

ALABAMA SECURITIES COMMISSION

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CONS FIND PROFIT IN GET-RICH-QUICK SCHEMES TIED TO ECONOMIC UNCERTAINTY

Alabama Securities Commission Identifies Most Common Investor Threats Among Financial Products and Practices

MONTGOMERY, ALABAMA (Aug. 23, 2011) – The Alabama Securities Commission (ASC) today released its annual list of financial products and practices that threaten to trap unwary investors, many by taking advantage of investors troubled by lingering economic uncertainty and volatile stock markets.

“Con artists follow the news and seek ways to exploit the headlines to their advantage while leaving investors holding an empty bag,” said ASC Director, Joseph Borg.

Borg said headline-related investor complaints reaching state securities regulators include questionable claims, such as: “Realize safety and appreciation in gold;” “Wave energy: the future to power our homes;” “Synthetic fuels take the oilman out of our pockets;” and “Invest in foreclosed homes, help others and make a fortune!”

“Promoters often offer investors an opportunity to get in on the ‘ground floor’ of new technology or ideas to help others and make a great economic return,” Borg said.

“Unsuspecting investors can be lured into these schemes, especially if they sound familiar. These offerings require careful research and a strong reminder that if it sounds too good to be true, it probably is not true, nor will it be profitable to anyone but the promoter.”

The following alphabetical listing of the Top 10 financial products and practices that threaten to trap unwary investors was compiled by the North American Securities Administrators Association, of which ASC is a member.

- **PRODUCTS:**
 - Distressed real estate schemes
 - Energy investments
 - Gold and precious metal investments
 - Promissory notes
 - Securitized life settlement contracts

- **PRACTICES:**
 - Affinity fraud
 - Bogus or exaggerated credentials
 - Mirror trading
 - Private placements
 - Securities and investment advice offered by unlicensed agents

Borg urged investors to learn the warning signs of investment fraud and independently verify any investment opportunity as well as the background of the person and company offering

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the investment. The ASC provides detailed background information about those who sell securities or give investment advice, as well as about the products being offered. Investigate the person and the investment BEFORE sending your hard earned money.

“Investors should do business only with licensed brokers and investment advisers and should immediately report any suspicion of investment fraud to us,” Borg said.

Additional information on how to protect yourself from investment fraud is available on the Commission’s website at www.alabama.asc.gov or by calling 1-800-222-1253.

2011 Top Investor Traps and Threats *Products and Practices*

Products

- **Distressed Real Estate Schemes.** Investment offerings involving distressed real estate have been on the rise following the collapse of the real estate bubble. While many legitimate investment offerings are tied to real estate, investment pools targeting distressed real estate have become increasingly popular with con artists as well as investors. Investments in properties that are bank-owned, in foreclosure, pending short sales or otherwise in distress inevitably carry substantial risks and should be evaluated carefully. Just like other securities, interests in real estate ventures also must be registered with state securities regulators.
- **Energy Investments.** Swindlers continue to attempt to trick investors by using high-pressure marketing tactics touting the mystique associated with untapped oil and gas reserves and bountiful production runs. Even genuine oil and gas investments almost always bear a high degree of risk. Investors must realize the distinct possibility that they could lose their total investment in legitimate ventures. Energy investments tend to be poor alternatives for those planning for retirement and should be avoided by anyone who cannot afford to strike out when trying to strike it rich.
- **Gold and Precious Metals.** Higher precious metal prices and the promise of an ever-appreciating, “tangible” asset have lured unsuspecting investors into a variety of scams. Many recent schemes are variations on old themes: a promoter seeking capital for extraction equipment to reopen a long dormant mine in exchange for a full refund plus interest and a stake in the mine. In another case, operators claimed to have special coins or nuggets that they can store or trade for investors in special markets for high profits and returns. Investors suffered heavy losses in each of these cases. And despite ubiquitous promises to the contrary, there are no guarantees with gold or precious metals, even in legitimate markets. In the spring of 2011, silver’s value declined by 30 percent in a single three-week period.
- **Promissory Notes.** Investors seeking safety in uncertain economic conditions or those enticed by the promise of big returns through a private, informal loan arrangement may suffer deep losses investing in unregistered or fraudulent promissory notes. These notes give investors a false sense of security with promises or guarantees of fixed interest rates and safety of principal. However, even legitimate notes carry some risk that the issuers may not be able to meet their obligations. Often initially pitched as personal loans or short-term business arrangements, most promissory notes and the persons who sell them must be registered with state securities regulators. Unregistered promissory notes are often ‘covers’

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for Ponzi schemes and other scams. Investors should check with their state regulator to determine whether a promissory note and the seller/borrower are properly registered.

- **Securitized Life Settlement Contracts.** Life settlement contracts are investments in the death benefits of insurance policies that insure the lives of unrelated third parties. Legitimate investments in life settlement contracts involve a high degree of risk, and investors may be responsible for routinely paying costly premiums for policies that insure people who outlive their life expectancies. Outside the legitimate offerings, crooks are embracing new schemes to deceive even cautious investors. For example, “securitized” life settlement contracts are increasingly popular investments that combine life settlement contracts with traditional securities, such as bonds that supposedly guarantee a fixed return on a fixed date, regardless of whether the insured outlive their life expectancies. This risk-reducing structure has too often proven fraudulent and left victims with nothing but worthless paper issued by a bonding company that does not maintain sufficient assets to fulfill the guarantee, operates in an unregulated overseas territory or simply does not exist.

Practices

- **Affinity Fraud.** Marketing a fraudulent investment scheme to members of an identifiable group or organization continues to be a highly successful and lucrative practice for Ponzi scheme operators and other fraudsters. A recent national study of Ponzi schemes over the past decade found that one in four were marketed to affinity groups to increase the scheme's credibility and build the fraud. The most commonly exploited are the elderly or retired, religious groups, and ethnic groups. Investment decisions should always be made based on careful evaluation of the underlying merits rather than common affiliations with the promoter.
- **Bogus or Exaggerated Credentials.** State securities regulators have led the effort to prevent the misuse of credentials or designations intended to imply special expertise or training in advising senior citizens on financial matters. Now, state regulators are noting an increase in the use of other bogus credentials or exaggerated designations. State securities regulators have encountered salesmen pitching financial services or products with nonexistent law degrees or CPA certificates and expired or nonexistent CRD numbers. Others have boasted of impressive sounding designations that prove to be meaningless. In one case, a broker listed “C.H.S.G.” after his name on his business card – “Certified High School Graduate.” In every circumstance, investors should press for full disclosure and the meaning behind all designations, and should check with their state regulator if they have any suspicions about claimed credentials.
- **Mirror Trading.** The securities market is constantly evolving to provide investors with new products, different platforms and a variety of choices. The latest evolution is “mirror trading,” which is promoted as an automated trading platform that ensures investors will participate in real-time transactions placed or executed by a skilled and knowledgeable third party. Whenever the third party executes a trade in his or her account, the same trade is mechanically placed on behalf of the investor in the investor’s account. Investors should not be lulled into a false sense of security, and they need to continue to objectively evaluate and carefully consider all new or popular investment platforms. They should also recognize that unscrupulous traders and promoters may use trendy platforms such as mirror trading as a way to launch fraudulent schemes or manipulate markets by lying about their qualifications, misrepresenting the success of their strategies, or concealing their motivations and conflicts of interest.
- **Private Placements.** Investors should be aware that, even in the case of legitimate issuers, private placement offerings are highly illiquid, generally lack transparency and have little

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regulatory oversight. In the United States, the federal exemption for private placement offerings provided under Rule 506 of Regulation D continues to be a prime area of abuse for scam artists. Although properly used by many legitimate issuers, unscrupulous promoters use Rule 506 to cloak an otherwise fraudulent offering in legitimacy.

- **Securities and Investment Advice Offered by Unlicensed Agents.** State securities regulators have identified a consistent increase in investor complaints regarding salesmen unlicensed as securities brokers or investment advisers giving investment advice or effecting securities transactions. For example, insurance agents offering securities or investment advice without a securities license have not demonstrated sufficient expertise to legally recommend that an investor liquidate securities holdings in favor of insurance products. Investors are often unaware that their insurance agent may not be licensed to give investment advice, and these recommendations too often turn out to be unsuitable or result in investors placed in under-performing products or those with hidden fees or long lock-up periods. Investors should insist that any time anyone recommends or suggests any transaction related to an investor's stocks, bonds, mutual funds or other securities holdings, the person must produce a proper license.

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For further information contact Dan Lord, Education and Public Affairs Manager, 334-353-4858.

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