge cash upon retirement by way of gratuity payments. The new retirees would have been attracted to join Ponzi schemes possibly for two reasons. Firstly, the expected returns from the scheme would serve as a source of passive income and secondly, retirees would feel that putting a small portion of the windfall into an investment scheme is not considered risky as they still have a lot of money left from the windfall. Findings from the interviews reveal that some victims fell prey to Ponzi schemes through close association with members of an affinity group. The fraudsters cultivated and acquired the trust of others and then took advantage of that confidence (Amoah, 2018; Azim & Azam, 2016). Victims such as the retirees are often members of local religious groups, local neighborhoods and other hobby or personal interest groups.

Affinity was found to be an influencing factor for victim Z to join a Ponzi scheme. Z is a homemaker with secondary school qualification and who was once working as a bank employee. Z was motivated to join a scheme introduced by a fellow neighbour who was a member of the neighbourhood committee. She trusted the neighbour for his good-mannered behaviour and the long term relationship between them. However, Z realised that the scheme was dubious when she received no returns for her investment despite demanding for it several times. Fraudsters benefit from affinity trusts since it is easier for them to persuade the victims compared to trying to convince individual investors who may not trust the fraudster (Amoah, 2018: Bosley & Knorr, 2018; Blois & Ryan, 2013). Due to the tacit confidence earned from the broader community, the fraudsters had little trouble in attracting respectable clients for without raising any doubt.

Our findings further indicated that victims who lack financial knowledge do become cheated easily. However, there are also people who have some experience, knowledge and expertise in financial matters who have become victims. This suggests that financial knowledge does not necessarily affect investors' ability to evade Ponzi schemes. Two possible explanations for the findings are: (1) those who lack basic understanding on financial matters may have entered into Ponzi schemes mainly due to ignorance, and (2) investors who have financial literacy background may have joined the scheme driven by greed. An interviewee noted that victims in the first category are those who are either completely ignorant of the fraud or those who tried to investigate the scheme but with limited information failed to carry out due diligence on the legitimacy of the schemes. Meanwhile, the second category of victims still put their money into the scheme even though they are equipped with some knowledge of the risks involved with the intention of earning abnormally high returns promised. Therefore, while the first category did not take action to validate the scheme due to ignorance of the law, the second category may have been influenced by their risk-taking preference. This was evident from findings of victim Y. Victim Y holds a degree in Business Administration and has a history of joining get-rich-quick schemes in the past. When asked why he joined the scheme, Y stated that:

> *"I just want to try...and I received some returns. That kept me investing more...but later I no longer receive anything. I did not quite cover my total investment, so in the end I lost hope."*

These findings are consistent with propositions by Greenspan (2009) on the profiles of gullible victims particularly on the cognition, personality and emotion factors. The summary of the fraudsters and victims is presented in Table 3.

Table 3: Profiles of Fraudsters and Victims

No.	Entity	Traits / Circumstances	How fraudsters influenced victims? / How victims fall prey to fraudsters?
1	Fraudsters	Competent mastermind Lavish appearance Eloquent Good communication skills Influential Excellent public relationship	Displaying luxurious lifestyle Displaying expensive cars Displaying expensive houses
2	Victims	Individuals expected to receive windfall (usually due to retirement) Close association with members of an affinity group Trusted the fraudsters Lack of financial knowledge Financially literate but join scheme due to greed	Confident with the mastermind/spokesperson Risk-takers Ignorance on the knowledge of financial investment

In addition, an interesting finding highlighted the role of victims in promoting Ponzi schemes. An officer at one of regulatory authorities interviewed noted that it is sometimes difficult to resolve complaints from victims as they can be considered as an “accomplice” rather than a “victim” of the scheme. By entering the scheme, investors provide the cash as required by fraudsters and as long as they continue to get some returns, these investors will stay in the scheme. In other words, these investors are “accomplice” to the crime. However, once the schemes collapse, the same investors will play victims, and some may even blame the authorities for not preventing the fraud much earlier. Thus, as “accomplices”, the investors may have unintentionally supported the growth of Ponzi schemes through the basic law of supply and demand. Tougher penalties stipulated by relevant laws may therefore need to apply to “accomplices” as well as fraudsters for more effective detection and prevention of Ponzi frauds.

Regulation, Enforcement and Education to Prevent Ponzi Schemes

Findings of this study indicated that the prevention measures are led by three core elements consisting of regulations, enforcement, and education shown in Figure 2. It is essential that all three elements are coordinated and communicated well to ensure effective prevention of Ponzi schemes. Each of the elements are discussed below.

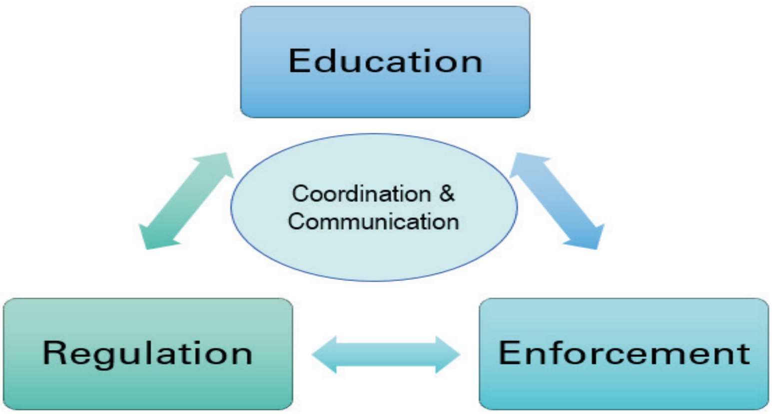

Figure 2: Ponzi Scheme Preventions Strategies

Education

Consistent with Amoah (2018) and Baker and Puttonen (2017), this study found that education is the most important prevention strategy to fight Ponzi schemes, as shown in Figure 2. Evidence showed that three main regulators and enforcers, *viz*. Bank Negara Malaysia, Securities Commission Malaysia, and the Royal Malaysia Police implement various education and awareness programmes to the public. In the case of BNM, most of the information disseminated to the public can be found in their website at https://www.bnm.gov.my/. For example, the website provides consumer alerts and updates such as a list of illegally operating investment schemes including Ponzi schemes. These are listed under the Financial Consumer Alerts page within their website. Two types of alerts are provided by BNM i.e., financial consumer alerts and financial fraud alerts. The financial consumer alerts list down the companies which are not regulated by BNM. Meanwhile, the financial fraud alert provides a listing of cases that have been brought to the court.

In an effort to provide direct communication channel between BNM and the public in financial matters, BNM set up a department known as "Laman Informasi Nasihat & Khidmat" or LINK. Any queries and complaints from the public regarding Ponzi schemes can be submitted through visits to LINK or via its "telelink" contact numbers. Once received, the complaints are addressed by conducting a preliminary assessment. The assessment will be based on the requirement of the law and must be furnished with documented evidence such as brochures and agreements of the Ponzi schemes. If the complaints are sufficiently considered as a case to be highlighted, the case will be forwarded to a working committee or the investigation department. However, at BNM Ponzi scheme-related complaints received are found to be much less than enquiries by the public. Another tool used by BNM to educate the public on Ponzi schemes is the mobile applications. BNM has launched several mobile applications such as MyBNM, BNM MyLINK and MyTabung (Bank Negara Malaysia, 2015). These applications are easily downloaded and serves as a convenient platform to educate the public. For instance, MyTabung application guides individuals to create personal or household budgets whereby they can record recurring income, savings, and expenses as well as display their financial position and spending patterns. Through these applications, the public can also seek financial advice and spending tips to help them practice prudent financial management and avoid Ponzi schemes. Based on the current awareness programmes initiated by BNM such as public announcement, media coverage and face to face communication with community leaders, the public is expected to be well-informed on how to avoid Ponzi schemes. As commented by an officer at BNM:

> *"...lack of awareness could not be used as the reason for Ponzi schemes to occur because sufficient warnings have been given by BNM through various means".*

Similar to BNM, the Securities Commission Malaysia conducts similar education platforms through their websites at https://www.sc.com.my/ by regularly announcing a list of unauthorised websites, investment products, illegal companies or suspected individuals for the public to refer to. Apart from that, SC also created a website called “InvestSmart” specifically to educate the public on investment matters. Among the aim of the website is to encourage the public to take control of their finances in a responsible manner, to equip investors with the knowledge, skills and tools needed to exercise good judgement and discretion in making investment decisions, and to encourage more informed retail participation in the capital market. Apart from that, SC also educates the public through its mobile application known as “InvestSmart® mobile app” (Saieed, 2014). Findings suggest that the Royal Malaysia Police also plays an important role in preventing Ponzi crimes. Various warnings have been communicated through the media such as newspapers and television programs to warn the public not to be deceived easily. The police also seek cooperation from the public to immediately report to the police if they suspect any fraud taking place. In an effort to reach a wider public outreach, Royal Malaysia Police uses social media (https://www.facebook.com/PolisDirajaMalaysia/posts/829829790360663) to educate the public on the danger of Ponzi schemes. Through Facebook, regular warnings are posted using various infographics posters for ease of understanding.

Evidence further showed that social media group initiated by the public can play a major role in disseminating information on the risks of Ponzi schemes. For example, a vigilante group known as “Ponzi Scheme Alert in Malaysia” is a private group in the social media Facebook (https://www.facebook.com/groups/2747672548810963) which aims at warning investors about the existence of companies and get-rich-quick schemes including Ponzi schemes. While education through regulators’ and enforcers’ websites and applications represents a “passive education” strategy, vigilante groups on social media provide a more interactive platform and “active education” for the public through focused and rapid dissemination of warnings on Ponzi schemes.

Regulation

A closer look into these schemes revealed that regulations (Figure 2) play an important role in preventing Ponzi schemes. However, currently there areis no specific law and/or regulations for Ponzi crimes. With the absence of a specific law on Ponzi crimes, the fraudulent scheme is frequently seen as a violation of several laws. Table 4 lists the relevant laws used by regulators and enforcers to incriminate Ponzi scheme fraudsters.

Table 4: Relevant laws to incriminate Ponzi Scheme Fraudsters

Name of document	Regulator/Enforcer
Penal Code (Act 574)	Royal Malaysia Police
Companies Act 2016 (Act 777)	Companies Commission of Malaysia
Interest Schemes Act 2016 (Act 778)	Companies Commission of Malaysia
Financial Services Act 2013 (Act 758)	Bank Negara Malaysia
Anti-Money Laundering, Anti-Terrorism Financing and Proceeds of Unlawful Activities Act 2001 (Act 613)	Securities Commission Malaysia
Capital Market and Services Act 2007	Securities Commission Malaysia

As the central bank of Malaysia, BNM is one of the main the regulatory bodies involved in preventing Ponzi schemes. According to an interviewee at BNM, the central bank uses a broader definition for Ponzi scheme. He added that:

> *"a scheme can be considered as a Ponzi scheme if there is an offer by an entity or a company that promises a fixed return on investment that are unrealistically high with the intention to deceive the public".*

At BNM, the focus is not only on preventing Ponzi schemes but also various other illegal activities such as illegal deposit taking, illegal forex trading, illegal remittance, illegal insurance and illegal money changing business. As such, any schemes that are clearly involving any of these activities would be monitored by BNM as these are considered to be under the purview of the Bank.

Regulators such as BNM and Securities Commission Malaysia regulate investment matters through the Financial Services Act 2013 and Capital Market and Services Act 2007 respectively. Several convictions were given to Ponzi fraudsters under these laws. Cases such as PP v. Raja Noor Asma bt Raja Harun [2013] 9 MLJ 181 have shown that despite the Sessions Court and High Court being sympathetic to investors for losing money, the decisions made by the judges of the Court of Appeal in October 2013 who unanimously allowed the appeal by the prosecution (who acted on behalf of Bank Negara Malaysia and the Securities Commission Malaysia) to forfeit the money proved that investors' claims must be bona fide claims. In this case Raja Noor Asma was charged for defrauding investors and trading in future contracts without a license. She pleaded guilty, convicted and sentenced to imprisonment of five years for each of the four charges and a RM5 million fine in default of six months' imprisonment. She was also charged to offences under the Anti-Money Laundering and Anti-Terrorism Financing Act 2001 (AMLATFA) and sentenced to a two-year imprisonment for each of the 50 charges that are to run concurrently but consecutively after the five-year imprisonment. In total, Raja Noor Asma had to serve a seven-year jail-sentence. The Securities Commission Malaysia convinced the court to impose a retributive and deterrent sentence on the grounds of public policy, i.e. to preserve the interest of the public considering the huge amount of investors' funds. (Mohd Sulaiman et al., 2016). The court decided that the victims had failed to discharge the burden of the requirements under Section 61(4) of the AMLATFA when claiming back their money from the investment.

Section 61(4) of the AMLATFA states, "The court or enforcement agency shall return the property to the claimant when it is satisfied that:

1. the claimant has a legitimate legal interest in the property;

2. no participation, collusion or involvement with respect to the offence under subsection 4(1) which is the object of the proceedings can be imputed to the claimant;

3. the claimant lacked knowledge and was not intentionally ignorant of the illegal use of the property, or if he had knowledge, did not freely consent to its illegal use;

4. the claimant did not acquire any right in the property from a person proceeded against under circumstances that give rise to a reasonable inference that any right was transferred for the purpose of avoiding the eventual subsequent forfeiture of the property; and

5. the claimant did all that could reasonably be expected to prevent the illegal use of the property.

Our findings showed that law and regulations play a vital role in prevention of Ponzi schemes. However, despite its importance, the current lack of a specific law to incriminate Ponzi fraudsters have caused a challenge for relevant authorities to take speedier actions. This has led the Ponzi fraudsters to continue with their scheme by taking advantage of the limitations of the current legislation in preventing the fraud. Hence, a new law on Ponzi schemes is timely and highly warranted given the exponential growth of such schemes in recent years.

Enforcement

The enforcement actions by the regulatory authorities are important in detecting and preventing Ponzi frauds as depicted in Figure 2. One of the main enforcement agencies in Malaysia is the Royal Malaysia Police. In their effort to enforce laws on commercial crimes, Royal Malaysia Police set up of a formal department known as the Commercial Crime Investigation Department. The department was established in the police headquarters in Kuala Lumpur in 2006 and headed by a Director appointed by the Police Commissioner and assisted by two Deputy Directors namely Deputy Director I (Investigation) and Deputy Director II (Administration). The main functions of the the Commercial Crime Investigation Department are to arrest, carry out investigations and prosecute white collar criminals who commit fraudulent acts, criminal breach of trust, cyber crime forgery and others whether such activities are committed by individuals or by syndicates. This list includes frauds of Ponzi schemes.

Royal Malaysia Police defined Ponzi schemes as investment schemes that have the element of cheating based on the provisions of section 420 of the Malaysian Penal Code. The Code states that "Whoever cheats and thereby dishonestly induces the person deceived, whether or not the deception practiced was the sole or main inducement, to deliver any property to any person, or to make, alter, or destroy the whole or any part of valuable security, or anything which is signed or sealed, and which is capable of being converted in a valuable security, shall be punished with imprisonment for a term which shall not be less than one year and not more than ten years and with shipping, and shall also be liable to fine." Based on the Code, Royal Malaysia Police will proceed with the investigation on the cheating offences when the schemes involve deception, dishonest inducement of delivery of property as well as wrongful gain and wrongful loss. Common examples of Ponzi schemes detected include the "get-rich-quick schemes", pyramid-based direct selling, illegal forex trading, Bitcoin, commodity trading as well as recreation club membership.

A review of a document from the Royal Malaysia Police revealed that in 2017 and 2018, there were 43 companies and 10 companies respectively that were listed on the "Police Radar" as potential Ponzi schemes. The amount of financial losses ranged from around RM5,000 (or approximately USD1,200) to RM1.2 billion (or approximately USD285,850,000) in 2017 alone. In 2018, although fewer companies were suspected to be Ponzi schemes, the lowest financial losses in each case amounted to an estimated amount of RM650,000 (or approximately USD155,000) while the highest was RM46,824,000 (or approximately USD11,153,883). The sheer amount of financial leakages associated with Ponzi Schemes are clearly alarming. This has led Royal Malaysia Police to watch closely on suspected activities linked to Ponzi Schemes. Interviewees further stated that in order to monitor the crime and to enable swift action against the fraud to be taken, Royal Malaysia Police relies on both a technology-enabled reporting system and daily face-to-face meeting. The meeting is used to report on daily crimes among the staff. In general, a specific alert is made when the police receives more than ten complaints regarding a particular case. Complaints on Ponzi schemes are either initiated by individuals who claim as victims themselves or made through a third party such as a consumer association. This is because as noted by Ganzini, McFarland and Bloom (1990), victims do feel embarrassed to admit their mistakes of joining the schemes. These findings are consistent with Mohd Sulaiman et al. (2016) who suggest that enforcement is essential in ensuring successful custodial sentence of imprisonment and compensation for investors.

CONCLUSIONS AND RECOMMENDATIONS

Key findings of this study highlight that prevention of Ponzi schemes should be addressed holistically. The modus operandi used such as digital platforms to promote schemes, mastermind heading a group of individuals and the use of public figures, influential persons and celebrities will reach out a greater scale of potential victims. Characteristics of victims such as lack of financial knowledge and gullibility play a significant role in helping the mastermind to succeed in their scheme. Fraudsters who are eloquent with good communication skills and excellent public relations are able to induce their victims to fall prey.

Findings of this study also indicated that the prevention measures are led by three core elements consisting of education, regulations and enforcement. These elements should be well coordinated and communicated to ensure effective prevention of Ponzi schemes. Proper education strategies have been found to be the best approach to prevent Ponzi schemes. Education is not only important for investors, the warning on fraudulent investments must also reach the younger generations. When education is given the highest priority, the researchers believe there is a good chance to break the chain of Ponzi fraud. Findings also revealed that regulators and law enforcement agencies do undertake preventive measures but they differ in their strategies. The absence of specific law on Ponzi schemes has led to different legislations being relied on in detecting, investigating and preventing fraud. Thus, this study recommends that there should be a single legislation which deals specifically on Ponzi schemes, consistent with Padil et al. (2020). Due to the emergence of newer and more innovative Ponzi schemes in recent years, both regulators and law enforcement agencies are constantly faced with new challenges related to tracking and handling innovative Ponzi schemes. This may have posed difficulties in their effort to prevent fraud. This study therefore recommends that all relevant authorities need to keep updated with the latest technology used by fraudsters as their modus operandi.

This research is limited to only three relevant authorities identified as having key roles in preventing Ponzi schemes. Challenges were faced in obtaining information since some information could not be disclosed due to secrecy (Abdul Ghani, Abdul Halim & Abdul Rahman, 2019) and it will only be released if it has become public documents. Researchers recommend future studies to broaden the perspective by investigating other institutions such as the Ministry of Domestic Trade and Consumer Affairs and the Malaysian Communications and Multimedia Commission. Despite these limitations, finding of this study adds current evidence to the existing limited body of literature on Ponzi Schemes.

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