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# You don’t have to be a Dupe to be Duped: Lessons from the Madoff Affair

## By Dr. Robert Cialdini

By now, we’ve all been exposed to varied analyses of the highly publicized Ponzi scheme that Wall Street player Bernard Madoff is charged with orchestrating. While some analysts have focused on certain remarkable aspects of the fraud such as its size ($50 billion by most estimates) and its duration (going undetected for decades), I’ve been impressed by another remarkable feature: the level of financial sophistication of many of its victims. The list of those taken in by Madoff is rife with the names of hardheaded economists, seasoned money managers, and highly successful business leaders. With Madoff, it wasn’t another case of the fox outwitting the chickens; this guy bamboozled the other foxes. How’d he do it?

For me, the answer starts with the opaque and complicated nature of the hedge fund he was operating and the derivatives-based financial mechanism he was employing to create profits, which seemed beyond the comprehension of the majority of even the most sophisticated financial analysts. In addition, Madoff elevated the consequent mystery of what he was doing and how he was doing it by enforcing strict policies of secrecy around his business. But why, of all things, should the difficult-to-penetrate character of Madoff’s operation form the basis for his astounding effectiveness at persuading others to join him—especially others who, by virtue of savvy and experience, should have known better?

**The Power of Persuasion under Conditions of Uncertainty**

Under conditions of uncertainty like those Madoff cultivated, a pair of principles of social influence gain special traction: Authority and Social Proof. Let’s take each in turn and examine how they were commissioned by Madoff to advance his persuasive success.

<u>Authority</u>. When people are uncertain of what to do, they don’t look inside themselves for answers; all they’ll see there is vexing ambiguity. Instead, they look outside. One prominent place they look is to the counsel of experts, credible authorities on the topic. And, by any measure, Bernard Madoff certainly had the look of a credible authority in financial matters. He possessed expert credentials from long years in the investment industry. After starting his firm in 1960, he grew it into a juggernaut that was reported to be the largest dealer in NYSE-listed stocks in the United States. His firm helped to develop the NASDAQ, where he served as Chairman of the Board of Directors and where Madoff Securities became the exchange’s largest

market-maker. Beyond expertise, Madoff spent substantial time and money establishing a reputation for possessing the second element of credible authority—trustworthiness. He was active in an organization oriented to the self-regulation of the securities industry, the National Association of Securities Dealers, and even sat on its Board of Governors. Moreover, he was widely known for his good heart via multiple charitable and philanthropic involvements.

Against such a backdrop, we can begin to understand why so many knowledgeable and experienced financial professionals followed Mr. Madoff down the garden path. Under conditions of uncertainty, they did not look inside (to their own knowledge and experience) for direction. They looked outside to credible authorities on the topic. And, there were few on the murky topic of derivative-based hedge funds more credible than Bernie Madoff.

Social Proof. Besides authorities, do people seek any other source of external information when uncertain of how to choose? They do. They look to—and then follow—what most people just like them are doing. Here, the proof of a correct choice isn't based on knowledge or logic or empirical evidence; it's based on social evidence of what one's peers and those in one's social network have decided to do. For instance, if the evidence were clear that your friends and coworkers were flocking to a new restaurant for lunch, you'd likely follow suit. At developing, honing, and providing this kind of social evidence, the Madoff client recruitment program had few equals. Madoff is Jewish, and so, too, are the majority of his victims, who were often recruited at country clubs by Madoff's lieutenants, who were also Jewish and also members of the same country clubs. Plus, new recruits knew and were similar to past recruits, who served as unwitting sources of social proof that an investment with Madoff must be a wise choice "for someone like me." Of course, fraud of this sort is hardly limited to one ethnic or religious group. Called affinity schemes, these investment scams have always involved members of a group preying on other members of the group—Baptists on Baptists, Hispanics on Hispanics, Armenian-Americans on Armenian-Americans. Indeed, Charles Ponzi, who gave his name to the infamous Ponzi scheme that Madoff copied, was an Italian immigrant to the U.S. who fleeced other Italian immigrants to the U.S.

**Implications for Ethical Influence in Times of Uncertainty (Like Now!!)**

What lessons can be gleaned from the Madoff case for those who want to be influential but who refuse to tumble to Mr. Madoff's ethical level in the process? Honestly informing prospects, customers, clients, superiors, or coworkers of the views of legitimate authorities and/or the choices of comparable others is a both a potent and ethical route to persuasive success. But, to maximize the effect of these two sources of influence, there is one additional aspect to consider: They will have particularly strong impact under conditions of uncertainty, when people are looking outside rather than inside themselves for answers.

This means that when the economic environment has become unpredictable, as is currently the case—or even when business conditions have recently changed for more ordinary reasons, such as a new product introduction or a new organizational policy or the emergence of a new competitor—the resulting uncertainty will make audiences especially attentive and responsive to information about how experts and similar others are dealing with it. It also means that communicators would lose great persuasive leverage (more bluntly, would be fools) if they failed to marshal and honestly employ those two sources of information in their messaging at precisely these times.

Thus, when things are uncertain, the judgments and actions of authorities and of comparable others can provide a goldmine of persuasive resources. And that mine is…well…a terrible thing to waste.