Legacy Trust

Investment Perspectives

The Hucksters Handbook: Four Tips, Tricks and Insights for Crooks, Swindlers, and Delusional Thinkers

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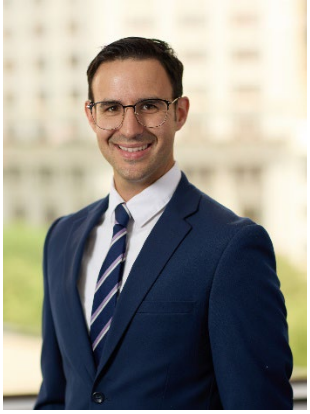

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Key Takeaways

- While each fraudster is unique, many of the schemes share similar qualities
- It is not always easy to spot a fraud in the moment, but oftentimes they will eventually be exposed
- There's truth to the old adage that if something sounds too good to be true, it probably is

If there's an opportunity for making a quick buck, there will be opportunities to exploit the rules to do so. From rare wines, to cryptocurrency, to scientific discoveries and more, there will always be people who will cut corners, bend the truth and outright lie in order to push their products. Below are four rules that many of these modern-day snake oil salespeople follow.

"Rodenstock is charming and debonair. He is also a con artist," begins the opening salvo delivered by Bill Koch's 2006 civil complaint against Hardy Rodenstock, world-renowned wine trader. Koch alleged that over several years, Rodenstock (whose legal name was Meinhard Goerke) had been in possession and sold several bottles of French wine that Rodenstock had claimed belonged to the third President of the United States, Thomas Jefferson. While Koch had never purchased directly from Mr. Rodenstock, as the originator of the bottles, Koch claimed that it was Rodenstock who had orchestrated a decades-long scheme to pass along expensive wines as priceless.

The numbers didn't make sense, but that didn't matter. All that mattered was that they kept going up; cryptocurrency valuations, deposits, and profits. All up up up. It looked like an unstoppable ride to the moon until it all came ingloriously crashing back to earth. In November of 2022, Sam Bankman-Fried's Bahamas-based cryptocurrency exchange came under heavy scrutiny due to a report of irregularities in its accounting, compounded with a lack of regulatory oversight. After the initial shock, Sam's goal no longer became growth. It became sell the business as quickly as possible. But when the only buyer who was willing to pay the ask price had a look at the books, they walked away within a day. Three days later, Sam Bankman-Fried was arrested by Bahamian authorities and within two weeks was on his way back to the United States, facing criminal and civil charges by the DOJ, SEC and CFTC.

Elizabeth Holmes had gone from Stanford dropout to founder to visionary in the span of a decade. Her company, Theranos, had gone from a $30 million valuation in 2004 to a peak of $10 billion in 2015. This lofty amount was based on proprietary technology that would be able to revolutionize blood tests. The only problem was that the technology did not work. In 2018, after Theranos had settled several previous lawsuits with investors, authorities charged the company's executives with wire fraud.

If there is money to be made in a hurry, there will be those that will try to make that happen, especially if legality is more of a suggestion than a necessity. While some are more willing than others to move from beyond the morally ambiguous and into the actually illegal, many of these hucksters, shysters and scammers share similar qualities across their schemes, plots and skullduggery. Below are some of the ways in which these people operate, as well as ways you might be able to spot their deception before it's too late.

Rule 1: Your Product/Invention/Idea Will Change The World

In between leaving Stanford in 2003 and the complete dissolution of her company in 2015, Elizabeth Holmes had stated that the goal of Theranos was to "democratize healthcare" by extracting vast amounts of data from a few droplets of blood. Despite being told by several medical experts that it could not be done, Holmes (ultimately to her detriment) persisted. Even after an article in The Wall Street Journal had discredited much of the company's claims, Holmes was adamant, stating, "This is what happens when you work to change things, first they think you're crazy, then they fight you, and then all of a sudden you change the world."

In a May 2022 piece (written about six months before the fall of FTX) "Time" magazine writer Andrew R Chow posited that Sam Bankman-Fried's philosophy of effective altruism could be a driver to "help democratize financial markets and reduce poverty and corruption." Meanwhile, Bankman-Fried's own cryptocurrency hedge fund, Alameda Research was committing blatant acts of corruption almost hourly.

While there are revolutionaries among us that are working to change the world, there are many others who claim to have these grand ideas that either fail or never plan to deliver on their promises.

Rule 2: Ideally, Both the Leader and the Followers are True Believers, But You Really Only Need One or the Other

As Zeke Faux explains in his book "Number Go Up," not everyone who bought into Bitcoin believed it was going to revolutionize and democratize international finance. Fortunately, they didn't all have to believe, just as long as there is someone else left holding the bag when it all goes to pieces. In a good con, it's irrelevant whether people buy in because they truly believe in it or because they see a chance to make a quick buck, or simply because they're afraid of missing out. A huckster can make the ride run for years and generate several billions of dollars before it all comes to an end if either they or their "customers" believe in the project.

Rule 3: Replace Proper Due Diligence with Influencers

Hardy Rodenstock had Bill Koch buying his wine. Elizabeth Holmes had Rupert Murdoch as an investor and Henry Kissinger as a board member of Theranos. Sam Bankman-Fried had Tom Brady, Giselle Bündchen and Larry David as spokespeople for FTX.

If you are going to swindle, you will want the extremely wealthy and influential to be on board. They serve a multitude of purposes. First, who wouldn't want to put their money in the same exchange as a six-time Super Bowl winner? A celebrity endorsement can help bring your scheme from a small niche of people to the masses. Second, a celebrity endorsement gives it an air of authenticity. These people are all incredibly famous and wealthy, so of course they must have done their due diligence before tying their name and reputation to it and investing in it, right? Right? Or did they get taken for a ride just like everyone else? Having a wealthy and influential spokesperson will not guarantee your success, but it may help extend its runtime.

Rule 4: When in Doubt, Just Commit Fraud

During his investigation into Hardy Rodenstock, Bill Koch had hired a retired FBI agent to look into the wine purveyor. During the investigation, it was discovered that "Hardy Rodenstock" was not distant relative of the wealthy Rodenstock family as he had claimed to be but was a Polish engineer. These facts on their own do not constitute fraud, of course. But as they dug into the Professor of Wine, they discovered he had no background in the wine industry at all.

In October 2015, John Carreyrou of the Wall Street Journal released an exposé of the Theranos. Through his investigation, he discovered that the Edison blood testing device was giving inaccurate results and the company had been using commercially available machines for most of its testing. There was no "secret sauce" and in fact the technology that had been touted as world-changing simply did not exist. Lying to patients wasn't what ultimately led to Holmes's undoing; it was lying to investors about the patients results that led to her conviction on three charges of wire fraud and an additional charge of attempting to commit wire fraud.

When Alameda Research, the investment fund arm of FTX needed cash to cover its losses, instead of abiding by the company's policy of closing out losing levered positions, Bankman-Fried would simply authorize the transfer of customer funds to Alameda to cover the shortfall. In November 2022, the cracks in the façade began to cause the crumbling of the whole exchange. Customers began to realize that their money might not be as safe as they had been led to believe and began to demand their funds back. Bankman-Fried's solution was to take to the internet and, with a tweet that was equal parts mealy mouthed and insipid, proclaim that "FTX is fine," which of course it was not. Within 24 hours of the tweet, $6 billion had been withdrawn from the exchange.

theranos

Top to bottom: The now-defunct Alameda Research logo, the now defunct theranos logo and a photo of the allegedly fraudulent Thomas Jefferson 1787 wine

A good con can last awhile. Almost always it will eventually end, oftentimes ignominiously and with many innocent victims in the wake. The goal of a good scam is to get out while the getting is good. Short of that, they can try to go legitimate before getting caught. Based on the traits of the grifters outlined above, most are unable to walk away until it's too late. It may not always be obvious or easy to spot frauds, but hopefully with the lessons of the Hucksters Handbook, people can be inoculated with a healthy dose of skepticism before the next time they find an opportunity that sounds too good to be true.