

Investment Risks



Picture This:

In search of investments for working capital, an oil company sends consumers surveys of property that suggest the land is oil-rich. The company's sales force tells interested consumers that top oil experts project the fields will yield thousands of barrels of oil a day — and a tidy return to investors within a year.

A film production company tells potential investors it is raising capital to produce a high-quality, low-budget family film with actors who are willing to sacrifice their usual high salaries for the sake of art. Claiming that the independent film market, cable television and video stores have increased the demand for movies, investors are “guaranteed” to make their money back. According to the prospectus, investor money will be spent on production, distribution and the screenplay.

Brokers of gemstones, rare coins or precious metals tell investors that the market price of these hard assets is skyrocketing. According to the brokers, the assets will increase in value — not only because experts have graded them rare, but also because of the demand.

Brokers of an FCC-licensed partnership tell consumers they're raising capital to acquire a communications business that can be enhanced with new technology and turned into a competitive high-tech enterprise to be sold or developed for huge profits.

Investment brokers are claiming to sell ownership interests in a company that will offer Internet access to the public. The brokers maintain that investors will realize substantial gains from the fees the company will charge its users.

What's wrong with these pictures?

In a word — plenty.

- ✘ The oil surveys are fake. The land owned by the company has not been drilled for oil, and in a legitimate deal, much more capital is required to determine if oil could be produced from the land at all.
- ✘ The principals of the film-flam scam are the “producers” and “screenwriters.” They take most of the money raised and then use a small amount to produce a low-quality film that is unlikely to turn a profit, let alone be released commercially.

Facts for Consumers

- ✘ Gemstone, rare coin or precious metal scam promoters often charge very high mark-ups and, as a result, consumers who try to resell their assets almost always lose most of their money.
- ✘ The communication technology promised may be unavailable, unworkable or too costly. The partnership brokers take most of the money for themselves after they acquire low-tech businesses for consumers that would require millions of dollars more to have even a slim chance at turning a profit.
- ✘ The fraudulent promoters generally structure the deals to siphon off at least 85 percent of investor money, never intending to turn over a functioning business with Internet expertise, equipment or staff. Investors are left with little capital, expertise or business with which to compete on the Internet.

It's easy to make a new venture sound like a sure-fire money-maker, especially if the press is writing about successful legitimate companies in similar industries. Fraud promoters create the illusion of authenticity and success by incorporating, renting office space and issuing partnership units or stock certificates. But while they claim to offer investments in exciting sounding businesses or sell lucrative assets, they deliver cheap imitations of what they promise. As for consumers, they remain unaware that they've bought something of little or no value until their money is gone and profits have not materialized.

Pre-Investment Questions

Fraud is always a possibility, even with secured, regulated investments. Before investing, ask tough questions, both of yourself and those who are soliciting your investments. If the answer to any of these questions is "no" — or if the answers are vague or complicated — more than likely the investment being pitched is a fraud.

Is the company I'm investing in registered to sell securities?

Be cautious if the company selling you stock, assets, or partnership units has not registered its securities. Companies that register their securities file prospectuses and annual reports with securities regulators. If a promoter tells you that your investment is "structured" to exempt the securities of the company from registration, you may be dealing with an outfit that's purposely avoiding contact with regulators.

Is it "too late" if I don't invest my money now?

Using sales scripts, scam artists create the impression that only a few shares of stock or partnership units are left. They try to convince you that you'll miss out on a big opportunity if you don't send them thousands of dollars by overnight courier or wire transfer. Once you give your money to a scam artist, it may be too late to get it back.

Does the investment have a track record?

Claiming that their "opportunity" is similar to those of "hot" entrepreneurs, scam artists often use news stories about the success of legitimate companies as bait. Unfortunately, success stories of other companies in the field are irrelevant for your purposes. Get the track record of the company you're considering investing in and the background of the people promoting it.

Where is my money going?

Legitimate companies account for investors' money at all times. Ask for written proof of how much of your money is going to the actual purchase or development of the opportunity and how much is going to commissions, promoters' profits and marketing costs. If most of your financial investment is slated to cover expenses and costs, much less will be available to earn a return. Telemarketing is particularly expensive; if you are investing in a telemarketed investment,

how much are your brokers getting paid to talk to you?

Do I have an independent, knowledgeable, trustworthy person who can advise me?

Get an independent appraisal of the specific asset, business or venture you're considering. An appraisal offered by the party selling the investment opportunity can be fake. Talk to the previous owners of an asset or a business you're acquiring for its value history. Discuss all investment ideas or plans with an accountant or an advisor you know and trust.

Do I know who I'm dealing with?

Can you find published information about the company in which you're investing, proof that the company has registered the securities it is selling with a government agency (if required), or someone you trust who has heard of the company? Have you checked with your state securities agency to see if the promoter or sales person is licensed to sell securities in your state, if required? If not, be cautious. You're giving your money to strangers.

Checking law enforcement agencies and Better Business Bureaus in the community where promoters are located is prudent, but not fool-proof. It may be too soon for the company's victims to realize they've been defrauded or to have lodged complaints with the authorities. In addition, fraudulent promoters can lie about their name or their business history, or even pay people to be "references."

Can I tell a genuine company from a fictional one?

Don't let appearances fool you. For a few dollars, anyone can incorporate an entity. Personal computers and desktop publishing software help scam artists produce slick promotional materials. Phone service providers can put toll-free telephone numbers in homes.

Did my sales representative tell me the risk of losing my money was high?

Sales representatives should tell you the risk of particular investments. Be particularly suspicious of sales pitches that play down risk or portray written risk disclosures as routine formalities required by the government. Believe the risk disclosures that say you could lose your whole investment. When your money is gone, fraudulent investment promoters often use "risk disclosures" against you.

Can I be certain a promoter is not lying to me?

Scam artists lie. Their success depends on having an airtight answer for everything. They inflate the costs and value of worthless investments. They promise you profits years down the road so you won't find out that your investment is a scam until long after they've disappeared with your money.

Do I know when something is too good to be true?

Investing is risky business. Anyone who tells you an investment is likely to turn a profit quickly should have a basis for the claim. Demand written proof of profit projections from independent sources. Be especially wary when someone tells you profits will be big enough to offset the risk of investing. Every potentially high profit investment is high risk.

For More Information

Several government agencies and business organizations register, regulate, investigate or monitor companies and individuals who offer investment opportunities. If you have questions about a company or an individual, or you wish to make a complaint, contact one or more of these offices, as appropriate. When you seek information, understand that the absence of complaints filed with governmental and private agencies does not mean that a company or an investment is necessarily sound.

Facts for Consumers

- ✓ The FTC works for the consumer to prevent fraudulent, deceptive, and unfair business practices in the marketplace and to provide information to help consumers spot, stop, and avoid them. To file a complaint or to get free information on consumer issues, visit ftc.gov or call toll-free, 1-877-FTC-HELP (1-877-382-4357); TTY: 1-866-653-4261. The FTC enters Internet, telemarketing, identity theft, and other fraud-related complaints into Consumer Sentinel, a secure, online database available to hundreds of civil and criminal law enforcement agencies in the U.S. and abroad.
- ✓ Your State Attorney General's office and your local District Attorney's office investigate and prosecute fraud cases. You can find their telephone numbers by checking your local directory in the state and local government section.
- ✓ Your State Securities Commission, Securities Department, or Department of Corporations regulates the public offer and sale of securities by companies in your state. Call NASAA toll-free at 1-888-84-NASAA for the appropriate phone number or visit www.nasaa.org on the Internet.
- ✓ The Chief United States Postal Inspector, United States Postal Service, Washington, D.C. 20260-2112, handles complaints about bogus mail-order investment services. The USPS has jurisdiction over fraudulent business operations that use, advertise or sell through the mail. The Federal Bureau of Investigation also has jurisdiction when investment offerings constitute mail or wire fraud or other violations of criminal law.
- ✓ The Commodity Futures Trading Commission regulates most firms that deal in commodity futures markets. Futures trading markets include petroleum products, U.S. government securities, foreign currencies, options on futures contracts, and dealer options. Write the Commodity Futures Trading Commission at 2033 K Street, N.W., Washington, D.C. 20581 or visit www.cftc.gov on the Internet.
- ✓ The Securities and Exchange Commission is a federal agency that regulates the public offer and sales of securities. Contact the SEC toll-free at 1-800-SEC-0330 or visit www.sec.gov on the Internet.
- ✓ The Better Business Bureau mediates disputes between consumers and businesses and may be able to inform you about complaints lodged against local investment firms. Contact the BBB in the city in which the firm is located for information or to report a problem. For the phone number of an out-of-state BBB, write to the Council of Better Business Bureaus, 4200 Wilson Boulevard, Arlington, VA 22203.
- ✓ The National Association of Securities Dealers is a self-regulatory organization that governs stock brokers. Check your phone directory for a local district office of the NASD, or call toll-free 1-800-289-9999.
- ✓ The National Futures Association is a self-regulatory organization that governs all registered individuals and brokerage firms that sell commodities. Call the National Futures Association toll-free at 1-800-621-3570. In Illinois, call toll-free 1-800-572-9400.

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