TESTIMONY OF JOSEPH P. BORG

Director, Alabama Securities Commission
and
President
North American Securities Administrators Association, Inc.

Before the
Special Committee on Aging
United States Senate

"Advising Seniors About Their Money: Who Is Qualified - and Who Is Not?"

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Chairman Kohl, Ranking Member Smith and Members of the Committee,

I'm Joe Borg, Director of the Alabama Securities Commission and President of the North American Securities Administrators Association, Inc. (NASAA).[1] I commend you for your Committee's ongoing investigation of investment fraud targeting our nation's seniors. State securities regulators share your outrage at the practices used by unscrupulous brokers and other predators who swindle seniors out of the hard-earned money they need for a secure retirement. State securities regulators are considered the first line of defense for investors, and it should come as no surprise that we have been at the forefront in detecting the problem of senior abuse and responding to it aggressively.

We believe the most effective weapon against fraud is: vigorous enforcement, investor education, and innovative regulation. The states have been active in all of these areas. For example, our enforcement data confirms the trend toward senior investment abuse and it also reflects the states' role in taking enforcement action against the perpetrators. According to our 2005 NASAA enforcement survey, 28 percent of all investor complaints submitted to state securities agencies came from seniors, 26 percent of all state enforcement actions involved the financial exploitation of seniors, and 34 percent of all cases of senior exploitation involved variable or equity index annuities. Preliminary results from our most recent survey show that the percentage of senior investor complaints has risen to 44 percent. Later I'll highlight some specific enforcement actions addressing senior abuse. These cases represent just a small sampling from the states' campaign against senior investment fraud.

NASAA and its members have also led the effort to educate the public about senior fraud. For example, in 2003, NASAA recognized the investor protection challenges raised by the growth in our senior population and announced the creation of the "Senior Investor Resource Center" on our website. One of our more recent initiatives is "The Alert Investor," a series of podcasts produced by NASAA to provide individuals with investor protection news and information. The fourth episode in our podcast series, "How to Talk to Your Parents about Senior Investment Fraud," was released this May in conjunction with National Older Americans Month.

In addition, NASAA members actively bring important investor protection and awareness information to seniors in each of our jurisdictions through workshops, forums, and other public events. We also partner with grassroots organizations, such as AARP, to help reach even more seniors. One successful example of this outreach partnership is the Senior Sleuth Checklist program, in which AARP volunteers attend "free lunch" seminars targeting seniors and report their findings to state securities regulators.

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[1] The oldest international organization devoted to investor protection, the North American Securities Administrators Association, Inc., was founded in 1919. Its membership consists of the securities administrators in the 50 states, the District of Columbia, Canada, Mexico, Puerto Rico and the U.S. Virgin Islands. NASAA is the voice of securities agencies responsible for grass-roots investor protection and efficient capital formation.

The states have been in the vanguard developing innovative regulatory responses that will help states crack down on senior fraud. For example, Massachusetts adopted a rule limiting the use of professional designations that state or imply a special expertise in senior financial affairs and money management. These designations are often used to gain trust and perpetrate fraud against seniors. NASAA is helping to address the problem of senior designations through a model rule that will serve as a useful rulemaking guide for all state securities regulators.

After a brief overview of state securities regulation, I'd like to focus on two specific types of senior abuse that we find especially troubling: "free lunch" seminars and misleading professional designations. On each of these fronts, the states are responding with all three of the important weapons I mentioned above: enforcement, education, and rulemaking.

State Securities Regulatory Overview

The securities administrators in your states are responsible for enforcing state securities laws, licensing firms and investment professionals, registering certain securities offerings, examining broker-dealers and investment advisers, and providing investor education to your constituents. Some of my colleagues are appointed by their Governors and Cabinet officials; ten are appointed by their Secretaries of State; five fall under the jurisdiction of the state Attorney General; and others, like my office, are independent commissions. But regardless of how they are organized, state securities regulators share a profound and common goal: to protect investors from fraud and abuse in the offer and sale of securities.

Like the securities administrators in your states, the Alabama Securities Commission devotes much of its resources to enforcement. State securities regulators bring civil actions, administrative proceedings, and even criminal prosecutions against the companies and individuals who exploit investors. Our goals are to halt violations through injunctions, punish violators through fines and criminal sanctions, and help make investors whole through restitution. We also protect the public by suspending or revoking the licenses of the firms and individuals who have violated the law.

Free Lunch/Dinner Seminars

Let me now turn to two of our efforts in the war on senior fraud. Most of us over the age of 50 have received a card in the mail inviting us to a "free lunch" or dinner investment seminar that we are told we can't afford to miss. As you can see from the poster, there are recurrent themes in these enticing ads: a free gourmet meal, tips on how to earn great returns while eliminating market risk, and a warm welcome to spouses of the invitees. Nothing will be sold, they proclaim, and there is NO cost or obligation. In reality, the high-pressure sales pitch usually comes in the form of a follow-up call a few days after the meal from a salesman with a title such as "senior specialist."

Our members are seeing a variety of violations associated with many of these events, ranging from outright lies and the conversion of investor funds to more sophisticated forms of abuse. Often, the salesman recommends liquidating securities positions and using the proceeds to purchase indexed or variable annuity products that the specialist offers. These products are often grossly unsuitable for senior citizens, and this is one way that the "free lunch" seminars can cause harm to investors. These recommendations also may constitute the dissemination of investment advice for compensation. If the salesman is not properly licensed, then he or she is offering investment advice as an unregistered investment adviser, which is yet another violation of state securities law.

Since 2003, when NASAA first identified the risk that seniors face at "free lunch" investment seminars, state securities regulators have been actively investigating and bringing cases to stop the spread of abusive sales practices that often emanate from these events. From steakhouses in Sun City, Arizona, to country clubs in Fredericksburg, Virginia, the retirement savings of seniors, as well as those nearing retirement, are being targeted by well-trained salesmen who, in too many cases, put their own personal interests ahead of those of their clients. As the following state enforcement actions demonstrate, there is no such thing as a "free lunch".

For example, in June, 2007, the Missouri Securities Division issued a Cease and Desist Order against an Ozark man for allegedly misleading senior investors and using their money for personal expenses, such as credit card and country club bills. The individual, who previously served time in federal prison for fraud, generated potential clients by conducting seminars targeting older investors. During the seminars he would discuss tax, investment, and insurance issues with the participants – but not important facts and risks about the investments he was offering or his felony fraud conviction. The state's investigation found that $1.3 million was transferred between accounts controlled by this individual over a two-year period, and only $12,000 remains.

In Utah, World Group Securities, a broker-dealer based in Duluth, Georgia, agreed to pay a $50,000 fine and strengthen its supervisory practices after two of its agents were found offering "free lunch" seminars for seniors and misrepresenting the credentials of one of the agents. An investigation by the Utah Division of Securities found that the two agents generated their senior clients through investment seminars, where inaccurate and misleading information was presented in an attempt to persuade the seniors to transfer their investment accounts to one of the agents. For example, one agent told seniors that due to his skills, one of his clients could now afford to take three vacations a year and had invited him and his family to join the client on vacation. In truth, the client with whom the agent vacationed was his father.

In Colorado, the state's Division of Securities and county law enforcement authorities won a securities fraud conviction and 20-year prison sentence of a conman who defrauded at least 25 people – older adults for the most part – of almost $600,000 in retirement savings. Between 1999 and December 2002, the fraudster solicited money primarily through "free lunch" seminars and presentations at retirement and senior centers in Colorado and New Mexico.

In California, the Department of Corporations charged an individual with fraudulently operating as an investment adviser after he made recommendations to some 40 clients, primarily seniors, who invested $15 million in mutual funds. This investment activity generated an average of at least $150,000 annually in commissions for the "adviser" who hosted seminars where seniors commonly received free lunches at country clubs, golf courses, and high-end restaurants. Not only did this individual lack a state license to operate as an investment adviser, but he also had a history of disciplinary actions by the NASD.

In addition to bringing individual state enforcement actions, NASAA and seven states joined forces with the SEC, as well as the NASD and NYSE Regulation (now consolidated as the Financial Industry Regulatory Authority or "FINRA"), in targeted examinations to detect abusive sales tactics aimed at seniors during "free lunch" seminars. A full report on these examinations will be released next week, but the preliminary findings confirm that seniors attending "free lunch" seminars are often subject to fraud, misrepresentations and other violations of the securities laws.

The Senior Designation Problem

State securities regulators continue to see another disturbing trend in the area of senior abuse. Increasingly, licensed securities professionals, insurance agents, and unregistered individuals are using impressive-sounding but sometimes highly misleading titles and professional designations. Many of these designations imply that whoever bears the title has a special expertise in addressing the financial needs of seniors.

While some of these designations reflect bona fide credentials in the field of advising seniors, many do not. These titles can serve as an easy way for an unscrupulous sales agent or adviser to gain a senior's trust, which is the first step in a successful fraud. Often these designations are used in conjunction with the "free lunch" seminars I discussed earlier. In other cases, they are highlighted in mass mailings, business cards, and other promotional materials.

It is exceedingly difficult for prospective investors – particularly senior citizens – to determine whether a particular designation represents a meaningful credential by the agent or simply an empty marketing device. Use of such professional designations by anyone who does not actually possess special training or expertise is likely to deceive investors.

Earlier this year, the NASAA Board of Directors created a task force to address the growing problem of what we call "senior designations." One of the first actions of the task force was to survey the NASAA membership to understand the nature and scope of the problem. We found that nearly half of the respondents had taken an enforcement action against individuals who had used a senior designation in a deceptive manner, and other members were investigating such allegations.

NASAA and its members are also responding to the problem of senior designations with regulatory solutions. One prominent example is Massachusetts, which recently issued a rule prohibiting the use of senior designations that have not been properly accredited by a recognized accrediting organization. I want to commend Massachusetts Secretary of the

Commonwealth Bill Galvin for his leadership in addressing the problem not only through effective enforcement but also through innovative rulemaking. In addition, Nebraska has issued a special notice addressing the use of designations and Washington State is soliciting comments on possible rule amendments aimed at the use of professional designations relating to senior citizens.

Recommendations

Notwithstanding the multi-front offensive launched by state and federal securities regulators, today's hearing is a testament to the fact that senior citizens remain a target for unscrupulous sales persons. What further action is necessary to punish and deter the wrongdoing?

As I mentioned earlier, the NASAA Task Force has been working on a model rule that would be suitable for adoption by every NASAA member confronting the misuse of senior designations. The model currently under consideration would attack the problem by making it a separate violation of law to use a designation or certification to mislead investors. Once the model rule has been released for public comment and ultimately approved by the NASAA membership, we will urge its adoption in every jurisdiction.

NASAA also believes that Congress should explore proposals to assist law enforcement and prosecutors to ensure that those who take advantage of our nation's elderly will be held accountable. Fraudulent investment sales to seniors will remain a problem of epidemic proportions as long as the benefits to the perpetrators outweigh the costs. Enhanced penalties for senior abuse – ranging from fines to jail terms – should help to raise those costs, deter law violations and punish appropriately those who exploit senior investors.

Conclusion

This Committee's examination of investment fraud against the growing senior population is an important step in highlighting a serious problem and working toward solutions. The financial victimization of seniors is simply intolerable, and the entire community of state securities regulators will continue to play an active role in protecting seniors through enforcement, education, and regulation.

I thank the Chairman and each member of this Committee for allowing me the opportunity to appear today. I look forward to answering any questions you have and providing additional assistance to you in the future.