

Washington DFI Warns of Top 10 Financial Traps

Local News

Posted by: David Haviland

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Olympia ‐ With a new school year about to begin, the Washington State Department of Financial Institutions Securities Division reminds investors to take stock of their financial education and arm themselves with the knowledge to sidestep this year’s Top 10 Investor Traps.

DFI’s Director of Securities Michael Stevenson says investors under pressure from the struggling economy need to resist the lure of sales pitches to rebuild their savings.

“An educated investor should be alert at all times, but especially when money is tight,” Stevenson explained. “Falling into an investment trap makes it harder to get back on solid financial ground.”

The following traps were determined to be the top 10 for 2009 by the Enforcement Trends Project Group of the North American Securities Administrators Association, of which DFI’s Securities Division is a member. Many of the traps identified promise high returns to cash-strapped investors -- but provide little, if any, disclosure of risks and offer high commissions to aggressive sales forces.

“When it comes to investing, verify everything and everyone before you part with your money,” Stevenson said. “Education and information are an investor’s best defense against investment fraud.”

Investors should always be wary of unsolicited financial advice or investment opportunities. Before investing any money, consumers should contact their state securities regulators, which provide detailed background information about people and companies selling securities or giving investment advice, as well as the products being offered.

DFI’s Securities Division identified

real estate investment schemes, promissory notes, private placement offerings, natural resources investments and Ponzi schemes as the greatest potential threats to investors this year. Details on all 10 traps can be found online at <http://www.dfi.wa.gov/consumers/topscams.htm>. For more information, contact the Securities Division at 877-RINGDFI or visit our Web site at www.dfi.wa.gov/sd.

Ponzi Schemes. Despite the heightened awareness of Ponzi (or pyramid) schemes following Bernard Madoff’s multi-billion dollar fraud and 150-year prison sentence, these scams continue to trap investors. The Ponzi scheme is a house-of-cards swindle in which high returns are paid to initial investors using funds from later investors. The later investors often end up losing all or most of their money to the promoter.

Real Estate Investment Schemes. State securities regulators have noted a marked rise in scams disguised as offers to help homeowners caught facing foreclosure “save” their homes or “fix” their mortgages -- usually in exchange for a fee paid in advance. Most of these advance-fee offers only generate a quick profit for the con-artist and provide little or no benefit

to the consumer.

Short-term Commercial Promissory Notes. Many seniors have lost their life savings by investing in short-term commercial promissory notes that are nine months or less in duration. The seller of these notes may tout them as being "insured" or "guaranteed," but the insurance companies generally are located outside of the United States, are not licensed to do business in the United States, and lack the resources necessary to deliver on the promised guarantees.

Private Placement Offerings. Private placements offer businesses the opportunity to raise capital by selling securities to a relatively small number of investors as opposed to a public offering made through national securities markets, often under a federal registration exemption (Regulation D, Rule 506). Companies using this exemption can raise an unlimited amount of money without registering the offering with the SEC. Although properly used by many legitimate issuers, the exemption has become an attractive option for con artists, as well as individuals barred from the securities industry and others aiming to steal millions of dollars from investors through false and misleading representations.

Natural Resource Investments. DFI's Securities Division expects to see a continuing rise in energy and precious metals scams promising quick, high returns. Investors anxious to recover losses quickly likely will be hooked by fraudulent oil and gas "investments" as well as fraudulent offerings of investments tied to natural gas, wind and solar energy, and the development of new energy-efficient technologies.

Gold Bullion and Currency Scams. With the high price of gold, investors should beware of gold bullion scams in which the seller offers to retain "purchased" gold in a "secure vault" and promises to sell the gold for the investor as it gains in value. In many instances the gold does not exist.

Speculative Inventions and New Products. New products are for venture capitalists who know how to assess the risks. They are not good investments for your retirement money even though they may promise high returns.

Life Settlements. State securities regulators long have been concerned about life settlements -- commonly known as "viaticals" -- and the rising popularity of these products among investors has prompted a recent congressional investigation. While life settlement transactions have helped some people obtain funds needed for medical expenses and other purposes, those benefits may come at a high price for investors, particularly senior citizens.

Entertainment Investments. These unregistered investments, encompassing a variety of products including movies, infomercials, internet gambling and pornography sites, promise high returns while offering little disclosure of risk.

Leveraged Exchange-Traded Funds (ETFs). This relatively new product has been offered to individual investors who may not be aware of the risks these funds carry. The funds, which trade throughout the day like a stock, use exotic financial instruments -- including options and other derivatives -- and promise the potential to provide greater than market returns as the value of the underlying assets rise or fall. Given their volatility, these funds typically are not suitable for most retail investors.

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About DFI's Division of Securities www.dfi.wa.gov/sd ? 360.902.8760 ? 877.RINGDFI

(746.4334)

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