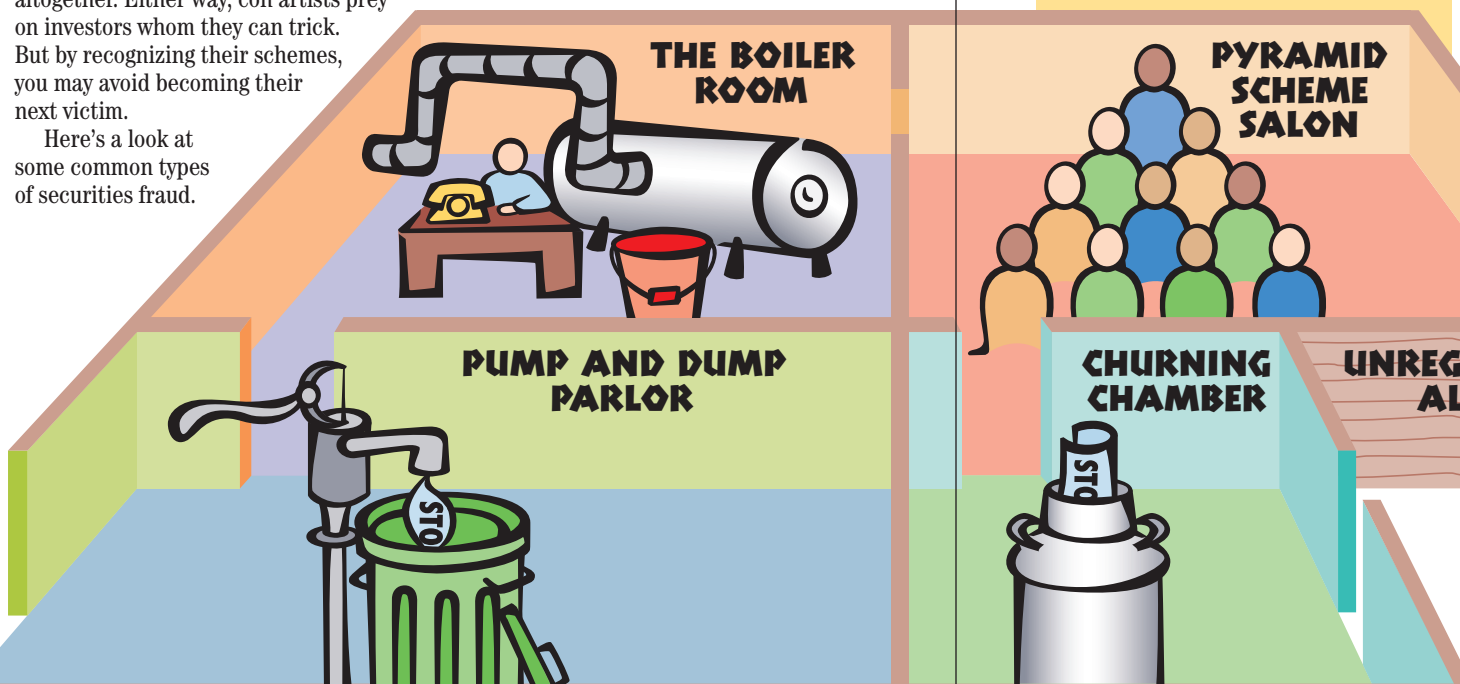


Recognizing Stock Scams

Illegal schemes lurk out there, but understanding how they work can help you spot and avoid them.

An investment scam might involve legitimate products, but the way they are sold might be illegal. Or a scam might be based on selling illegal investments altogether. Either way, con artists prey on investors whom they can trick. But by recognizing their schemes, you may avoid becoming their next victim.

Here's a look at some common types of securities fraud.



THE SCAM SHACK

- **Pump and dump** is a stock scam in which the scammer buys shares in low-priced stocks of small companies, known as penny stocks. He or she then spreads false information, often through a cold call or on the Internet, to pump up the price of these stocks. After investors caught up in the hoax buy shares, the scammer sells—or dumps—the stock at the highest price, and disappears with the profit, leaving other investors holding almost worthless shares. In an Internet chat room—where this scheme often takes place—you might identify a pump and dump scam by a surge of undocumented information on a particular penny stock, urging you to buy it. Steer clear of an investment if you hear about it only in chat rooms or in a phone call out-of-the-blue from a broker you have never talked to before.
- **Boiler rooms** and **bucket shops** are locations from which con artists launch

fraudulent stock scams or sell stocks illegally. The locations range from rented office space that might seem legitimate to private homes or even overseas sites.

Typically, boiler rooms feature rows of telephones used by cold callers. Cold callers phone potential victims randomly, using unscrupulous, high-pressure tactics and sometimes false information, to try to sell high-risk stocks or other investments.

A bucket shop, or illegal brokerage firm, may never buy the securities for you that you ordered. Rather, the con artists pocket your money, figuring that you won't notice the scheme right away. Then the entire operation disappears—sometimes literally overnight—before authorities can track down their whereabouts.

You should hang up if you receive an unsolicited phone call about an investment and the caller pressures

Pyramid schemes are another type of scam. A con artist recruits people who pay to participate in a supposed investment. To recoup their money, these new recruits are told to find more people, who in turn put in money. Each new recruit then is expected to recruit additional players. Be careful of any offering in which you have to not only put money up front but also find other investors.

- A **reload scam** takes place after you have been tricked on an investment and then told you can recoup your money by investing more money or rolling over your initial investment into a new investment. This way you're "reloaded" and set up for a second scam. You may be told you can get your funds back if you try again. Or for a fee, scammers may offer to file claims paperwork or give you a reimbursement they are holding for you. This is a fraud known as an advance fee scheme. If you have lost money to fraud, you can get legitimate government assistance by contacting your state securities regulator, which you can find from the North American Securities Administrators Association at www.nasaa.org.

you into making a decision on the spot. You should also hang up if you ask the caller for written information, and he or she refuses to provide it or evades questions.

You can avoid being scammed this way by never investing in anything over the phone without reading a prospectus first and understanding the risks of the investment. You should also know and feel comfortable with the person attempting to sell you the investment. One way to establish some level of comfort is to check out the person or firm with your state securities regulator to be sure they are properly registered or licensed.

- **Churning** is a type of fraud in which a stockbroker or investment adviser to whom you have granted control of your account buys and sells securities without explaining why so much trading is necessary. If you end up paying more in commissions than you earn on your investments because of your broker's frequent trading you might suspect your account is being churned. Fear of

churning is one reason to avoid turning control of your account over to a broker or investment adviser (known as giving them discretionary authority over your account). Always carefully review your monthly statements for illogical or overly frequent transactions.

- If a broker sells **unregistered securities**, he or she is not dealing in legitimate investment products. Investments must be registered at the state level before they can be sold, unless they are traded on a national stock exchange like the New York Stock Exchange, American Stock Exchange, certain regional exchanges, or the Nasdaq. Most unregistered securities promise low risk and high returns. Usually their promoters are the only ones who make any money. You can check the registration statement of a security by accessing a free database run by the Securities and Exchange Commission, at www.sec.gov/cgi-bin/srch-edgar. Don't invest in any securities unless they're properly registered or exempt from registration.