

## A-Rod and Financial Fraud

The New York Yankees are paying Alex Rodriguez more than \$275 million over ten years to play third base, making Rodriguez the highest paid player in baseball history. According to a news leak in February, Rodriguez was one of more than one hundred players testing positive for steroids in a 2003 test of players conducted by Major League Baseball.

While many want to make the steroid scandal into a morality play, there are problems with this simplistic approach. Credulous fans were thrilled when long-standing home run records started falling like autumn leaves; less-credulous team owners were thrilled when they booked the resulting revenues from record attendance and media contracts. Aging baby boomers were thrilled to identify with aging players who, on the downhill side of their careers, could suddenly rebound and outperform much younger competition.

There are many victims of baseball's steroid scandal, including legions of statistics-obsessed fans, wringing their hands about how to write the record-books that now include drug-enhanced entries. We feel the most empathy, however, with the baseball players who did not use artificial enhancements. By not releasing the names of the players other than A-Rod that tested positive for steroid use, Major League Baseball has made *all* players suspect. Every time a light-hitting utility infielder goes 3 for 5 in a game, cynics will question the legitimacy of the performance. It is hard enough for baseball's regulators to catch a player taking steroids, but it is impossible for a clean player to prove the negative, that he did not take steroids.

Honest financial advisers face a similar predicament now that operators of Ponzi schemes (fraudulent investment operations where supposed "returns" to investors are paid out of their own money or money from subsequent investors) seem to be part of the daily news cycle. For those of a certain age, Richard Nixon ruined the effectiveness of the plain assertion "I am not a crook." Declaring he is doing nothing wrong is exactly what a con artist will do, and nobody is more convincing than a sociopath. Just like the honest baseball players, it is hard for honest financial advisers to prove they are honest.

As with baseball, attempts to make events on Wall Street into a morality play will fail. It is illogical to condemn Ponzi schemes on the one hand while ignoring Social Security, Medicare and Medicaid reform on the other. Future generations, saddled with the repayment of the

cascade of new government bailout debt and entitlement obligations may be less than impressed with our outraged denunciations of financial operators who could not deliver on their promises.

*“There is nothing so bad but it can masquerade as moral.”*

– Walter Lippmann

There are two common elements of most of Wall Street’s recent swindles. The first is that the returns from the investments, relative to their supposed lack of volatility, seemed “too good to be true” – and they were. The second is that most of the alleged con artists avoided regulated sectors of

the financial markets. To invest with Sir Allen Stanford, after all, you had to buy offshore certificates of deposit in Antigua (Antigua because the Montserrat regulators threw him out, a fact easily discoverable by any potential investor with sufficient curiosity). Bernie Madoff ran a hedge fund, set up expressly to avoid mutual fund-like regulation. Some investors were not aware of the difference in regulation, but others flocked to it because they believed the exotic, unregulated, non-transparent nature of the investments made them something “special.” In the more regulated, un-special sector of the financial services industry, some mutual fund managers made very stupid decisions in the recent market decline, but none that we are aware of stole client money. Lord Acton assured us that absolute power corrupts absolutely; he could have gone on to observe that credulity (of the kind exhibited by clients of Messrs. Madoff, Stanford and their ilk) also corrupts absolutely.

Lest you think that we are stretching to link baseball’s steroid scandal with the recent financial markets, consider that the New York Yankees, employers of A-Rod, recently broke off negotiations with Bank of America regarding naming rights for the new Yankee stadium. The reason? Bank of America received a bailout from the Troubled Asset Relief Plan (TARP), and some understandably thought it unseemly to use taxpayer money to name a baseball park. The Yankees had good reason to be nervous – there was a fuss about the cross-town New York Mets playing at “Citi Field,” the result of Citigroup, recipient of \$45 billion of government bailout money (to date), paying \$400 million over 20 years for the naming rights to the field. Coincidentally, the owner of the Mets was a victim of Bernie Madoff. If Citigroup goes under, perhaps the Mets will finish the season playing at “Fed Field.”

If you send your investment money to whomever promises the best returns, you are pitting potential service providers against one another in a contest where the winner is the biggest liar. Human nature is odd but invariant. A-Rod, Barry Bonds and Roger Clemens were sure Hall of Fame inductees *before* they knowingly broke baseball’s drug rules. Given the size and scope of their alleged illegal acts, Sir Allen Stanford and Bernie Madoff were presumably smart enough and hard working enough to be very successful in honest endeavors, a depressing but unremarked upon feature of their alleged swindles. You probably can achieve your financial goals with a rational, reality-based investment plan; you assuredly cannot by giving your money to a con artist. Despite the recent unsettled markets, there still is a link between risk and return. You should be suspicious of anyone claiming that you can have the returns without the risk. When you take on investment risk, however, it should be as part of an intelligent, transparent process. We can help – contact us at (503) 419-3938 or at [www.sigmainvestment.com](http://www.sigmainvestment.com).