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U.S. SECURITIES AND EXCHANGE COMMISSION

SENIORS SUMMIT

(Amended 8-14-06)

COPY

U.S. Securities and Exchange Commission
Station Place-Auditorium
100 F Street, NE
Washington, D.C. 20549

Monday, July 17, 2006
9:30 a.m.

Diversified Reporting Services, Inc.
(202) 467-9200

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2

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4 Commissioner Paul Atkins

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6 Commissioner Kathleen Casey

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P R O C E E D I N G S

OPENING REMARKS

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3 CHAIRMAN COX: Good morning, and welcome to the
4 Securities and Exchange Commission's first-ever senior
5 summit. Before we get started, I want to give a rousing
6 welcome to our new SEC commissioner, Kathleen Casey, who was
7 just sworn in this morning.

8 Kathy comes to the Securities and Exchange
9 Commission from the United States Senate Committee on
10 Banking, Housing, and Urban Affairs, and their loss is our
11 gain.

12 As a former member of Congress, I know full well
13 that though the Members get credit for writing legislation,
14 the staff are the real heroes. And as the commissioner and
15 staff director for the last 3-1/2 years, and as a member of
16 the committee staff for 13 years, Kathy was responsible for
17 many important pieces of legislation that have had a deep
18 impact on our nation's economic health.

19 And that's why the Senate last week passed a
20 resolution expressing its deepest gratitude and most sincere
21 respect for Kathy and for her service to our country. And I
22 couldn't agree more. So, Kathy, welcome to the Commission.
23 Your qualities will serve us well.

24 Your first public event is an important one. I
25 want to give a special greeting to the representatives and

1 leaders of the North American Securities Administrators
2 Association, to the NASD, NYSE regulation, AARP, and the
3 California Department of Corporations, who all are here with
4 us today.

5 We often work together, but it's very rare that you
6 find us all under the same roof. And we have a very good
7 reason for doing that today. We are called here together for
8 an important purpose, to protect our nation's senior
9 citizens: we want to protect them from scammers who would
10 take their money that took them a lifetime to save. We are
11 committed to being cooperative in our approach, creative in
12 our thinking, and productive, when it comes to results.

13 Protecting seniors from investment scams is one of
14 the most important issues of our time. The numbers give us
15 an idea of why that's so, and of the magnitude of this issue.
16 This year, the Baby Boomers are starting to turn 60.

17 In fact, President Bush led the way last week, and
18 he is just one among the largest cohort of our national
19 demographic profile. The birthdays this year, all these men
20 and women turning 60, are just the beginning of a veritable
21 demographic flood tide. For the next two decades, 75 million
22 people will turn 60. That's 10,000 people every 24 hours.

23 Think of it this way. Imagine a medium-sized town
24 of 10,000 people, and one day everybody in that town turns
25 60. And the next day another town, and the next day another

1 town, and so on, every day, for 20 years. That is what the
2 graying of the Baby Boom generation is leading to.

3 The next 20 years will witness a retirement boom.
4 As this process proceeds inexorably, all evidence points to
5 the Baby Boomers taking the bulk of America's wealth with
6 them into old age. Households led by people over 40 already
7 represent over 91 percent of America's net worth. The Baby
8 Boomers will, in all likelihood, heed Dylan Thomas's famous
9 words, and will not go gentle into that good night.

10 Instead, because they will live longer and in the
11 main, they will be healthier than their parents, they will
12 work longer and remain active and aggressive investors even
13 longer still. Chances are that they will remain invested in
14 equities, and not switch to fixed income to the degree that
15 people over 60 have done in the past.

16 One reason for this is that many Americans are a
17 lot less prepared for the financial contingencies of old age
18 than they realize. For example, while we're living longer,
19 most people's retirement plans haven't taken that into
20 account. When my dad was born, life expectancy was 49 years.
21 Today it's pushing 80. And in a remarkable statistic, fully
22 half of all the babies born this year will live past 100.

23 All these trends, a huge number of people suddenly
24 turning older, the prospects of longer lives but fewer
25 guarantees of financial security, and at the same time, a

1 substantial percentage of national wealth in the hands of
2 seniors, have the makings of a perfect storm. Fraudsters
3 will go after seniors because -- following the Willie Sutton
4 principle, "that's where the money is." And seniors won't be
5 the conservative investors that they used to be. So they
6 will be more vulnerable than ever.

7 The result could be an avalanche of investment
8 fraud cases that could not only injure millions of seniors,
9 but also impact the broader market, as a whole.

10 Seniors aren't vulnerable just because of the onset
11 of years, by the way. Just as importantly, they are
12 vulnerable because once they lose their life savings, they
13 will have no second chance to earn it back. And when that
14 happens, tragedy strikes. The numbers alone don't tell the
15 whole story. Fraud of this kind would erode the very trust
16 on which investing depends, and undermine investor confidence
17 in the market, as a whole. On a personal level, this kind of
18 fraud robs people of their dreams, and destroys lives.

19 The SEC staff receives tens of thousands of calls a
20 year from people who have been scammed, or who have been sold
21 investments that they don't understand. These are bitter
22 personal tragedies. Let me take the time to recognize the
23 work of our office of investor education and assistance, for
24 their professionalism and compassion in dealing with these
25 cases.

1 As institutions and regulators charged with looking
2 after the interests of investors, businesses, and the
3 elderly, it's up to us to fight to prevent these personal and
4 systemic catastrophes. We are committed to vigorous
5 enforcement to protect our seniors. Many of our
6 organizations are already working together on a series of on-
7 site compliance examinations of firms that sponsor free lunch
8 seminars that are often targeted at seniors.

9 Our concern is that these events are being used by
10 unscrupulous individuals to sell investment products
11 unsuitable to seniors. We found out after our initial effort
12 that, unfortunately, we were right to launch these
13 examinations. So we have expanded the program. And just
14 last week, the Commission's New York office filed an
15 emergency enforcement action to halt a fraudulent real estate
16 investment scheme that bilked senior citizen retirees out of
17 millions of dollars since 1996.

18 Later today, our Denver office will file suit
19 against several California con artists who raised \$16 million
20 in a Ponzi Scheme that promised investors returns of up to 75
21 percent. Many of the victims were sick and elderly
22 investors, several of whom lost their entire life savings.

23 Today's summit is an important step in this process
24 of collaboration among government and law enforcement
25 agencies at all levels. One important contribution, which

1 will be the subject of much attention today, is the NASD's
2 investor education foundation's fraud study. All of the
3 study's findings caught my attention.

4 Some were intuitive, such as, for example, the
5 discovery that con artists and criminals vary their pitches
6 in order to fit their intended victims' profiles. The
7 finding that fraud victims tend to be more optimistic also
8 makes sense. Other findings may appear more counter-
9 intuitive to people not familiar with investment fraud, such
10 as the finding that fraud victims tend, on average, to be
11 more informed about investing than non-fraud victims. This
12 may go back to the old saying that a little knowledge is a
13 dangerous thing.

14 These findings should have an impact on how all of
15 us go about doing our jobs. As the study says, while
16 financial literacy programs are necessary, they are probably
17 not sufficient, in themselves, to prevent fraud.

18 To devise the proper response, we have an
19 impressive array of talent here today. From the Commission,
20 we're fortunate to have the participation of all of our
21 commissioners, including our newest addition. We also have
22 Linda Thomsen, director of the SEC's division of enforcement,
23 and Lori Richards, director of the office of compliance,
24 inspections, and examinations.

25 And we have eminent speakers from outside the

1 Commission. From the North American Securities
2 Administrators Association, we have its eminent national
3 president, Patty Struck. Patty, who is also the chief
4 securities regulator in Wisconsin, has been president of
5 NASAA, officially, since September. She has had top
6 positions in the organization since 1998.

7 NASAA, incidentally, is the oldest international
8 organization looking after investor interests. It brings
9 together regulators not only from the 50 states, but also
10 Canada and Mexico. Patty has used this powerful tribune to
11 speak about investor protection and education for several
12 years now.

13 From the NASD we have vice-chairman Mary Schapiro.
14 Mary joined the NASD in 1996 and, before that, she was
15 chairman of the CFTC. She was also an SEC commissioner and
16 acting chairman here at the Agency.

17 Chris Hansen is AARP's group executive officer for
18 state and national initiatives. His responsibilities include
19 government relations, advocacy, management of AARP offices in
20 every state, public outreach on key programs, and volunteer
21 management and support. Prior to that, Chris had a long
22 career with Boeing.

23 Rick Ketchum is chief executive officer of NYSE
24 Regulation Incorporated. He is a member of the NYSE
25 Regulation board of directors. Rick has served as the chief

1 regulatory officer of the New York Stock Exchange since March
2 8, 2004. He also is an SEC alum, having been director of the
3 division of market regulation for eight years.

4 We are also fortunate to have with us Professor
5 Anthony Pratkanis, who teaches psychology at UC Santa Cruz.
6 Professor Pratkanis has made research into persuasion,
7 influence, and fraud his life's work. Professor Pratkanis
8 has testified to the United States Senate's Special Committee
9 on Aging about what can be done to protect our seniors
10 against fraud. He currently works with the AARP and
11 government agencies on strategies to prevent fraud.

12 Also here is Doug Shadel, Washington State's AARP
13 director. Doug's experience as a former fraud investigator
14 and special assistant attorney general in Washington is
15 especially relevant to our deliberations here today. He is a
16 leading national expert on fraud on seniors, and has co-
17 authored three books on fraud.

18 Anthony Lewis has been deputy commissioner for the
19 securities regulation division and acting chief deputy
20 commissioner for the California Department of Corporations
21 since June 2005. In this position, he assists in the day-to-
22 day operations of the department. He has previous experience
23 fighting elderly fraud, having served as a supervising deputy
24 attorney general for the State of California Bureau of Medi-
25 Cal Fraud & Elder Abuse.

1 And rounding up the talent pool we have Preston
2 DuFauchard, who was just appointed by Governor Schwarzenegger
3 as commissioner of the California Department of Corporations.
4 It's very nice of Commissioner DuFauchard to make it here
5 from Sacramento.

6 Our format today will comprise four presentations,
7 running until 11:15. And from then, until 12:00 noon, we
8 will throw the floor open to a panel discussion among all of
9 the participants.

10 Our first discussion group will be comprised of
11 Patty, Chris, and Mary, and give us a broad view of the
12 current landscape.

13 Our second group will look at the senior investment
14 fraud study, and will be made up of Professor Pratkanis and
15 Doug Shadel.

16 Our third presentation on seniors against
17 investment fraud will be given by Tony Lewis. And our last
18 presentation, by Linda and Lori, will be an enforcement and
19 examination update.

20 So, now we will begin with that first discussion,
21 which I hope will be free ranging. And I will serve as the
22 moderator. Let's begin with Patty, Chris, and Mary.

23 OVERVIEW

24 MS. STRUCK: Thank you, Chairman Cox. I am honored
25 to participate in the first-ever senior summit, to highlight

1 the activities of state securities regulators in protecting
2 senior citizens from investment fraud.

3 From the Greatest Generation to the Baby Boomers,
4 seniors have worked hard to build both our nation's economic
5 prosperity, and a lifetime's worth of savings. As
6 regulators, we must do all we can to ensure that their golden
7 years are not tarnished by investment fraud.

8 Individuals aged 60 and older make up 15 percent of
9 the U.S. population, but account for 30 percent of fraud
10 victims. Con artists have migrated from the side streets and
11 back alleys to Main Street, where older investors live. They
12 know that today's retirees are facing greater responsibility
13 for their own financial security, and they need to maximize
14 their retirement investments.

15 That's one reason seniors today are flooded with
16 pitches for investment seminars, many of them promising a
17 free lunch, along with higher returns and little or no risk.
18 Unfortunately, in many of the cases that securities
19 regulators see, it's just the opposite: high risk; no
20 returns; just disastrous losses.

21 The bait for many of these seminars is that income
22 will be guaranteed, and substantially higher than the return
23 someone on a fixed income can expect to get from CDs, money
24 market investments, or other traditional financial products.
25 The current landscape facing senior investors is littered

1 with slick schemes and broken dreams.

2 While our cases of senior investment fraud may not
3 make national headlines, they are devastating in their impact
4 on victims and their families.

5 In my own state of Wisconsin, an elder in a Kenosha
6 church operated a long-running Ponzi Scheme that victimized
7 117 friends, relatives, and mostly senior parishioners of
8 more than \$6 million.

9 In Florida, state officials recently dismantled
10 Orlando-based Tropical Village, Inc., that they say defrauded
11 elderly investors of more than \$9 million through the sale of
12 unregistered securities.

13 With the first of the Baby Boomers turning 60 this
14 year, state securities regulators are deeply concerned that
15 investment fraud among seniors, already nearly half of all
16 investor complaints, could grow significantly.

17 Preliminary results of a new NASAA survey measuring
18 senior investment fraud show that 45 percent of all investor
19 complaints received by state securities regulators come from
20 seniors. The survey also found that one-third of enforcement
21 actions taken by state securities regulators involve senior
22 investment fraud.

23 Of course, the threats facing senior investors are
24 more pronounced in those states with large retirement
25 populations. In Florida, around 75 percent of all investor

1 complaints are made by seniors.

2 The NASAA survey also found that unregistered
3 securities, variable annuities, and equity-indexed annuities
4 are the most pervasive financial products involved in senior
5 investment fraud. In California, 75 percent of the state's
6 senior investment fraud cases involve unregistered
7 securities. Cases involving variable or equity-indexed
8 annuities were 65 percent of the caseload in Massachusetts,
9 60 percent in Hawaii and Mississippi.

10 Con-artists use the promise of high commissions to
11 lure brokers, insurance agents, investment advisors and
12 accountants, some of them not licensed, to sell securities,
13 and to offering investments that they know little about, such
14 as variable or equity-indexed annuities, bogus limited
15 partnerships, or promissory notes.

16 Some of these individuals hold nothing more than a
17 designation as "senior specialists," implying that they have
18 expertise in assisting seniors in structuring their
19 investments so as to reduce taxes, minimize risks, and avoid
20 state probate laws. State regulators are concerned that
21 these individuals are mis-using senior specialist
22 designations to provide a false sense of security to their
23 customers.

24 While there are organizations whose members
25 complete rigorous programs of study and pass extensive exams

1 to earn "senior specialist" designations, there are others
2 that require little or no training to use these designations.

3 So, what should senior investors do? Make sure
4 they deal only with individuals licensed by their securities
5 regulators at the state level. We license brokers and
6 investment advisors after they pass rigorous competency
7 exams.

8 While my colleagues and I currently see a
9 proliferation of troubling schemes involving unlicensed
10 individuals promoting and selling unregistered securities to
11 seniors, we continue to be concerned about the way variable
12 and equity-indexed annuities are marketed and sold.

13 Let me be clear. Our concerns with variable and
14 equity-indexed annuities are not about the products. These
15 annuities are legitimate and suitable for some investors.
16 But they are unsuitable for many retirees. Yet, they are
17 being pitched aggressively to seniors through investment
18 seminars.

19 We are concerned that investors aren't always told
20 about high-surrender charges for early withdrawals, the
21 potential of exposure to market risk, and the steep sales
22 commissions motivating agents to move investors into these
23 products.

24 NASAA survey results show that senior investment
25 fraud is a serious ongoing problem. State securities

1 regulators believe the most effective weapon against senior
2 investment fraud is targeted aggressive enforcement, combined
3 with financial education. For that reason, we are pleased to
4 be working with our regulatory partners represented here
5 today to help protect our nation's seniors.

6 The senior initiative that was discussed earlier by
7 Chairman Cox reflects the long-standing collaborative
8 relationship between state and federal securities regulators,
9 and it will lead to significant protections for seniors.

10 Today's senior investors are our parents, teachers,
11 our church leaders, our coaches, the same people we looked up
12 to in our childhoods. They deserve the same respect today.
13 We will not tolerate their victimization by those who would
14 profit from their lifetime savings. Thank you.

15 CHAIRMAN COX: Thank you, Patty. Chris?

16 MR. HANSEN: Thank you. I appreciate the
17 opportunity to participate in the senior summit today. And
18 we deeply appreciate the added emphasis that Chairman Cox and
19 of the Commission, members of NASAA, and the SROs are placing
20 on older Americans. And we particularly appreciate your
21 actions to help protect older Americans from investment
22 fraud.

23 Let me say a word about AARP, as an organization,
24 at the top here. We are a non-partisan, non-profit
25 membership organization that tries to help people 50 and over

1 age with dignity and purpose. Today, we have over 36.6
2 million members, and we are growing fast.

3 We publish: "AARP," the magazine, and that's
4 published bi-monthly; the AARP bulletin, which is a monthly
5 newspaper. We have the highest circulation in those
6 periodicals of any publications that there are. We have
7 staffed offices in all 50 states and 3 territories.

8 On this subject, as older Americans continue to
9 take on more individual responsibility for their retirement,
10 protecting them from investment fraud takes on increasing
11 importance for all of us. The 2004 survey of consumer
12 finances, which is the most recent data available from the
13 Federal Reserve, reveals why we are concerned with protecting
14 older investors from fraud.

15 In that study, the total aggregate value of
16 consumer financial assets exceeds \$21 trillion. The
17 demographics in that study suggest that: 25 percent of the
18 households are headed by someone under 50 years old; 43
19 percent are headed by someone between the age of 50 and 64;
20 and 32 percent are headed by people that are 65 and older.
21 In other words, 75 percent of the nation's consumer financial
22 assets, ordinarily \$16 trillion, are held by households
23 headed by someone who is 50 and older. That's huge.

24 AARP is actively involved in a variety of
25 educational and outreach efforts. One highlight is the

1 Campaign for Wise and Save Investing, which is a
2 collaborative outreach effort between the AARP Foundation and
3 the Investor Protection Trust. That activity is being funded
4 through grants by 33 state security commissions. And in that
5 activity, we are currently training AARP volunteers to
6 deliver educational seminars on how to fight fraud in states
7 all across the country. We are going to also use our
8 publications, our websites, our media outreach, to assist
9 these efforts.

10 Now, because scammers are doing their homework, we
11 want investors to do some homework also, and we're going to
12 be trying to help them with that. We're going to be
13 suggesting that they check the product. Fortunately, most
14 investment products need to be registered with the state
15 securities regulators or the SEC. When they're approached by
16 somebody selling these products, we want them to check the
17 person that's doing it, because the people selling most
18 investments must be licensed by state regulators or with the
19 NASD.

20 We also want them to check the tactics. And to the
21 point of tactics, our state director, Doug Shadel, and Dr.
22 Pratkanis are going to be discussing all of the tactics that
23 they uncovered in their investor fraud study. And I think
24 they are very telling.

25 I would like to also briefly mention a couple of

1 other policy initiatives that we think are going to be
2 helpful. The regulation in plain language initiative -- and
3 we are very appreciative that Chairman Cox and members of the
4 Commission are supportive of that concept -- we think it's a
5 wonderful thing to do.

6 We also think that it's going to not only make
7 regulations more accessible and understandable for the public
8 as a whole, but we think it will also compliment our efforts
9 to improve financial literacy.

10 AARP also would like to commit itself to work with
11 the Commission on the development of the interactive data
12 initiative. We think that this flexible business financial
13 reporting system can provide reliable and meaningful context
14 for the average investor. I want to thank you for inviting
15 us to this summit, and I look forward to the rest of the
16 discussion.

17 CHAIRMAN COX: Thank you. Mary?

18 MS. SCHAPIRO: Thank you very much, Chairman Cox,
19 and thank you for the invitation to be here. I think, more
20 importantly, thank you for bringing us all together for this
21 summit. I hope and believe it will be a defining moment in
22 the protection of senior investors.

23 NASD has long been committed to protecting
24 investors of all ages through a wide variety of programs.
25 When it comes to combating fraud targeted at seniors, we take

1 an approach we are sure our parents and grandparents would
2 applaud: we go back to basics, and focus on the three R's,
3 regulation, reaching out, and research.

4 The first R, regulation, encompasses rule making,
5 enforcement, and examination activities. As you have heard,
6 we are in the midst of a multi-regulator sweep that focuses
7 not only on the advertising that lures investors to free
8 seminars, but also on the promotional materials for the
9 products and services being pitched.

10 A primary focus for the examination teams, as they
11 review the firm's supervision, control, advertising, and
12 sales material for senior seminars is whether there are
13 product misrepresentations or unsuitable investments being
14 sold to the attendees.

15 We also understand that awareness, prevention, and
16 education are major deterrents to investment fraud. That's
17 why reaching out, the second R, is so important. NASD
18 educates seniors and other investors about how to invest
19 wisely and avoid investment fraud through our own investor
20 education programs, and through the NASD Education
21 Foundation.

22 In 2003, we conducted a survey that found an
23 overwhelming 97 percent of investors realized they needed to
24 be better informed about investing. We responded with an
25 expanded array of resources, including a series of investor

1 forums and workshops across the country, many held at senior
2 centers.

3 The NASD website and companion website for military
4 investors, saveandinvest.org, provide a wealth of information
5 for all investors, and specifically, for seniors. Investor
6 alerts warn of the latest scams or risky products. Several
7 focus on products we often see targeted for sale to seniors,
8 such as equity-indexed annuities, variable annuities, and
9 stretch IRAs.

10 The site also offers a number of interactive
11 centers and tools of particular interest to older investors
12 who are at or near retirement age. The 401(k) learning
13 center contains valuable information about withdrawals from
14 that essential retirement funding vehicle.

15 Many seniors will find the bond learning center
16 very helpful, since they typically invest a greater
17 percentage of their assets in fixed income securities. NASD
18 also provides investors via the Internet or toll free
19 telephone call with a service called Broker Check, which
20 allows investors to quickly access information about the
21 disciplinary history, professional background, and conduct of
22 the brokerage firms and individual brokers with whom they
23 seek to invest.

24 An increasingly important resource at NASD.com is
25 the professional designation database. It's the only tool

1 available that helps investors to decode professional
2 designations and better understand what education and
3 experience requirements, if any, are necessary for any given
4 designation, including those that suggest special expertise
5 in the needs of senior citizens.

6 Investors also benefit from the grant-making of the
7 NASD Investor Education Foundation. In its first two years
8 of grant-making, the foundation has funded two grants that
9 focus especially on older Americans.

10 One of those grants funded the development of an
11 interactive game-based educational program to provide
12 education on retirement planning, primarily for 45 to 60-
13 year-old women. The new game is called "Get Rich Slow," and
14 it's available free on the website of the Center for
15 Retirement Research of Boston College.

16 And that leads me to our third R, research. Before
17 we can devise workable solutions to senior investment fraud,
18 we must, as with any complex problem, first determine how and
19 why and through what mechanisms the problem occurs.

20 What motivates seniors to succumb to the persuasion
21 tactics of complete stranger? Who do seniors trust? And
22 where do those seniors who are most vulnerable to aggressive
23 sales pitches get their information? How can we best reach
24 them? How can we best equip them to avoid fraud?

25 The Foundation's second grant to WISE Senior

1 Services funded research to begin to answer these questions.
2 You will hear more about the fruits of this research in just
3 a few moments. Chairman Cox has already piqued your
4 interest, I believe, by saying that the WISE study provides
5 fascinating new evidence that victims of senior investment
6 fraud are not whom we so often assume them to be.

7 The research WISE conducted is a critical step in
8 helping all of us -- regulators, educators, and senior
9 advocates alike -- to understand senior investment fraud, and
10 develop practical messages to increase awareness among
11 seniors. I think that one of the many next steps should be
12 to complete our own understanding of senior investment fraud.

13 To that end, last month the NASD Foundation Board
14 authorized a comprehensive investor survey of senior
15 citizens. The survey will identify basic market knowledge
16 and financial literacy levels for seniors. It will also shed
17 light on: their savings and investment habits; which
18 investment products and services they purchase, and why; what
19 marketing messages resonate with them; which information
20 sources they use and trust; and where they turn for help.

21 As you will see in a moment, the WISE study
22 shatters the stereotypes of senior fraud victims, and forces
23 us to rethink how we approach the challenge of combating
24 senior fraud.

25 We at NASD look forward to working with the SEC,

1 state securities regulators, senior advocates, educators, and
2 other partners, on this important initiative.

3 CHAIRMAN COX: Thank you very much, Mary, Patty,
4 and Chris, for an outstanding overview. And we will now
5 move, as Mary suggested, into discussion of our senior
6 investor fraud study, with Professor Pratkanis and Doug
7 Shadel.

8 SENIOR INVESTOR FRAUD STUDY

9 MR. SHADEL: Thank you very much. Well, it's a
10 pleasure to be here, and really an honor to be here with all
11 these distinguished speakers.

12 And by way of introducing this study -- Anthony and
13 I are going to just go kind of back and forth -- but as you
14 see on the slide here, just by way of introduction, we wanted
15 to thank the NASD Investor Education Foundation for funding
16 this study. I don't think I've ever worked on a study where
17 we had more complete intellectual freedom to just find what
18 was there. And I just want to say, Mary and John Gannon,
19 thank you very much for that. Also, I want to thank WISE
20 Senior Services for allowing this group of researchers to do
21 this work.

22 You will see here this study was completed by the
23 Consumer Fraud Research Group, which is a multi-disciplinary
24 group of researchers, Dr. Pratkanis and myself, Melody
25 Klineman, who is in the audience, and Carla Pack, as well as

1 Bridget Small, were also on the research team.

2 We're just going to -- let me just give you an
3 overview of what we're going to talk about. First,
4 understanding investment fraud crimes.

5 We want to start with a story of a victim who lost
6 over \$500,000 to an oil and gas scam. Very briefly, I want
7 to just describe this, an AARP member, even. Then we're
8 going to talk about the -- outline the findings from this
9 two-year-long NASD investor fraud study that's being released
10 today. And then, briefly discuss the implications --
11 although I think we will have time at the end to do more of
12 that.

13 Let's just talk about one victim's story. Part of
14 the reason we're putting this in here is I can tell you,
15 having worked on this for two years, we were awash in data.
16 A lot of the findings, as Chairman Cox said, were sort of
17 counter-intuitive. And there was a point where I sort of
18 said, "Is this really true?" We were so immersed in the
19 data. And just when we were thinking that about two weeks
20 ago, an AARP member called the office to tell his story.

21 Henry, who does not want to be identified, was a
22 successful businessman, married for 30 years, raised a
23 family, and had a good life -- he was a sweet man, too. We
24 went down and interviewed him pretty much all day in his
25 home. And sharp as a tack. He could remember every detail

1 of these investments that he was talking about.

2 Well, shortly after his wife's death, he received a
3 Federal Express package containing a very professional
4 package of materials with all kinds of reports, and it was
5 offering an oil and gas investment, geology reports, no
6 detail was missing from this. And it was unsolicited. He
7 just got this in the mail. And he ignored it, because he
8 doesn't -- didn't remember ordering it.

9 But the next day, sure enough, a salesman called
10 him and used high-pressure sales tactics -- something we will
11 be referring to as social influence tactics -- to persuade
12 him to invest \$40,000.

13 And here is some examples of what was said to him
14 on the phone: "These gas wells are guaranteed to produce
15 \$6,800 a month in income;" "Some of the most successful
16 investors in the country are interested in these wells;"
17 "There are only two units left in this project;" "We drilled
18 a well in Texas that had these same early gas readings, and
19 the investors all made millions."

20 These are what you will come to, hopefully be
21 familiar with, as social influence tactics. And Dr.
22 Pratkanis is going to talk more about that in a minute.

23 So, once Henry invested the initial \$40,000,
24 because he finally succumbed to this high level of
25 persuasion, his journey into the world of fraud was just

1 beginning. Every day that went by after that first
2 investment he would get phone calls and he would get faxes
3 updating him on his investment.

4 But within six weeks of making the first investment
5 he was contacted again by the same company. And the caller
6 told him the well was being dug, but in order to access "vast
7 gas fields," he would need to invest another \$50,000. When
8 he asked, "What happens if I don't invest another \$50,000,"
9 they said, "Well, that's fine, but you will lose everything
10 you have invested up until this point."

11 Over a three-year period, Henry was recontacted 12
12 times and invested, essentially, his life savings in 4
13 different gas wells, each time thinking that he had to invest
14 or lose the original investment.

15 He ultimately lost over \$500,000 to this oil and
16 gas scam investing in wells that always seemed promising at
17 first, but then ran into trouble and were capped. And so
18 we -- this was an affirming story -- it's a terrible story,
19 but it's affirming to the extent that Henry really meets this
20 emerging new profile that the data shows is the modern
21 investment scam victim.

22 And it was stories like this, over time, that
23 generated our interest in who are these people, and how can
24 someone who is so successful, so smart, lose their entire
25 life savings to something like that?

1 PROFESSOR PRATKANIS: Okay, and I will talk a
2 little bit about the research, give you an overview about it.

3 One thing you can do is look at it as two separate
4 studies. The first was an uncover tape analysis. And the
5 purpose of this was to find out the environment, the
6 situation that the victim finds themselves in, and to look at
7 the social influence that's going on in that situation.

8 What we did is we had tapes provided to AARP by
9 various law enforcement agencies. These tapes were used to
10 investigate the crime, they were used primarily for law
11 enforcement purposes. Sometimes it was an actual victim,
12 sometimes it was a law enforcement agent playing along as a
13 victim.

14 They were -- we had 128 full-length tapes, and they
15 varied across scams, gold coins, investment scams, lottery,
16 travel, and so forth. And we analyzed these to find out what
17 was going on, what social influence tactics were being used,
18 to see what the environment is for that victim.

19 The second part of our study was a survey of
20 victims and non-victims. And this is to look at the victim
21 themselves, who are they, what are they about. And putting
22 those two pieces together, we could get a good snapshot of
23 the crime.

24 That part of the survey had two parts. First of
25 all, we ran a focus group to help figure out and prepare our

1 questioning. But the major part was an extensive survey of
2 150 non-victims, a randomly sampled group from the
3 population, and a group of victims, all over 45 years of age.

4 We had two groups of victims, one who had lost
5 money in investment fraud, and another group who that lost
6 money in a lottery fraud. And what we wanted to do is to see
7 who they were, how they differed, and so forth.

8 We knew that each of these people had lost at least
9 \$1,000 to fraud. We got on the sheets -- we had lead sheets
10 often times that the criminals had prepared. We could often
11 times tell you exactly what Visa card they used, or how they
12 delivered the money.

13 Let's look at each of these two parts of the
14 studies in detail, and I want to start with the tape study
15 and the major finding that comes out of that. And that is
16 investment fraud is committed using sophisticated social
17 influence tactics.

18 In a robbery, the weapon is a knife or a gun. In a
19 fraud crime, the weapon is social influence. And that has an
20 enormous amount of implications. People do not recognize
21 social influence in their lives. So when they see such a
22 crime, see such a victim, they think that person is crazy,
23 gullible, naive, or whatever. And they don't see the actual
24 influence taking place. And it makes it very difficult for
25 people to resist.

1 What we're going to do is give you a flavor for
2 that kind of influence now by playing a tape, Chairman Cox,
3 of some actual victim pitches, and so forth.

4 (Audio tape begins.)

5 VOICE: Anyway, I said I would not call unless it
6 was a rare and definitely undervalued situation. Are you
7 familiar with the \$2.50 gold Indian series?

8 VOICE: The coin is worth \$4,640. That's what it's
9 worth, and that's why I even sent you out the free book,
10 because I wanted to show you that. And we got it at the
11 estate sale, and we got it way below value. I sent it out to
12 you for only \$3,100. I didn't even take a broker's fee on
13 that.

14 VOICE: Don't worry about all that. I will give
15 you that information later, because it's obviously getting
16 too confusing now.

17 VOICE: You're going to shut your mouth, and you're
18 going to listen to me. I'm fed up with you talking over me.

19 VOICE: Now, John, back in 1860, from the
20 Philadelphia Mint, there were 22,675 of these coins minted.
21 Of those 22,000, only 4 have survived -- only 4, for God's
22 sake, just 4 remain -- at this grade.

23 VOICE: Here is the bottom line. Take and write
24 down what I'm going to tell you, and do this exactly as I
25 tell you, and don't switch up on me again, okay? Answer me.

1 Okay?

2 VOICE: If you don't want to make up your mind
3 right now, that's where I come in. I will make up your mind
4 for you.

5 (Audio tape ends.)

6 PROFESSOR PRATKANIS: This will give you a little
7 montage of various and taken from investment fraud tapes.
8 Let's look at some of the findings of those tapes in a little
9 more detail, and understand the social influence going on.

10 We found in those tapes that investment fraud
11 criminals used a wide array of influence tactics. These are
12 tactics that I and my colleagues in social psychology have
13 studied, brought into the lab, and understand how they work
14 and what their nature is. And we find that criminals use
15 these naturally. They're not reading our academic articles,
16 they're picking up on this all on their own.

17 What were some of the ones that were very typical
18 that were used? One is what we call phantom fixation. A
19 phantom is something that is designed to look real, but
20 doesn't actually exist. And the criminal wants to dangle
21 that out in front of the victim, and to make that phantom
22 look as real as possible. "These wells are guaranteed to
23 produce \$6,800 a month in income." "You're going to be
24 getting more return than Warren Buffet does, on average."
25 Dangling it out for them. They will tell stories, they will

1 trump it up, and they will use other influence tactics to
2 make that phantom look real.

3 The next thing that often times goes on is a
4 commitment trap. And that was very clear in Henry's
5 situation. The commitment trap is once you make a commitment
6 to something, people have a tendency to honor it. They don't
7 want to go back on their commitments. And in this particular
8 case, there was a cost to going back on that commitment.

9 So, if Henry had given up at any point along the
10 crime, he would have lost everything that he had invested
11 before them. The situation becomes not, "Do I give another
12 \$10,000," but, "How do I prevent from losing the previous
13 \$100,000?"

14 Another one that you see -- and this was very clear
15 in the audio tape that we listened to -- is the use of
16 authority. In social psychology, we find you dress somebody
17 up in a uniform and just ask them to give money to a parking
18 meter, they will, relative to a control. And the con
19 criminal has found that out, too. They put on all sorts of
20 roles, place all sorts of people, to create a sense that they
21 are an authority. And that creates the sense of trust that
22 they need, as a platform for this crime.

23 In Henry's case, he was told, "I have been in the
24 oil business for over 30 years," said the con criminal. We
25 have seen criminals play roles everywhere from lawyers trying

1 to get their money back, to CEOs, VPs of marketing, police,
2 Royal Canadian Mounties, and in one type that we analyzed,
3 the criminal was actually pretending to be the attorney
4 general of the State of Ohio as they were calling into a
5 surveillance tape managed by the State of Ohio's attorney
6 general.

7 That's an authority -- and when you see that, you
8 don't think, "Gee, well, you know, is this guy really calling
9 from Canada?" We have a tendency to click -- we follow that
10 authority.

11 Another tactic that they use is social consensus.
12 If everyone agrees, it must be good, it must be correct.
13 That's how the tactic works. And often times they will have
14 this play out like they're an investor, too. In this case,
15 Henry was told by -- that a lot of other people were
16 investing. Some people were balking, just like he did, but
17 they realized that, in the end, it's going to be worth every
18 dime. And within that group, that social consensus, the deal
19 looks much better.

20 Another tactic that got used very much in
21 investment fraud is scarcity. If you make it look scarce,
22 two things happen. In our mind, we say, "Oh, it's scarce.
23 It must be valuable. Gold is scarce, that's valuable." And
24 our gut says, "I've got to act now. If I don't do that, I
25 will be out of this special deal." And you can see that in

1 the tapes, and you can see it here. "There are only two
2 units left in this deal."

3 There are lots of other tactics. Maybe we will
4 skip through this a little quick to save some time.

5 But just to give you a feel, they play friends with
6 the victim. Many times, at the end of the crime, they don't
7 want to prosecute, because this became their friend. They
8 landscaped the situation so that the con criminal is
9 controlling all the choices. They make the deal look better,
10 compare it to others. They do favors for the individual,
11 creating a sense of reciprocity. So the criminal has done
12 something for the victim, now it's the turn of the victim to
13 do something for the criminal.

14 They play other roles besides authority, such as
15 one actually acts like a little kid, creates the
16 child/adult -- puts that person in the role of adult, who has
17 to then protect the child, the criminal. They use search
18 credibility, and in the tape we saw, fear and intimidation,
19 which is often times used at the end, to close the scam.

20 The swindler bombards victims with complex
21 combination techniques. Since this is -- I'm a scientist, we
22 ought to have a little numbers here. In investment fraud,
23 this is particularly the case. They have a -- it's a
24 particularly complex scam to carry out.

25 They use -- in our tapes, which are -- our

1 transcripts, they average about six to eight pages, about
2 five to six pages of actual influence, the rest being
3 introductions and so forth. They would use over five tactics
4 of tape, of influence. And over an average -- total, per
5 transcript, it was about 14.

6 MR. SHADEL: So, another finding, as Chairman Cox
7 alluded to, one of the hypotheses in this study was just
8 intuitive, as Chairman Cox said, that victims might know less
9 about finances than non-victims, and that's why they're
10 victims.

11 The study essentially found precisely the opposite.
12 Investment victims are more financially literate than non-
13 victims. This was pretty astounding as a finding, and I will
14 just briefly tell you how we got to it.

15 We asked a standard battery of questions. There
16 were eight financial literacy questions about APR, about
17 what's the highest return over 40 years, compound interest,
18 you know, mutual funds pay a guaranteed rate of return --
19 true or false -- and so forth.

20 And here is the finding. Essentially, the non-
21 victims got 41 percent correct; the victims got 58 percent.
22 So there was really an astounding 17 percent difference.

23 Now, one of the things we postulated about this was
24 that maybe the non-victim general population that we selected
25 weren't actually active -- likely active -- investors, and

1 that may account for the difference. So we went into that
2 population and got a sub-measure by sorting out people who
3 answered questions that predict likely active investor
4 status. And that's where you get likely active investor non-
5 victim on this screen.

6 But even so, there was still a statistically
7 significant difference between those -- that population and
8 the investor victims. And I'm hoping we can have some
9 discussion about this afterwards.

10 Another question or finding was that victims were
11 more likely to have experience than negative life event. And
12 so I'm not going to go through all of these, but this is a
13 list -- and you have the hand-out -- of all the various
14 questions we asked people whether they had experienced. Just
15 a series of about 26 questions, and the idea here is if
16 victims had experienced more negative life, maybe that takes
17 up cognitive capacity that could otherwise be used to defend
18 against the onslaught of these highly persuasive tactics.

19 And in fact, we found that there was a
20 statistically significant difference between the number of
21 people who were victims who had had negative life events. So
22 that hypothesis actually came out to be true.

23 PROFESSOR PRATKANIS: And I should point out that
24 every finding that we are presenting today is significantly
25 different using the standard scientific sorts of statistical

1 tests that are appropriate.

2 Let's move on and look a little bit more about the
3 victim in detail, and what they tend to think and feel. What
4 we found is, in our fifth finding, is that: investment fraud
5 victims are more likely to rely on their own experience; be
6 very optimistic; and be open to listening to sales pitches.

7 Let's look at these a little bit more in detail.
8 First of all, investment fraud victims are more likely to
9 rely on their own experience and knowledge when making
10 investment decisions. This has been found in two studies,
11 one that was conducted by AARP in 2003. You see that
12 answering "yes" to that question was higher for the victim
13 than for the non-victim. And again, we found it in the NASD
14 study that we just completed.

15 Now, that would be fine and well, but this comes at
16 a cost. What we find is that the victim is relying on their
17 own experience. And relative to the likely investors in our
18 control group -- the people who were doing investments on
19 their own -- the investment victims were less likely to
20 consult brokers, financial analysts, planners, accountants,
21 lawyers, stock brokers, and even family members for advice.

22 So, what they're doing is they're not going to the
23 reliable kinds of sources that the various agencies offer up
24 here, that are available in community. And, instead,
25 shooting from the hip, relying on their own experiences.

1 They are also extremely optimistic about the
2 future. And this comes up in a number of questions. But one
3 of the questions we asked is in spite of what people say, the
4 lot of the average person is getting worse, not better. And
5 investment fraud victims say, "Hey, that's wrong. The future
6 is looking bright, I am very optimistic about it."

7 We should contrast that, by the way -- and I will,
8 in an upcoming slide -- with the lottery victims. The
9 lottery victims are more likely to say "yes" to this
10 question, to agree to it. They think the future is bleak.
11 And it's evidence for an old quote from Eric Hoffer, who
12 said, "Both fear and hope promote credulity." And that's
13 what these two types of victims have, fear and hope,
14 pessimism and optimism. And the criminal is profiling them,
15 finding them out, tailoring the pitch to them, tailoring the
16 scam to them.

17 And this is on the same line -- but it's
18 particularly troublesome -- investment fraud victims are more
19 likely to listen to sales pitches, especially from sources of
20 a dubious nature. They're more likely to read materials in
21 the mail, that came in the mail, or come over the phone, from
22 people that they didn't know previously. They are more
23 likely to attend that free lunch seminar.

24 And, interestingly enough, they were more likely to
25 respond to our survey. We had 22 percent of the people in

1 our random sample agree to participate, and 50 percent of the
2 investment victims did.

3 The next major finding is that investment and
4 lottery fraud victims have widely different profiles. And
5 this is coming up in a lot of our survey and a lot of our
6 research. Criminals tailor their pitches -- they find out
7 who they're talking to -- and go from there.

8 In the investment fraud, the victim is most likely
9 to be male, living with one or more persons. They are likely
10 to be married, have a high education, making more than an
11 average amount of money. The lottery fraud victims tend to
12 be older, be female, live alone, be widowed, and making less
13 money, and less educated.

14 The bottom one fits the stereotype of the lonely
15 widow that stays at home. The top finds out the -- is a
16 little different. The stereotypes don't suggest that they
17 would fall prey.

18 Important point here is that criminals are
19 tailoring their pitches. With this kind of demographics, we
20 know how to start to tailor our prevention messages, what
21 media to use, what to say, and how to communicate.

22 And just to give you a summary slide of what we
23 found, we find that investment fraud victims are more likely
24 to believe that their fate is up to them, they're in control
25 of the situation, they're optimistic, and they are open to

1 sales pitches. And as Chairman Cox pointed out, that little
2 bit of knowledge, that feeling of control, becomes dangerous
3 in this situation.

4 Lottery victims feels like the world controls them,
5 they're pessimistic. They're actually some of the most
6 skeptical, untrusting people in any of our surveys. They
7 just say, "What the heck, let's do it anyway."

8 MR. SHADEL: We're almost finished here.
9 Investment and lottery fraud victims dramatically under-
10 report fraud. We have, in previous studies, looked at this
11 question, where we have identified -- we have been able to
12 verify victim status, like the NASD findings we are
13 describing here today.

14 In this case, we knew that 100 percent of the
15 victims had lost at least \$1,000. And we asked in three
16 different ways -- we tried to get at what is the most
17 effective way to ask about victim status. And what you see
18 here are the combination of all three of those ways, and it's
19 not that great.

20 Essentially, 23.94 percent of the investment fraud
21 victims admitted that they had lost money -- meaning that
22 there is a staggering error rate, in terms of self-reported
23 data, just staggering -- and 47 percent of the lottery
24 victims admitted their victimization. So, even there, it's
25 over a 50 percent error rate.

1 We want to just give you a concluding couple of
2 slides, just to go back over. So, essentially, con-men use
3 many different combinations of social influence, tactics.
4 And we think this suggests that, in order to defend against
5 fraud, consumers must learn to identify such tactics.

6 Investment fraud victims score higher on financial
7 literacy questions than non-victims, which suggests financial
8 literacy education may not inoculate investors from
9 fraudulent brokers; may help you with legitimate brokers.

10 Investment fraud victims are more likely to have
11 experienced a negative life event. Such events, we believe -
12 - we hypothesize; we don't know this, for sure -- may
13 decrease the victim's ability to defend against swindlers, by
14 using up cognitive resources.

15 And investment fraud victims are more open to sales
16 pitches, which may increase their vulnerability.

17 Investment and lottery victims have divergent
18 profiles, which suggests con-men customize their pitch. And
19 as Dr. Pratkanis mentioned, this also has implications for
20 how we in the community that's trying to stop this might
21 customize our prevention efforts.

22 And finally, investment fraud victims tend to rely
23 on their own knowledge and experience, which could create
24 barriers to reaching them with prevention information.

25 PROFESSOR PRATKANIS: And finally, our

1 recommendations. Now, what new approaches does our research
2 present for actually preventing this crime?

3 First of all, it says we should be teaching
4 investors about social influence, expand from financial
5 literacy -- which is very important -- and look at teaching
6 them about persuasion, and how they can bone themselves up to
7 prevent it.

8 Imagine if Henry had had that information earlier
9 in the slides on fixation, scarcity, and so forth, and he
10 heard that pitch coming in. It would give him one more clue,
11 one more piece of information that this could be a fraud.

12 Second, we want to spread the word about life
13 stresses, disseminate it to families and friends of
14 vulnerable adults, to law enforcement, and so forth. This is
15 really the first time we found anything that predicted across
16 victims. We find things that predict for each specific
17 crime; this is the first one across. And it says to people,
18 "Look, if your family members, your friends have these kinds
19 of experiences, be on the alert. They are especially
20 vulnerable."

21 And finally, we want to conduct additional
22 research. We want to investigate how best to teach about
23 social influence. We want to explore the differences between
24 victims and non-victims, as they think about the social
25 influence situation. Why does one person say, "Ah, that's a

1 scam," when they hear that initial pitch, and the other
2 person says, "No, I'm getting out of that situation?"

3 And finally, we want to look at resistance to
4 influence. We want to find people who went to the free
5 seminar, got initially taken in, but found a way out, and
6 find out how they found that way out, to bottle it, and use
7 it in prevention.

8 That concludes our talk. On behalf of Doug and
9 myself, I want to thank you for coming, thank you for helping
10 to fight this crime. And especially a thanks to you,
11 Chairman Cox, for showing the leadership to bring this
12 together. There are a lot of victims that need it, and every
13 one of them appreciates it. Thank you.

14 CHAIRMAN COX: Thank you very much. An excellent
15 presentation.

16 For five years, the State of California, the
17 Department of Corporations, has had its own initiative,
18 "Seniors Against Investment Fraud," and Anthony Lewis is
19 going to tell us about that.

20 SENIORS AGAINST INVESTMENT FRAUD

21 MR. LEWIS: Thank you, Chairman. I'm Tony Lewis,
22 I'm with the California Department of Corporations. I'm
23 going to speak today about our Seniors Against Investment
24 Fraud program. It's been going on for five years. We
25 believe it's very successful. We have been able to have

1 outreach to probably over 200,000 seniors since inception.

2 Our Seniors Against Investment Fraud -- I will go
3 through the history, our current program, and then the scope
4 of our program. The history of our program is in 2001 we
5 launched the program with a grant from the California
6 governor's office of criminal justice planning. It was to
7 educate Californians over the age of 50 about investment and
8 telemarketing fraud, common schemes, and to protect the
9 citizens against illegal activity.

10 Our current program consists of efforts to
11 strengthen and support our financial market through
12 licensing, regulation, and enforcement. We currently
13 regulate and license 285,000 businesses. That includes
14 investment advisors, financial planners, security brokers and
15 dealers, escrow agents, residential mortgage lenders,
16 commercial and finance lenders, payday lenders, and credit
17 counselors.

18 Our senior education outreach consists of an effort
19 to get out and educate the seniors on a variety of programs.
20 Now, in the hand-out today we just put two pages of our
21 package in there, which are the top financial scams, and I
22 will just go through those now.

23 What we try to warn the seniors against when we go
24 out to these presentations is a variety of scams being
25 perpetrated against the senior citizens. One of them is

1 affinity group fraud, and that is where these perpetrators go
2 out to a religious group, ethnic group, some type of social
3 group, and they either are a member of that group, by virtue
4 of race or ethnic background, or they act like a member of
5 the group, say for a religious purpose, and they infiltrate
6 it. And they may spend months and months to get in with the
7 group, and to get their trust, and then, lo and behold, they
8 sell a financial product.

9 Many times they will get one of the leaders of the
10 group to invest a little bit of money, and then they start to
11 pay that person back, so that they can make that leader, who
12 has years and years of credibility with the group, to
13 convince others and say what a great product it is, because
14 they were able to make their money back. We're just -- we're
15 trying to warn the seniors against that type of approach to
16 taking their money and fleeing.

17 The bait and switch. Many times, senior magazines,
18 senior newspapers, they will offer financial products that
19 offer a great return, a guaranteed return, no risk
20 investment, and then when they get in there they are sold
21 some other type of product that is not insured, not risk-
22 free. Sometimes not even an actual product, they're just
23 taking their money with a promise that the product is out
24 there, and then they flee with the money.

25 The bogus credentials, we talked a little bit about

1 that earlier, in the earlier presentation. But a senior
2 specialist, a certified elder planner, we warn the seniors
3 about those bogus titles. And we actually have a worksheet
4 that we provide to our seniors that tells them to ask that
5 question, "Who certified you? What were the requirements of
6 that certification," and a question on how to contact the
7 organization that provided that certification.

8 CD and bonus. Many times this one works with the
9 bait and switch, and that's where -- especially a year, two
10 years ago, when the interest rates were very low, there was a
11 CD and bonus, offering to pay several times more than the
12 people were getting on their CDs. When they got in there,
13 they found out -- or they didn't find out, but they were led
14 to believe -- that it was an FDIC-insured product, and in
15 fact, they were being switched over to a product that was not
16 guaranteed and, in many instances, did not exist.

17 Charity scams. With the hurricanes, the hurricane
18 relief funds, those scams can be either they're charitable in
19 nature and they're being sold bonds that they say are
20 guaranteed to pay off, or they are business opportunities
21 that say, "We're going to buy all this water in one state and
22 take it over where they need it, and make a lot of money."
23 They are scams, and we encourage our participants to ask
24 questions about that, and to be very critical of those
25 offers.

1 The online escrow accounts. These are -- in
2 California, we have one licensed online escrow agency. And
3 in all those computer online auctions, they always offer
4 these online escrow accounts. And there is only one that's
5 licensed in California, and we encourage people to check them
6 out, make sure they're licensed in the state where they're
7 doing business.

8 Generally, they will ask them to send a certified
9 check or wire money to these accounts, and then they never
10 hear from the person again. So we really encourage them to
11 check out the online escrow companies.

12 The Ponzi pyramid schemes. This one is used in a
13 variety of areas, but basically new money is used to pay off
14 the first investments. A few people are successful, they go
15 out and encourage many others. But ultimately, it just falls
16 apart, because there is just not enough new money coming in,
17 and everybody is left holding the bag with their investment.

18 Many times you will see this one combined with
19 affinity group fraud, where they keep pumping in the money
20 with the new investors, but ultimately it can't survive when
21 the new investors dry up.

22 The variable annuity sales. This is -- and this
23 issue is one that is very sensitive to the elderly
24 population, and that is where it's a perfectly legal product,
25 but it's being sold to unsuitable investors. And that is, we

1 encourage our investors to ask questions like, "What are the
2 penalties? How long is the penalty period? Is it 15 years?
3 If I want that money within 15 years, am I going to have to
4 pay a substantial penalty?"

5 And for someone who is 85 years old, even though
6 the rate of return is guaranteed not to go below a certain
7 amount, if they need that money in the next 15 years, they
8 may be paying a substantial penalty.

9 The other question was ask them to ask those
10 salesmen is, "How are you compensated for selling this
11 product?" If it's 15 percent for selling that product, they
12 need to ask the question of themselves, "Is this person
13 really giving me good advice, or are they giving me self-
14 serving advice?"

15 Buying the death benefit for another person. This
16 can be a confusing product when it's being sold by the
17 salesperson. They're guaranteeing the rate of return. You
18 invest \$10,000, they guarantee that you will get \$15,000
19 back, or \$20,000 back. But the triggering event is the death
20 of somebody else, which, in many instances, is hard to --
21 there are a lot of variables in it, but one is the death of a
22 life, but also is, is the premium going to continue to be
23 paid on that until that person dies? Is there going to be a
24 challenge? Can the insurance company challenge the validity
25 of that life insurance policy?

1 So, we just warn the investors to ask those
2 questions and know those answers before they part with their
3 money.

4 The wrong number stock tip. I was looking on the
5 Internet for one, and I couldn't find it, but these are very
6 sophisticated phone calls, in that they find a stock, a penny
7 stock.

8 They make these phone calls, and they will only
9 leave a message when they get a telephone answering machine,
10 and it's, you know, "This is So-and-So, I hope you still live
11 at this number. I just found out from my new girlfriend that
12 works at this company, that the stock is going to go through
13 the roof, and so you should buy it today," and then they hang
14 up and then the person invests in it, they move that penny
15 stock value way up, and then as soon as it gets up to the
16 certain point, the person who has made that -- those phone
17 calls.

18 I think now, with the Internet, you're seeing it
19 packaged a little bit differently, and I know I've been
20 getting some of this junk e-mail where it says, "Invest
21 today. The target is going to be \$2 a share, and right now
22 it's at \$.15 a share." And so they get you to try to drive
23 it up. And of course they can reach many more people on the
24 Internet than they can on the phone calls. So those are the
25 main top financial scams.

1 So we're looking at prevention, instead of
2 victimization. So we try to educate the senior population.
3 And the way we do that in California is we have extensive
4 training of our volunteers. We go out, we call in a group of
5 volunteers. When they sign up, we put them on a list.

6 And then, when we have time and the ability to do
7 the training in the location where the volunteers are, we do
8 some extensive training, we give them a comprehensive
9 training manual, we support them by telephone, and in person
10 when necessary. We give them educational materials to hand
11 out.

12 And currently, we just approved a new package --
13 and it's on our Internet site -- which is on the form that's
14 in your package today. But it's 16 pages of investment fraud
15 information that we give out to all of our seniors. Some of
16 it is California-specific, but other parts are -- I think
17 could be adapted to any jurisdiction.

18 We deliver it in an appealing package. At some of
19 the events we have a canvas carrying package that people can
20 use for their grocery shopping, or other shopping needs.
21 They have developed, I know in some of the jurisdictions, a
22 bingo game, so that when they go out to the lunches, they can
23 get the seniors to learn.

24 And then probably the most important one -- and
25 it's -- I didn't put it in the package, but it is on our

1 Internet site, and it is a page that we ask the seniors to
2 use, as a worksheet, when they go to these investment
3 seminars, and it's called "Check Before You Invest," and it's
4 asking the person's name, their license number, who they are
5 licensed by, if they are a specialist, who gave them that
6 specialist designation, what they had to do.

7 And then, it also asks them to disclose how they're
8 compensated for selling that product. And we really drive
9 home the fact to the people that are buying the financial
10 product, "Know the answer to that question, and you will know
11 whether you are getting objective advice, or advice that
12 could be self-serving to the salesperson."

13 Our presentations currently, we do it at senior
14 centers, churches, community groups, conventions, and health
15 fairs. And that's -- we found that that's the best way to
16 get out there to the public, and educate these folks.

17 Our partnerships. We have -- do community groups.
18 Last month, we were at Laguna Woods, which is in Orange
19 County, in California, 15,000-plus person retirement
20 community. We participated in the fraudfest, handed out
21 these packages. We were on their closed circuit cable, did a
22 presentation, and answered their questions.

23 We partner with state governments. Florida and
24 Icwa have used our program currently, and Missouri and
25 Tennessee are considering implementation. We work with the

1 SEC. We're on the free lunch sweeps, joint investigation and
2 sharing of resources, and security regulators associations --
3 NASAA and NASD -- we assist in development and distribution
4 and expansion of these types of programs.

5 So, in closing, our message is pretty simple, and I
6 think it's one that will go a long way. And it's, "If it
7 sounds too good to be true, it is." Thank you.

8 CHAIRMAN COX: Thank you, Tony. And to wrap up the
9 presentation portion of our program, we're going to have
10 Linda Thomsen and Lori Richards give us an update on
11 enforcement and examinations.

12 ENFORCEMENT AND EXAMINATION UPDATE

13 MS. RICHARDS: Thank you, Chairman Cox. I'm going
14 to start with an update on the SEC's examination efforts.

15 As part of the initiative to protect seniors, in
16 the examination program at the SEC we have been working very
17 closely with our colleagues at the state securities
18 regulatory agencies, and with the NASD, and we have
19 prioritized the protection of seniors as investors in our
20 exam program.

21 One key part of the initiative is to focus on the
22 detection side, on the detection of use of sales practices.
23 And what I mean by that are the high-pressure overtures that
24 can lure investors to invest in products that may be highly
25 unsuitable for them, or even fraudulent.

1 In our onsite compliance examinations of both
2 broker dealers and investment advisors, we are taking a very
3 hard look at the representations that are made to investors
4 to determine if they are overblown and misleading. And we
5 are also seeking to identify the firms that target senior
6 investors.

7 And based on the information that I have seen to
8 date, including the internal communications within firms
9 where salesmen talk to one another, it seems very clear that
10 there are some salesmen that are out to get the senior, as an
11 investor. I think that we should be very certain that
12 seniors are a target, and they are a target not just of the
13 scrupulous and the legitimate securities salesman, but also
14 of the unscrupulous.

15 One very successful method that salesmen -- both
16 legitimate and not -- use to attract investors is the free
17 lunch sales seminar. These sales seminars are often
18 advertised in local newspapers, and they are often advertised
19 to potential investors and attendees by cards that are sent
20 in the mail. These seminars are held at hotels and at chain
21 restaurants. And in addition to the sales pitch, you get a
22 free lunch or a free early bird dinner.

23 As part of the Chairman's initiative in this area,
24 we have commenced onsite compliance examinations of the firms
25 that sponsor these free lunch sales seminars. Along with

1 state securities regulators and the NASD, examiners are
2 conducting examination sweeps in Florida, California,
3 Arizona, Texas, North Carolina, and Alabama.

4 Regulators are now examining almost 40 firms, and
5 more firms have been identified for examination. In these
6 examinations, we are looking at: whether the sales seminars
7 are supervised; and whether the sales materials used have
8 been approved by the NASD; whether sales people are making
9 wild claims of possible returns on investments; whether the
10 risks inherent in any investment are disclosed to prospective
11 investors; whether investors are sold out of perfectly good
12 investment products and into new products with higher fees,
13 and which entail more risk; and whether the products
14 recommended appear to be suitable for the investor.

15 While these exams are very much underway, let me
16 give you a sense of what we're finding, particularly with
17 respect to the sales pitches that are being used.

18 These sales seminars are, indeed, specifically
19 targeting seniors. Most of the people that attend these
20 seminars are seniors. The seminars have titles that are
21 designed to particularly appeal to the senior investor. They
22 are titles like, "Senior Financial Survival Seminar," "Senior
23 Citizen Tax Special," "Senior Financial Safety Workshop,"
24 "Senior Citizen Retirement and Asset Protection Education
25 Seminar."

1 In addition, we found that these seminars are also
2 designed to play on seniors' interests in health care. So
3 there are seminars called, "Annuity health check-ups," and
4 "Sleep Well at Night Financial Doctor." These seminars are
5 being held in communities of all sizes.

6 I believe that one of the reasons why they are
7 successful in attracting attendees is that, in addition to
8 the free lunch, they are not at all intimidating. They are
9 not held in some ivory tower office park. They are held in
10 the local spots where people feel comfortable, maybe where
11 they have had a meal in the past. They are held in the local
12 chain restaurant or local hotel, and the participants
13 attending these seminars look very much like the senior
14 attendees. They are other retired seniors in the community.

15 And the salesmen may also be local, or they may
16 advertise that they have been serving the local community for
17 many years. The seminars are not advertised as being held by
18 some faceless financial services company, "Independence
19 Financial," but they are advertised as being held by the
20 sponsor himself, the salesman himself, in his own name. So,
21 often, the investment cards and the advertisements will say,
22 "Bob Jones invites you to attend a special personal financial
23 seminar."

24 Often, Bob Jones's smiling photograph will appear
25 on the advertisement, soliciting attendees. The salesmen may

1 also be members of the local country club, church, or other
2 group. And seniors feel comfortable attending these events.
3 They're not intimidating.

4 Many of the sales seminars are also specifically
5 targeting seniors through advertising investment advice,
6 estate planning, retirement planning, and inheritance advice.
7 Then, at the sales seminar, the salesmen often pitch
8 particular products. And we have heard from the other
9 panelists this morning about what products are being pitched.
10 They are often variable annuities, mutual funds, equities,
11 separately managed accounts, and equity indexed annuities, in
12 particular.

13 Some of the sales materials that we are seeing in
14 these examinations are loaded with exaggerated claims and
15 gimmicks. Let me give you a couple of examples.

16 These are actual examples from the sales literature
17 that we have seen: "How to maximize your estate up to 10
18 times for your heirs, based upon current assets." That was a
19 pitch used by a certified senior advisor. "Immediately add
20 \$100,000 to your net worth." And, "This is the most
21 important gourmet meal event that you will ever attend. Free
22 food, free golf, and free drinks." "Making money on the
23 downside of markets: how to receive 13.3 percent return."
24 "How \$100,000 can pay \$1 million to your heirs."

25 "Help protect your nest egg from being taxed up to

1 71 percent." "Reduce income taxes up to 42 percent."
2 "Lifetime payouts of seven percent and higher. Learn
3 portfolio techniques that can eliminate investment losses."
4 "Turn any account into a tax-free inheritance. Triple the
5 size of the account, using annuities."

6 These are troubling representations. But what's
7 maybe more troubling is that many of the firms that we're
8 examining appear to have weak or no procedures to supervise
9 some of these sales seminars. And we're finding that some of
10 the sales seminars seem to be completely unsupervised.

11 We're concerned about whether seniors at these
12 seminars are buying financial products, legitimate financial
13 products, variable annuities, mutual funds, equity index
14 annuities that are not suitable for them because of their
15 time horizon for investing, because of the need for cash in
16 the near term, because of the very high fees that accompany
17 these investments, and because of the risk of the
18 investments.

19 Let me give you a couple of examples of perhaps
20 unsuitable sales to seniors. At one seminar, participants
21 were pitched illiquid investments that they could not sell
22 after they purchased them, and very speculative limited
23 partnership interest. One elderly gentleman, who needed the
24 funds to live on during his retirement years, put over 60
25 percent of his net worth into the investment.

1 Another salesman sold a variable annuity to a
2 retired couple with an annual income of \$50,000, and a liquid
3 net worth of \$200,000. But the cost of the policy that they
4 purchased was \$174,000, taking most of their liquid net
5 worth. While what they wanted was to leave the principal for
6 their children. They had to continue to draw on it for
7 monthly expenses.

8 Unfortunately, in these examinations, we're also
9 finding some examples of what may be misleading statements or
10 even outright fraud. For example, salesmen at one seminar
11 said that they used advanced technical knowledge in
12 developing an advanced mutual fund selection system,
13 combining various services and numerous databases. In fact,
14 this advanced technical knowledge consisted of no more than
15 an off-the-shelf software program that was available to
16 anyone on the Internet.

17 And at another seminar, the salesmen touted their
18 extensive and successful industry experience, over 50 years
19 of industry experience with major investment firms. One
20 salesman said he was a member of the chairman's club at two
21 prior large financial services firms, and another one said
22 that he had been featured in several publications, and
23 identified as one of the top brokers in the state.

24 In fact, these salesmen had received many, many
25 customer complaints, and were the subject of many

1 arbitrations awarding other investors damages for fraud,
2 misrepresentations, and non-suitable investments. So, I
3 suppose that while these salesmen may have been experienced,
4 their experience was not of the type that any investor would
5 appreciate.

6 While these examinations are very much underway,
7 we, as regulators, have concluded that we were quite right to
8 focus on this issue. And we hope that by working together
9 with the state securities regulators, and with the NASD, we
10 can help protect seniors by better detecting fraud and
11 unsuitable sales practices, and by educating seniors about
12 the problems in this area. And perhaps most importantly, we
13 have put the firms on notice that their compliance systems
14 and their supervision of sales seminars must be robust.
15 Thank you.

16 MS. THOMSEN: Thank you. It is really an honor to
17 be with this crowd, and I think it is fair to say that it is
18 fitting that enforcement speaks last in this matter. Because
19 the truth of the matter is, enforcement should be the last
20 resort.

21 Not because we aren't more than willing and able to
22 go out and make every scamster we run into's life miserable,
23 but because when we're on the scene, that means there is at
24 least one victim, and probably more. And when all is said
25 and done, however effective we are, at the end of the day,

1 for the victims involved it will always be an unhappy day.

2 I've got good news and bad news. The good news is
3 that we have investigations ongoing into conduct that
4 victimizes seniors throughout the country. The bad news is
5 we have investigations into conduct that victimizes seniors
6 throughout the country.

7 As the chairman pointed out, just recently we
8 brought a case in New York, and today there is a case being
9 filed in California. These scams, these types of problems,
10 are everywhere. And one of the first rules of law
11 enforcement is you follow the money. And the reason that's
12 one of the first rules of law enforcement is because it's one
13 of the first rules of scamming. You follow the money.

14 As the chairman alluded to, when Willie Sutton, the
15 notorious bank robber, was asked why he robbed banks, he
16 said, "That's where the money is." And the reason people
17 victimize seniors is that's where the money is. There is an
18 enormous concentration of wealth among senior citizens. And
19 just -- if you're going to rip somebody off, you might as
20 well rip off somebody who has got real money. So, that's
21 what we're seeing.

22 I think of the categories of schemes, if you will,
23 in three major buckets. And we have alluded to all of them
24 here today. And they overlap. The first bucket is the
25 bucket of inappropriate product. In some instances, it's a

1 perfectly fine product for some investors, but not the
2 investors it's being marketed to. It's too illiquid, its
3 time range is too long. Someone is looking for a very safe
4 investment, it's a highly risky investment.

5 We also see with seniors fairly frequently that
6 seniors actually have a portfolio that really does meet all
7 their needs and all their objectives. And someone comes in
8 and tries to tell them that those needs will be better met by
9 something else, when all they are actually doing is
10 generating higher commissions, selling -- causing people to
11 sell perfectly fine investments, and maybe investing in other
12 fine investments.

13 But in the interim, what they're doing is paying a
14 lot of commission. So that's one bucket of problems that we
15 have seen, and that have -- we have discussed.

16 The other -- or the second, if you will -- are what
17 I categorize as offering frauds. Sometimes it's an
18 investment in a legitimate company. Sometimes in one that's
19 less legitimate. But more often than not, you see
20 downplaying of risk over promising of return, as Patty
21 referred to. And there are practices associated with those
22 offering frauds to get people invested in highly risky
23 ventures that they think are perfectly safe, and end up with
24 enormous losses. So that's a second bucket of problems.

25 And the third, and perhaps in some ways the most

1 dangerous -- and certainly the one that can generate the
2 biggest losses -- are the Ponzi and pyramid schemes which,
3 when you strip them all down, are nothing more than chain
4 letters. You put money into some kind of investment, nothing
5 is invested, the promoters use the money either to pay off
6 the early investors, or to pay for their own lifestyles,
7 their limousines, their hotels, other costs and expenses,
8 their lavish lifestyle.

9 Because I guarantee you that while they victimize
10 people who are savers, they are not themselves savers. They
11 are very much spenders. And at the end of the day, the money
12 is dissipated very, very quickly in those schemes.

13 And the real tragedy in those schemes is that it is
14 often late in the game before anyone finds out about them,
15 because some of the early investors are getting paid with
16 other investors' monies -- frequently their friends and
17 relatives who they have brought into this scheme -- or they
18 are getting statements showing they are making the kinds of
19 returns they have been promised. It is only towards the end
20 when things start to collapse, and at that point there is
21 very little to recover.

22 So those are the three sort of basic buckets that
23 we see, and that we are focus on as we go along. And I must
24 say that I, too, have a one investor story, and my investor
25 story goes back to one of the first cases I tried when I came

1 to the Commission. And as far as I can tell, it's a case
2 study for the study.

3 This investor was 78 years old. She was widowed
4 young, and raised three boys on her own. She educated them
5 on her own, she got them through college. She was a bank
6 manager and financially savvy. She invested in a Ponzi
7 scheme. She -- we, on our side -- this was a very successful
8 law enforcement effort. We got a TRO very early.

9 It turned out that all the money had not yet been
10 spent. We were able to freeze all of the assets. We held
11 auctions, we sold off the limousines -- but of course they
12 were poorly maintained, because Ponzi scheme people don't pay
13 all that -- they're just going to go buy another limousine.
14 We drilled out safe deposit boxes.

15 And at the end of the day, we very, very proudly
16 delivered \$.60 on the dollar to those investors, which was an
17 enormous success, from a law enforcement perspective. From a
18 victim's perspective, who went into this scheme thinking that
19 the \$100 they had, the \$1,000 they had, the \$10,000 they had
20 was not sufficient for their investment needs to get \$60
21 back, or \$600 back or \$6,000 back on the \$10,000 was really
22 not a great success.

23 And the true tragedy in all this is that when my 78
24 year-old victim got her \$.60 on the dollar back, she
25 reinvested with the same promoter for the same reasons that

1 we heard about in the study, and ultimately became one of the
2 key witnesses in the second contempt trial against this man.
3 And we were quite successful, again, thanks to her testimony.

4 But in the meantime, she ended up, at the age of
5 78, working at the local supermarket so that she could
6 maintain her household. So, on the one hand it's a
7 successful law enforcement story. It's a terrible personal
8 story, and it just goes to demonstrate, at least in my mind,
9 what we have all been saying all along, that law enforcement
10 is the last resort here, and that education is enormously
11 important, as we move forward.

12 And on that less than optimistic note, I think I
13 will -- I am done.

14 CHAIRMAN COX: Well, thank you very much. For the
15 next portion of this summit, what we are going to do is have
16 almost no ground rule whatsoever, other than request that you
17 identify yourself as you just leap right in.

18 We have four commissioners: Paul Atkins, Roel
19 Campos, Annette Nazareth, and Kathleen Casey, who have been
20 silent throughout, so I encourage you to leap in and lead the
21 questioning, perhaps. But rather than a requirement that you
22 be recognized by the moderator, just feel free to dive in.

23 And I will -- if it becomes necessary, if there are
24 three to five people talking at once, maybe I will restore
25 some order. But let's try it completely free form, and see

1 how that goes.

2 PANEL DISCUSSION

3 MR. KETCHUM: Chairman Cox, maybe -- it's been, I
4 think, a great presentation. I would like to perhaps take it
5 in a slightly different direction that may be -- and suggest
6 the Exchange is leaning towards some of the larger firms that
7 are our members, and go back to some of the things that Lori
8 Richards indicated. They were quite powerful.

9 Our battle at the Exchange tends to be less about
10 scams and more about questions that -- how do basically good
11 firms allow bad things to happen to people, good people who
12 are customers that they supposedly value?

13 And firms that do sink substantial money into
14 compliance do sink some money into education, into review of
15 sales literature, and a variety of other stuff, yet -- and
16 with customers who do not fall victim to moving -- going
17 along with scams, but instead choose to work with highly
18 recognized firms, and yet still receive substantial industry
19 injury and mistreatment.

20 And I guess there is something I would like to put
21 on the table and basically -- what we're trying to do is we
22 look and work with the NASD and the Commission in pushing the
23 firms to basically reassess how they go about their oversight
24 and compliance efforts in three ways.

25 First, the failure of many large firms not to

1 integrate the tools they have for compliance. We find again
2 and again that firms have sophisticated central compliance
3 tools, high efforts to look at new products as they come on,
4 and yet still devolve most of their responsibility onto a
5 branch office without following the indications that there
6 are problems there.

7 In particular, failure for firms to follow up on
8 activity letters, to truly probe, from the standpoint of
9 investors, what's happening and what trends are occurring
10 with respect to a rep and a branch manager, but instead,
11 being willing to accept the fact that a customer simply
12 doesn't complain with an initial letter, and without really
13 looking at the trends of activity letters. And I think
14 that's one key reason why firms miss these things, and why we
15 are continually sweeping up bodies, rather than getting in
16 front of it.

17 Secondly, the effort of even major firms today
18 still seems to be too wooden, in the way they look at
19 incentives and look at trends. And they don't pick up
20 changes in what may have been commonly thought to be good
21 strategies, and the rest. They don't focus on exactly the
22 type of science that was described here earlier, to identify
23 situations of high risk when there hasn't been an event, when
24 an investor who has been investing relatively small amounts
25 suddenly receives a large amount of money, and how that's

1 invested.

2 And we find again and again that there just isn't
3 the firm focus on those events of risk at a high enough
4 level, versus just overall reviews that don't seem to pick
5 that up.

6 And it -- and finally, we find that a good deal of
7 the frauds that we see with respect to major firms occur with
8 respect to reps selling away, and pulling customers into
9 things that are not firm-sponsored products. And there has
10 been a tendency, even by ourselves and by regulators and by
11 the firms of saying, "Well, we can't help that, because we
12 can only control the products that we sell, and if reps lead
13 people down a path by putting them in scams outside of that,
14 unless we have a customer complaint we don't see how we can
15 address that."

16 And I guess, again, I would challenge that, and
17 we're trying to begin challenging that, because it seems to
18 me when was the last time, when you opened an account, that
19 somebody explained to you that a rep can't sell anything
20 other than a firm's product? When was the last time you have
21 been asked, while operating -- while significant withdrawals
22 have been made in your account, as to what you are doing with
23 the money, and the rest?

24 And I think, again, that type of more interactive
25 issues, even when there doesn't seem to be, on its face, harm

1 in an account, is something that we are trying to begin to
2 ask the firms to be more proactive, both from the standpoint
3 of their supervisory responsibilities, and a best practice
4 standpoint.

5 So, I would just like to add that to the table,
6 that it does seem to me that we have got to worry not only
7 about the scams, but about developing the science with
8 respect to the firms that want to do the right thing, so that
9 they are more effective at it.

10 COMMISSIONER ATKINS: Yes, I wanted to second that,
11 I guess as well, and I do think what was very instructive was
12 the empirical studies that you all have done regarding the
13 social aspects. I think that's very important. It shows
14 just how important investor education is.

15 But going into, you know, a lot of the problems
16 that we see are because of recidivists, people who -- you
17 know, they might get smacked with an injunction, or some sort
18 of regulatory penalty, but yet they do it again. And I think
19 that's our biggest challenge, to try to see how we can get at
20 that.

21 Linda's story comports with my own experience of
22 having tried to work out Ponzi schemes where investors -- in
23 one, 20,000 investors lost more than \$1 billion. And even
24 though we were able to recover 70 percent of their money,
25 that's still a lot of money down the drain.

1 And so, I think we really have to work with the
2 states and with the exchanges and the NASD, to try to see how
3 we can get at these recidivists. But I think, more -- also
4 as important is to look at ourselves internally, and see how
5 we can help make it -- help build incentives for our own
6 people to be able to go after these particular things.

7 Because all too often, these recidivists rely on
8 our losing interest, because it's very difficult and hard to
9 do the footwork and the legwork and the real detective work
10 to track this down, and to build a record in order to be able
11 to shut something down and to talk to witnesses and all that.

12 And so, they count on -- you know, in our case,
13 being a big federal agency, trying to look after a whole
14 country. But that's where we can, I think, work very
15 effectively with the states and other law enforcement
16 agencies. We have done it with the FBI and other things with
17 scams, and I think we just -- we need to figure out how we
18 can help incentivize our own people so that they realize that
19 this is an important priority.

20 MR. CAMPOS: I just have -- I sort of agree with
21 what Mr. Atkins just said. I think we need to worry about
22 all of those things. I guess what troubles me a little bit
23 is the results of the survey. I would like to go back to
24 that for a second.

25 I think many of us have felt that -- maybe, at

1 least -- a major part of the answer was investor education.
2 And yet, your study very clearly shows that it is many who
3 are very well educated, who understand the details of
4 diversification, the details of financial products that are,
5 themselves, the most susceptible to some of these scams.

6 And I guess that goes to sort of a -- as you said,
7 a psychological or a social vulnerability. We are many
8 things, but we are not psychiatrists, psychologists -- at
9 least not in make-up. You know, maybe that's the way we
10 should, in the future, ask for Congress's money. Maybe we
11 should have that kind of a subdivision in our Agency.

12 But I only half jest. I suppose I -- what would
13 you recommend be the next -- how do you fight that? Or does
14 the regulator have a role in that particular vulnerability to
15 psychologically, socially, your biggest threat are your
16 friends, perhaps, you know, your community? What -- where do
17 you stand on that issue today?

18 MR. SHADEL: Well, if I had the answer to that, I
19 would probably be out -- no. This is a hard question. And I
20 think, you know, we don't have a silver bullet answer.

21 But one of the things we have found, when we
22 compared -- on the question of financial literacy, there are
23 other studies we have found -- one done by Washington State
24 University -- that found a similar trend where they did a
25 study of predatory lending victims and non-victims. And they

1 found in the domain in which the people were victimized, they
2 knew a lot about credit card debt, APR, and so forth, just
3 like in this study, the NASD study, the investor fraud
4 victims knew a lot about the domain in which they operated.

5 But this is what keeps pointing us back to teaching
6 people about the persuasion tactics. This is just my own
7 opinion, but I think if we go out and just teach people the
8 difference between a stock and a bond -- and I'm
9 oversimplifying -- and not about persuasion tactics, it's
10 like teaching a new poker player the difference between three
11 of a kind and a full house, and nothing about the concept of
12 bluffing, that there are all these nuances in the sales
13 environment that people just aren't taught.

14 And so, that's, I think, all that's being said
15 here. Chairman Cox quoted us accurately, as the report is
16 saying financial literacy is necessary, but perhaps not
17 adequate. And I just think we need more testing of can you
18 teach these persuasion tactics, and does it inoculate people
19 from being victimized? I don't think we know that yet. We
20 need to look into it more, and do more research.

21 CHAIRMAN COX: You know, I just want to jump in and
22 say that Chris Hansen and I have talked a little bit about
23 this, the idea that interactive data might actually provide
24 more opportunities for people to do an end-run around that
25 personal selling.

1 What's going on in the dynamic here of educated
2 investors nonetheless succumbing to fraud is that what we're
3 calling the social influence, the either persuasion
4 techniques or such high-pressure sales tactics that it
5 amounts to abuse, is that the interpersonal part is clouding
6 their judgement.

7 So, if we can find a neutral objective setting for
8 them to test some of these claims that are being made, we've
9 got a way around it. If you think about the paradigm of the
10 high-pressure sales person, it's the used car salesman. Now
11 we can go onto Edmunds.com, and check and see, you know,
12 what's really out there. And when we show up at the used car
13 lot, we're armed with some real facts.

14 Now, the Internet, of course, is fraught with
15 peril. There are just as many scams on the Internet -- or
16 more -- as everywhere else in life. So that's a two-edged
17 sword. But properly applied, this could be a great tool.

18 MS. SCHAPIRO: I think that that's exactly right.
19 If we could eliminate the social influence, that would be
20 enormously beneficial. And we don't know if we can do that.

21 The other way might be to override it with such
22 credible, authoritative information that comes from source
23 that seniors really trust.

24 And one of the things we have been toying with as
25 an idea, when you go to the public library during the week,

1 you will find lots of senior citizens there, looking up stock
2 prices, researching investments, looking at the prices of
3 gold coins in the magazines, and so forth. If we could
4 empower librarians, for example, to intercept those people
5 and point them to some more credible sources of information -
6 - from the SEC, from the states, from the NASD -- that might
7 be a way to help counteract some of the social influence.

8 It obviously doesn't deal with the broker who calls
9 and tells you you urgently have to get involved in an
10 investment, but I think if we could explore -- and hopefully,
11 we will do so through this survey this summer -- what other
12 sources senior citizens might find as credible that we could
13 help to use to balance the social influences of the con-men,
14 it might be a valuable way to go about it, as well as trying
15 to eliminate them, as you suggest, Chairman Cox.

16 MR. DUFAUCHARD: I just want to make one point
17 about the social influences. I think it has two effects.

18 The first effect, of course, is to get someone into
19 the investment scheme. But the second effect, I think, may
20 be to inhibit prosecution of valid fraudulent claims. We
21 hear about these stories that came up in the study, as well
22 as the case that Linda Thomsen successfully prosecuted.

23 But the important information that came out of this
24 study, as well as some of what we are trying to influence our
25 seniors to do through our educational programs, is to report.

1 There is a lot of investment fraud that goes under-reported.
2 I think the data you showed indicated, like what, 50 percent?

3 PROFESSOR PRATKANIS: Fifty percent for lottery,
4 and seventy-five percent for investment.

5 MR. DUFAUCHARD: So, to the extent we can combat
6 the social influences, I think it would be good to do that up
7 front, on the educational piece, but as well to encourage
8 prosecutions.

9 MS. NAZARETH: First, I would like to say this is
10 really a fantastic use of social sciences research, to assist
11 us in protecting investors. And I think that's a very
12 exciting opportunity.

13 I also note that when you compare sort of what you
14 were talking about in educating people on social influences,
15 you could do that, combined with the type of work that
16 California has done, which really is sort of targeted at the
17 types of products, or the types of scams that are common, I
18 think, you know, that's a very powerful tool in educating
19 investors, both in how they're going to deal with these
20 situations when they confront them, and then what are the
21 common types of, you know, actual products or services that
22 they do confront.

23 I thought that Mary raised a point that, you know,
24 I find really the sort of next step, which is what is the
25 best way to use all of this information to have broad

1 outreach to investors. It just strikes me that, you know, we
2 talk about libraries, we talk about, you know, these sort of
3 grass roots ways of dealing with people. But I do wonder if
4 we don't sort of do it in a much bigger way, either through
5 the use of television or other telecommunications, how you're
6 really going to be effective.

7 I listened to one of those -- I must say -- to one
8 of those sales tactics that sounded like -- it said to Kathy,
9 "It sounds like the Home Shopping Network." You know? I
10 mean, people hear this kind of thing all the time, I think.

11 I think they're actually, at this point, so used to
12 hearing high-pressured sales tactics on television and things
13 like that, it would be sort of an opportunity to sort of have
14 people step back and say, you know, "I do not have to be
15 influenced by this." You know, and I think they would be
16 better able to protect themselves, going forward.

17 MR. HANSEN: I would just like to say I think in a
18 way, in this conversation that we have been having, I think
19 that we have been redefining what financial literacy is. I
20 think that we are really saying that it has to be far broader
21 than people traditionally think of it. We have to help
22 people not only understand the basics of finance, we have to
23 help them understand where the trip wires are out there, and
24 what kinds of things they will run into.

25 And then, we need to have other tools, like

1 interactive data and regulations they can read, et cetera, et
2 cetera, and everything else we can do to create transparency
3 in the system overall, so that people have an opportunity to
4 keep making themselves not only literate, generally, but
5 making themselves literate about specific things that they
6 will encounter.

7 MS. STRUCK: I would be interested in knowing if
8 there have been any studies of whether securities regulators
9 and people like those of us up here can compete to become
10 trusted advisors, because one of the things we have talked
11 about a lot this morning is educational efforts that we
12 actually make in the communities where seniors live.

13 And I -- as I was coming to today's program, I
14 received an e-mail from an investor in Wisconsin who said,
15 "Dear Patricia. I see you will be attending a senior summit
16 in D.C. on senior fraud. If you can, please tell them how we
17 here in Wisconsin stopped this fraud case with the help of
18 your department and our DoJ."

19 I think that getting the word out through programs
20 like this, but also in the community where the investors
21 live, and making them a part of the process -- Linda's
22 example notwithstanding -- I think that we can prevent
23 individual instances of this from occurring.

24 MS. CASEY: I wanted to follow up on a couple of
25 the comments that were made earlier, most recently by Mr.

1 DuFauchard.

2 In as much as you are addressing the challenge of
3 under-reporting -- and it seems to me that this really speaks
4 to the need for additional research, and understanding the
5 limits of education -- some of the findings of the senior
6 investor fraud study I thought were pretty insightful, in as
7 much as it identified particular psychological profile of
8 individuals that are most vulnerable to investment fraud.

9 And some of the key findings, as we noted earlier,
10 were that they were more financially literate, but that they
11 were also less inclined to report that fraud.

12 So, the question I would ask, maybe to Dr.
13 Pratkanis and Mr. Shadel and others, is what kind of research
14 is necessary to better appreciate the kind of education that
15 is necessary to encourage greater reporting? And is that
16 more targeted than general financial information, or
17 understanding the powers of persuasion? And if you can,
18 identify research that perhaps has been done in other lines
19 of study.

20 PROFESSOR PRATKANIS: Thank you, Commissioner
21 Casey. I think there are a number of things that need to be
22 done. First of all, how does a person -- how do these
23 victims think about the offer when it comes to them? What
24 kind of metacognitions do they have? What are they thinking?

25 We did some preliminary in the focus group studies

1 of this, and what you find is the victims are thinking, "That
2 sounds like a good idea." The people who were not victims
3 said, "That's a scam. I want to get out of this situation."
4 And it would be very helpful to understand those kinds of
5 thought processes in detail, to look where we can cut it off.

6 Another thing to do is the reason it's -- there is
7 a lot of reasons why it's under-reported. Sometimes people
8 may not view it as an investment fraud. It was just a bad
9 deal. But one of the keys is that people find themselves in
10 a rationalization trap. They can't admit that they have been
11 taken. They are in a situation where if I say I've been
12 taken, I'm losing all the money, I lose the self-esteem, I
13 lose the trust. And it's a very difficult situation there.

14 And what we want to do is focus on how to get
15 people out of that rationalization trap. There is literature
16 in social psychology about it. We want to look at places
17 where people have gotten -- like their family and friends
18 have gotten victims out of that situation. We want to look
19 at people who go with the free investment, may take a little
20 nibble at the apple, but find themselves getting out. We
21 want to look at that.

22 And then, we also want to try out these kinds of
23 interventions to see if they actually work, and to get the
24 information from that situation and start to apply it.

25 CHAIRMAN COX: I would like to throw out a question

1 for I'm not sure whom, because we don't have a lot of
2 industry represented here. But Rick, maybe you can help us,
3 or the regulators who deal with these firms every day might
4 know something about what I am going to ask.

5 One of the unique aspects of what we're talking
6 about today is that investors, be they novices or
7 sophisticated, who run into these problems also might be in
8 these circumstances at the very moment when their acuity is
9 in decline. And that happens differently with different
10 people, and with some people not at all. They go to their
11 grave at 101, sharp as a tack. But for some people, dementia
12 and other things are issues.

13 Are there best practices in the industry so that
14 when you have got discretion over someone's money, and their
15 ability to interact with you is in obvious decline, you do
16 something about it? Do you have a requirement to check with
17 a care giver? Should people be setting up these arrangements
18 for themselves in advance, and being very specific about the
19 broker's ability to deal with another person? What is out
20 there?

21 MR. KETCHUM: Well, I think it's a great question.
22 Far be it from me to speak for the industry from my wizened
23 one year of experience in the industry, but I think firms do
24 worry about that.

25 I think you're absolutely right, Chairman Cox, that

1 one of the things investors should think about is
2 understanding how firms will address that if they run into
3 periods where they may be ineffective, and not -- and as
4 well, frankly, speaking to people they trust, their family
5 and otherwise, to make sure that their family will intervene.
6 Because depending on a firm to have the controls to recognize
7 that is, I think, risky for the individual. They ought to
8 first focus on people they trust, and make sure that those
9 persons are paying attention.

10 It is things that firms worry about, but as I said
11 before, I don't think worry enough about. I don't think -- I
12 think firms are -- have fallen -- as they have evolved better
13 techniques over time, they are still far too wooden and far
14 too much not looking at risk levels as individuals, for one
15 reason or another. They appear to change the way they're
16 investing, appear to change the way they're relating to the
17 salesman.

18 So, I think it's a great point. It really comes
19 down to, again, that firms need to be more proactive with
20 their customers, and with those risks, than they have been in
21 the past.

22 MS. SCHAPIRO: The only thing I would add to that
23 is the foundation, really, of investor protection for the
24 securities markets is the suitability concept, that no broker
25 can recommend a product to an investor that's not suitable.

1 And part of a suitability analysis has to be the competence
2 of the investor to understand and appreciate the intricacies
3 of the product. But also, at their age is it an appropriate
4 product? If it's an annuity with a 15-year surrender period
5 and this person is in their eighties, that's not likely to be
6 a suitable product. So suitability, as practiced by the
7 firms that do it really well, is an elastic concept that
8 really should capture both the competence and the age of the
9 individual investor. And I would just add to that good
10 firms, in fact, do have compliance systems that will
11 analyze -- particularly very risk transactions -- against an
12 investor's age so that, you know, certain kinds of options
13 strategies for a 65-year-old widow ought to create a red flag
14 immediately for the branch manager, in order to go and
15 investigate that particular transaction.

16 CHAIRMAN COX: Are there any cases where
17 suitability has been dichotomized in that way? Not only a
18 question of whether or not, given someone's chronological
19 age, this investment is appropriate, but completely
20 separately, this investor at this moment wasn't what he or
21 she used to be mentally?

22 MS. SCHAPIRO: Yes, absolutely.

23 CHAIRMAN COX: Good.

24 MS. SCHAPIRO: Can't recite them, off the top of my
25 head, given my chronological age, but there certainly are

1 some.

2 CHAIRMAN COX: Well, we are, I note, a quarter of
3 an hour past our promised conclusion. And as much as we have
4 reached an air gap here, I think I will take full advantage
5 and leap in. I want to conclude as I began, by thanking our
6 outstanding panelists, thanking the staff and the
7 commissioners for being here. I know some of you traveled a
8 good distance to be here; I very much appreciate it. The
9 collaborative effort that this represents, the cooperation
10 that it represents, I won't say is unprecedented. I am sure
11 that there have been such efforts in the past. But it is
12 certainly as high a level of mutual support and interest as
13 we could possibly expect to see among regulators at all
14 levels and outside groups. And so, this is a very, very good
15 moment, if not a watershed moment, in our focus on this
16 topic. Given the demographic comparative that we have
17 discussed, given what's going on in the market, given its
18 impact on the broader markets, I think this is a very
19 appropriate focus.

20 So, thank you very much for your contributions,
21 thank you for what you all do every day, and, most important,
22 thank you for what we will all do together today, and going
23 forward.

24 (Whereupon, at 12:14 p.m., the meeting was
25 adjourned.)

PROOFREADER'S CERTIFICATE

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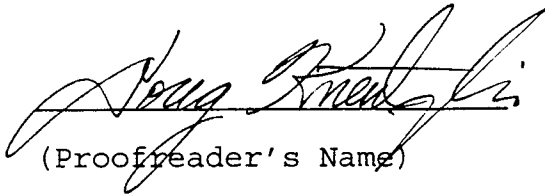
Seniors Summit Presentation

File Number: 4-522

Date: Monday, July 17, 2006

Location: Washington, D.C.

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