Investor Protection: Using Social Influence to Combat Investment Fraud


FINRA & FINRA Foundation

Financial Industry Regulatory Authority (FINRA)

 ► Largest independent regulator for all securities firms doing business in the United States
 ► Empowered by federal government
 ► Created through consolidation of NASD and NYSE Regulation
 ► Regulation, enforcement, education

FINRA Investor Education Foundation

 ► Awards grants and manages targeted projects focused on investor education and protection
Challenges to Preventing Investment Fraud

Psychological Barriers
► Illusion of invulnerability (I can’t be taken.)
► Reactance (You’re not the boss of me.)
► Threats to self-esteem (I am not stupid.)
► Too much information (I can’t remember what you taught me.)

Systemic Barriers
► Scams everywhere (how do you warn against so many different frauds?)
► Scale (how do you reach a critical mass of consumers?)
► Proving a negative (how do you show when something doesn’t happen?)
► Persistence (if you can show a preventative effect, does it last?)

How Big is the Problem?
Recent Major U.S. Cases:
► Nevin Shapiro – $880 million Ponzi scheme
► K. Wayne McLeod – $34 million Ponzi scheme
► Bernard Madoff – $50 billion Ponzi scheme
► Stanford Investments – $8 billion Ponzi scheme
► Greater Ministries – $500 million in losses – 18,000 victims
► Hundreds of cases with losses in the $10-$50 million range
Common Features of Scams

► Scams are creative and consistently changing
  – Disaster Relief
  – Green Energy
  – Oil & Gas
  – “China” Stocks
  – Bird Flu
  – Terrorism

► New distribution channels are constantly being created
  – Seminars
  – Email & Internet
  – Direct Mail
  – Word of Mouth
  – Telephone
  – Text Messages
  – Answering Machines

Moving Beyond Warning Campaigns

Investor alerts and warning campaigns have limited focus.

<table>
<thead>
<tr>
<th>Warning Campaigns</th>
<th>Educating Campaigns</th>
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<tbody>
<tr>
<td>Specific</td>
<td>Generic</td>
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<tr>
<td>Reactive</td>
<td>Proactive</td>
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<td>Short-term</td>
<td>Long-term</td>
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<tr>
<td>Information-based</td>
<td>Skills-based</td>
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Major Research


Methods of Solicitation

• Top Methods of Receiving Unsolicited Investment Offers
  – Free Seminars (68%)
  – Spam Email (64%)
  – Direct Mail (61%)
  – (Cold Calls are a distant 5th at 27%)

• While few seniors purchase investment products as a result of the free seminars, males (13%) are almost twice as likely as females (7%) to invest.
Who is Victimized?

- Victims of investment fraud have which of these characteristics?
  1) Female
  2) No college education
  3) Below average financial literacy
  4) Live alone
  5) None of the above

Who is Most Victimized?

Victim demographic trends:
- Male
- 55-65 years old
- More financially literate
- College-educated
- Self reliant
- Recent change in financial or health status
- Risk-takers
Key Risk Factors

► Own high-risk investments
► Relying on friends, family, co-workers for advice
► Open to new investment information
► Failing to check background and registration of financial professional and product
► Inability to spot persuasion used by fraudsters

Fraud Weapon – Social Influence

► Scam pitches are tailored to the “hot buttons” of targets
► An investment fraud pitch is full of influence

Average # Total Tactics per Transcript

Investor Protection Strategy

Teach investors to:
► Know that they are vulnerable
► Recognize persuasion techniques
► Take simple, highly protective steps
  – Ask questions
  – Check answers

Accepting Vulnerability – Risk Meter

Are you a high-risk candidate for fraud?
► 12 Simple Questions
► Research-based
► Identifies Areas of Concern for You
► Provides Detailed Explanations and Resources

www.SaveAndInvest.org/meters/risk
Persuasion Tactics

**Phantom Riches** – Dangling the prospect of wealth; something you want but can’t have.

![Assess the pitch.](image)

**Is the salesperson dangling incredible returns or guarantees?**
Persuasion Tactics

**Source Credibility** – It is better to deal with credible people or individuals in positions of authority.

![Credibility can be faked. Can the claims be independently verified?](image)

Professional Designations

![Understanding Professional Designations](image)
Social Consensus – If everybody wants it, it must be good.

Are YOU really interested in the investment? Does the pitch focus on how many others are interested?

Reciprocity – Doing a small favor in return for a big favor.

Was the pitch preceded by a free meal, book or video? Do you feel obliged to do the salesman a favor?
Scarcity

**Scarcity** – If something is rare or scarce, it must be more valuable.

Is the offer good for only a limited time or in limited quantity?

Videos are only available for viewing during the live presentation and within the Foundation’s documentary, *Trick$ of the Trade: Outsmarting Investment Fraud*. DVDs may be ordered for free at [www.SaveAndInvest.org/TricksoftheTrade](http://www.SaveAndInvest.org/TricksoftheTrade).
Preventing Fraud – Ask and Check

- Those who counter-argue and actively question a communication are less persuaded.
- Interviews of cons reveal that they do not like to be questioned.
- Ask and check the registration status of the professional and investment.
  - ASK if they are licensed to sell the investment and if the product is registered.
  - CHECK that they are licensed and the product is registered – SaveAndInvest.org or (888) 295-7422.
# Before You Invest, Ask and Check

### Where to Check

<table>
<thead>
<tr>
<th>Professional or Product Type</th>
<th>Check</th>
<th>URL and Phone</th>
</tr>
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<tbody>
<tr>
<td>Broker</td>
<td>FINRA BrokerCheck</td>
<td><a href="http://www.SaveAndInvest.org">www.SaveAndInvest.org</a> (888) 295-7422</td>
</tr>
<tr>
<td>Insurance Agent</td>
<td>State Insurance Regulators – check National Association of Insurance Commissioners (NAIC)</td>
<td><a href="http://www.naic.org">www.naic.org</a> (866) 470-6242</td>
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### Outsmarting Investment Fraud Curriculum

- **Outsmarting Investment Fraud**
  - Understanding Fraud **Risk**
  - Recognizing **Persuasion** Tactics used in Fraud
  - **Preventing** Investment Fraud
- Incorporates moderated presentation, videos, and learning activities & exercises
- Full version runs 60 minutes; adapted to range from 20-60 minutes in different settings with varying audio-visual capacity
- **Call to Action:** Deputizes participants to warn others
Curriculum Changed Behavior

Those who had been to the OIF seminar responded positively to the fraud appeal 50% less frequently than those who had not.

Percentage of Respondents who Agreed to Receive Information

- Experimental Group: 17.65%
- Control Group: 36.71%

Free Resources

► Documentary DVD
► Partner Toolkit
► Curriculum CD and Flip Charts
► Handouts
  – Fighting Fraud 101
  – Investor Kits
  – Playing Cards
NCVC National Conference
Using Social Influence to Combat Investment Fraud

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SaveAndInvest.org/FraudCenter

Financial Fraud Research Center

• Partnership with Stanford University Center on Longevity
• Serves as a hub in the fight against financial fraud
  – consolidates information
  – connects research to practice
  – catalyzes research and funding
• Online at www.fraudresearchcenter.org
Before You Invest, Ask and Check

SaveAndInvest.org

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