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Securities Fraud and the Individual Investor

*United States Securities and Exchange Commission
American Association of Individual Investors, SV Chapter
May 14, 2016*



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Tips for Investors to Help Avoid Fraud

- ☐ *Research Both the Financial Professional and the Investment Product*
- ☐ *Be Aware of Common Red Flags*
- ☐ *Be Wary of Unsolicited Offers to Invest*
- ☐ *Be Thoughtful about Privacy and Security Settings*
- ☐ *Ask Questions*



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Research the Financial Professional

- ☐ **BrokerCheck:** *BrokerCheck is a free tool to help investors research the professional backgrounds of current and former FINRA-registered brokerage firms and brokers, as well as investment adviser firms and representatives.*
 - ☐ (800) 289-9999
 - ☐ FINRA.org or www.saveandinvest.org

- ☐ **Investment Adviser Public Disclosure (IAPD) database:** *IAPD features professional background information on individuals acting as investment adviser representatives and current and former investment adviser firms.*
 - ☐ (800) 732-0330
 - ☐ SEC.gov or www.adviserinfo.sec.gov

- ☐ **State Regulators**
 - ☐ North American Securities Administrators Association NASAA.org



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BrokerCheck can tell you...



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...what has been disclosed to regulators.



...about a broker's experience.



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...what has been disclosed to regulators.



...about a broker's experience.



...about what a broker or brokerage firm is able to do.



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Research the Investment

- ☐ **Stocks.** Use the SEC's Electronic Data Gathering, Analysis and Retrieval (EDGAR) database to research public companies. EDGAR provides free access to corporate information, including information about a public company's activities, registration statements, prospectuses, and periodic report.
- ☐ **Municipal Bonds and 529 College Savings Plans.** The Electronic Municipal Market Access (EMMA) database is a free website that contains information about municipal bonds and 529 college savings plans.
- ☐ **Mutual Funds.** Read the mutual fund prospectus and the annual and semiannual shareholder reports for each fund that you are researching. In addition, all these documents are usually posted on the fund company's website and may also be available through popular financial websites.
- ☐ **State-Registered Investments.** You should contact your state securities regulator to determine whether a particular investment product is registered with the state or whether the issuer of the investment product has claimed an exemption from state registration.



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Is the investment registered?

- To find out whether an investment product is registered, investors can check EDGAR, the SEC's online database of corporate filings.
- If the product is not in EDGAR, that could be a red flag!
- There are valid reasons why an offering might not appear in EDGAR – but registration provides access to important information about the company.



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Resource: EDGAR

www.sec.gov/edgar/searchedgar/companysearch.html



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Common “Red Flags” of Investment Fraud

- ☐ **It sounds too good to be true.** Any investment that sounds too good to be true probably is. Compare any promised return with the returns on well-known stock indexes. Be extremely wary of claims on a website that an investment will make “INCREDIBLE GAINS” or is a “BREAKOUT STOCK PICK” or has “HUGE UPSIDE AND ALMOST NO RISK!”
Claims like these are hallmarks of extreme risk or outright fraud.
- ☐ **Pressure to buy RIGHT NOW.** Don’t be pressured or rushed into buying an investment before you have a chance to think about – and investigate – the “opportunity.”
- ☐ **Lack of Documentation.** Be very skeptical of investments where the promoter will not provide you written documentation reflecting the promoter’s claims.



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Common “Red Flags” of Investment Fraud

- ❑ **Offers to invest outside of the United States.** You should carefully examine any unsolicited offer to invest outside of the United States. Many fraudsters set up operations outside the United States to make it more difficult for regulators to stop their fraudulent activity and recover their victims’ money.
- ❑ **Unregistered investments.** Ponzi schemes typically involve investments that are not registered with the SEC or with state regulators. Registration is important because it provides investors with access to information about the company’s management, products, services, and finances.
- ❑ **Unlicensed sellers.** Federal and state securities laws require investment professionals and firms to be licensed or registered. Most Ponzi schemes involve unlicensed individuals or unregistered firms.



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Be Wary of Unsolicited Offers to Invest

- ☐ Investment fraud criminals look for victims on social media sites, chat rooms, and bulletin boards. If you see a new post on your wall, a tweet mentioning you, a direct message, an e-mail, or any other unsolicited – meaning you didn’t ask for it and don’t know the sender – communication regarding a so-called investment opportunity, you should exercise extreme caution.
- ☐ Many scams use spam to reach potential victims. For example, with a bulk e-mail program, spammers can send personalized messages to millions of people at once for much less than the cost of cold calling or traditional mail.
- ☐ If you receive an unsolicited message from someone you don’t know containing a “can’t miss” investment, your best move is to pass up the “opportunity” and report it to the [SEC Complaint Center](http://www.sec.gov/complaint/question.shtml) (<http://www.sec.gov/complaint/question.shtml>).



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Be Thoughtful about Privacy Settings

- ☐ Investors who use social media websites as a tool for investing should be mindful of the various features on these websites in order to protect their privacy and help avoid fraud.
- ☐ Understand that unless you guard personal information, it may be available not only for your friends, but for anyone with access to the Internet – including fraudsters.
- ☐ Check the Following:
 - ☐ Default Settings
 - ☐ Biographical Information
 - ☐ Accepting “Friends”
 - ☐ Strong Passwords
 - ☐ Account Information – never list
 - ☐ Social Security numbers
 - ☐ Bank information



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Ask Questions and Check Everything Out

- ☐ Be skeptical and research every aspect of an offer before making a decision.
Investigate the investment thoroughly and check the truth of every statement you are told about the investment.
 - ☐ *Is the product registered with the SEC or state regulator?*
 - ☐ *Is the person registered with the SEC, FINRA, or state regulator?*
 - ☐ *Why is this investment suitable for me?*
 - ☐ *How does this investment make money?*
- ☐ Never rely on a testimonial or take a promoter's word at face value.
- ☐ You can check out many investments using the SEC's EDGAR filing system or your state's securities regulator. You can check out registered brokers at FINRA's [BrokerCheck website](#) and registered investment advisers at the SEC's [Investment Adviser Public Disclosure website](#).



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A Few Common Scams

Pump-and-Dumps and Market Manipulation

- ❑ “Pump-and-dump” schemes involve the touting of a company’s stock (typically small, so-called penny stock or “microcap” companies) through false and misleading statements to the marketplace.
- ❑ These false claims could be made on social media such as Facebook and Twitter, as well as on bulletin boards and chat rooms. Pump-and-dump schemes often occur on the Internet where it is common to see messages posted that urge readers to buy a stock quickly or to sell before the price goes down, or a telemarketer will call using the same sort of pitch.
- ❑ Once these fraudsters “dump” their shares at the pumped-up price and stop hyping the stock, the price typically falls, and investors lose their money.



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A Few Common Scams

Fraud Using “Research Opinions” and Online Investment Newsletters

- ❑ While legitimate online newsletters may contain useful information about investing, others are merely tools for fraud. Some companies pay online newsletters to “tout” or recommend their stocks. Touting isn’t illegal as long as the newsletters disclose who paid them, how much they’re getting paid, and the form of the payment, usually cash or stock.
- ❑ Fraudsters often lie about the payments they receive and their track records in recommending stocks. Fraudulent promoters may claim to offer independent, unbiased recommendations in newsletters when they stand to profit from convincing others to buy or sell certain stocks – often, but not always, penny stocks.
- ❑ *The fact that these so-called “newsletters” may be advertised on legitimate websites, including on the online financial pages of news organizations, does not mean that they are not fraudulent.*



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A Few Common Scams

High Yield Investment Programs

- ☐ These are unregistered investments typically run by unlicensed individuals – and they are often frauds.
- ☐ The hallmark of an HYIP scam is the promise of incredible returns at little or no risk to the investor.
- ☐ A HYIP website might promise annual (or even monthly, weekly, or daily!) returns of 30 or 40 percent – or more. Some of these scams may use the term “prime bank” program.



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A Few Common Scams

Affinity Fraud

- ❑ Affinity frauds target members of identifiable groups, such as the elderly, or religious or ethnic communities. The fraudsters involved in affinity scams often are members of the group, which may give the appearance of legitimacy to the fraud. These scams frequently involve Ponzi or pyramid schemes.
- ❑ Never make an investment based solely on the recommendation of a member of an organization or group to which you belong, especially if the pitch is made online. An investment pitch made through an online group of which you are a member, or on a chat room or bulletin board catered to an interest you have, may be an affinity fraud.
- ❑ ***Even if you do know the person making the investment offer, be sure to check out everything – no matter how trustworthy the person seems who brings the investment opportunity to your attention.*** Be aware that the person telling you about the investment may have been fooled into believing that the investment is legitimate when it is not.



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Common Persuasion Tactics Used by Fraudsters

Phantom Riches

Dangling the prospect of wealth, enticing you with something you want but can't have.



Source Credibility

Trying to build credibility by claiming to be with a reputable firm or to have a special credential or experience.



Social Consensus

Leading you to believe that other savvy investors have already invested.



RED FLAGS OF FRAUD

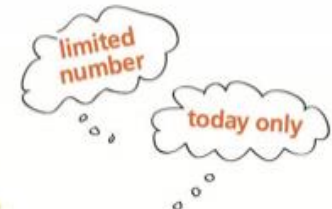
Reciprocity

Offering to do a small favor for you in return for a big favor.



Scarcity

Creating a false sense of urgency by claiming limited supply.





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OIEA Investor Alerts and Bulletins

- ☐ Fraudulent Stock Promotions (March 29, 2016)
- ☐ Zika Crisis May Give Rise to Investment Scams (March 9, 2016)
- ☐ Crowdfunding for Investors (February 16, 2016)
- ☐ Variable Annuities (November 24, 2015)
- ☐ Social Media and Investing –Stock Rumors (November 5, 2015)
- ☐ Investment-Related Radio Programs used to Defraud (September 23, 2015)
- ☐ Identity Theft, Data Breaches and Your Investment Accounts (September 22, 2015)
- ☐ Non-traded REITs (August 31, 2015)
- ☐ Beware of Fantasy Stock Trading Websites Offering Real Returns (June 17, 2015)
- ☐ Automated Investment Tools (May 8, 2015)
- ☐ Structured Notes (January 12, 2015)
- ☐ Private Placements Under Regulation D (September 24, 2014)
- ☐ Be on the Lookout for Advance Fee Fraud (September 9, 2014)
- ☐ Affinity Fraud (June 18, 2014)
- ☐ Investment Newsletters Used as Tools for Fraud (June 2, 2014)



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