

# THE UNLUCKY 13

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In a classic example of the Markowski Investments/Watchdog on Wall Street echo chamber many of the scams and investment fraud that we have been highlighting and discussing for years have been named by the North American Securities Administrators Association (NASAA) in a list of the most widespread ways investors are likely to be trapped in 2006.

### **Affinity Fraud**

Members of closely knit religious, political, or ethnic groups are targeted frequently by con artists. Their pitch is essentially, "since I am like you and believe like you, you can believe in me and in what I say." When an investment is presented in this context, the potential investor should be extremely wary. This pitch seeks to substitute an emotional appeal for careful analysis and critical thought. This is becoming more and more prevalent through churches and other religious institutions around the country. It is in our humble opinion that there is probably a special place in Dante's inferno for the perpetrators.

### **Churning**

This is old abusive sales practice in which unethical stock-brokers make unnecessary excessive trades for the sole purpose of generating commissions.

### **Equity Indexed Certificates of Deposit.**

This is a relatively new scam that has been targeting senior citizens all over the country. These EICD's are not FDIC-insured, bank-issued certificates of deposit with guaranteed principal and interest. Equity Indexed CDs are hybrid securities products that offer an interest coupon payment or return that is based on a stock market index. Individuals are tricked into believing that their interest payments and principal are guaranteed by seeing the certificate of deposit label however, returns are not FDIC insured. EICD's are complex high-fee securities that promise a rate of return calculated over a defined period of time based upon some form of securities market index. A declining stock market means the possibility of no return on your investment. As a result, these products pose all sorts of liquidity problems and are not suitable for seniors who may need the money for retirement income.

### **Oil and Gas Investment Fraud**

High oil prices mean oil and gas scams will continue to attract victims. Oil and gas deals are complicated investments that generally require a significant investment, often requiring a minimum deposit of thousands of dollars. Increasingly, these deals are being promoted via the Internet with claims of attractive tax advantages. Sales materials with "official-looking" surveyor maps and "geologist" opinion letters touting the likelihood that the "managers" of the drilling enterprise will hit pay dirt are sent regularly to prospective investors more than 1,000 miles from the region being "prospected."

### **Personal Information Scams**

The first step in separating a victim from his or her money is convincing the victim to divulge personal financial information. Con artists frequently style themselves as "senior specialists" or adopt a pretext of preparing "living will" or a "living trust." A pretext that is of current concern to insurance and securities regulators is the offer to help senior citizens qualify for prescription benefits by preparing forms. In the guise of filling out forms, the crook may ask unnecessary questions about personal financial assets. To the con artist, this information provides a comprehensive laundry list of what is available for the taking.

### **Prime Bank Schemes**

These schemes often promise high-yield, tax-free returns that are said to result from “off-shore trades of bank debentures.” Investors are told that only very wealthy people can get the benefit of these programs but the promoter is able to make it available to the victim. Wealthy trust-fund kids are often targeted by these scams. Sometimes the victim is required to execute a “confidentiality agreement” in order to invest and is told not to consult an attorney, accountant or financial planner because they keep these programs for the “big boys” and will deny that they exist. There are no such programs, no such debentures and no such high-yield trades. These prime bank schemes are the securities equivalent of a purse snatch. Once the seller has your money, it’s literally gone off shore for good.

### **Pump and Dump Schemes**

This time-tested scam has been utilized by unethical broker-dealers and stock promoters for over twenty years. Brokers pump up the value of low-priced securities traded on the NASDAQ “pink sheets” and then dump the stock after naïve investors have purchased the stock at inflated prices. The balloon breaks when the promoters no longer maintain the myth that there is value in the shares and investors are left holding worthless shares. This scam is not limited to the boiler room operations of downtown New York and south Florida, all of the major brokerage firms utilized the same scam to drive up technology stocks in the 1990’s.

### **Recovery Rooms**

Con-artists use the names and financial information of victims who have lost money on pump and dump or other schemes, who then promise, in return for a fee that the victim must pay in advance, to recover the money lost in the worthless investment. These “sucker lists” are bought by crooks who know that people who have been deceived once are vulnerable to additional scams; especially scams that give hope of recovering lost money. If you have been the victim of a fraud, never give out your credit card or other personal information to someone who contacts you with a promise to recover your money. Remember, in the scam world this caller is known as a “reloader” and he is setting you up for a second bite at the apple. This scam is usually played out by the same individuals that pull-off the pump and dump schemes.

### **Registered High-Interest Promissory Notes Publicly Advertised**

Generally, the higher the return promised, the greater the risk to your money. A track record of paying high interest and repaying principal is not an assurance that you will get your money back if the company fails. These notes are not suitable for retirement funds.

### **Sale and Leaseback Contracts**

In an attempt to avoid the investor protections of securities laws, some investments are structured to resemble the sale of a piece of equipment such as a payphone, ATM machine or Internet booth located at a remote venue where the investor cannot service and maintain the equipment and must enter into a servicing agreement. In order to make the deal more attractive, investors are told that after a given period the equipment can be sold back to the seller at the investor’s original purchase price. The investor is also promised a specific rate of return. In a variant of this scheme, a real estate interest such as a long-term lease in a resort community is sold instead of physical equipment. Frequently the equipment or property does not exist and the seller lacks the financial capacity to keep the promise of repurchase.

### **Self-Directed Pension Plans**

Many types of securities fraud require the victim to remove funds from legitimate investments such as stock brokerage accounts, insurance policies, deferred compensation plans and mutual funds so that they can be invested in a worthless scam. This scam may begin with advice to convert an employer-sponsored pension into a self-directed pension plan. While these plans may serve legitimate investment purposes, all too often they only serve to benefit the scam artist.

### **Unsuitable Recommendations**

Just as every investor is different, so too should be their portfolios. What may be a suitable investment for one investor may not be right for another. All of the individuals that are on

television or radio handing out stock picks to callers are not acting as a fiduciary and should be given as much credence as a degenerate gamblers NFL picks. True financial advisors must know their customers' financial situation and refrain from making recommendations of securities that they have reason to believe are unsuitable. How can some "financial guru" make an investment recommendation to someone based on a 30 second conversation? Would a doctor recommend intrusive brain surgery based upon a 30 second phone call?

### **Variable Annuities**

Variable annuities are tax-deferred investments that typically place mutual funds inside of an insurance wrapper for tax deferred potential investment growth. While these products can be legitimate investments, they are more often sold because of their high-commission to the salesman. Commissions to those who sell variable annuities can be as high as 15%, which provides incentive for sellers to engage in inappropriate sales. Variable annuities are only suitable for a very small percentage of the investing public and generally are not appropriate for most seniors, yet they are one of the most popular investment products with brokers and insurance salesman today. Variable annuities carry heavy penalties for early withdrawals which also make them unsuitable for short-term investors. Be especially wary of any broker who wants to sell you a variable annuity to hold inside a 401(k) or IRA. You are already getting tax-deferred growth in an IRA or a 401(k), and the variable annuity simply adds a layer of cost with no additional tax benefit.

We have been educating investors in regards to these and other popular frauds for years and are happy to see the NASAA follow suit. If you feel you may have been victimized by any of the following please contact us at (800) 447-0579 with any questions you may have.