

You Can Trade on This Advice

By

Robert C. Port, JD

Unless careful, an eager investor can fall prey to dishonest stockbrokers, advisors, financial planners and insurance agents claiming to have the best investment advice. An Atlanta attorney offers a tip sheet of some of the ways to help protect you and your clients from getting scammed.

- **Understand and Monitor Your Investments:** An investor's best defense is to be cautious, and to understand the reasons a broker is suggesting a certain investment. Ask questions. If the answers are not satisfactory, don't conclude that this is something too complicated for you. If you can't understand why your hard-earned money should be placed in an investment, you probably shouldn't invest.
- **Do Independent Research:** Companies traded on the public markets file numerous disclosures with the Securities and Exchange Commission, and these can be accessed for free at a number of sites, including www.freeedgar.com. [need to show as hyperlink] Internet sites such as www.morningstar.com and www.valueline.com provide independent analysis and rating of stocks and mutual funds. Many companies have their own Web sites, which often contain contact information for "Investor Relations." Mutual fund companies will be happy to send you a prospectus on the fund, which contains important information on fees and sales charges, as well as a description of the fund's investment approach.
- **Check Public Records on the Broker's Background:** A broker's employment history, records of customer complaints, state registrations, and other background information are public records. Be sure the broker is licensed to do business in your state. A broker's CRD (central registration depository) record can be obtained from the NASD at (800) 289-9999 or your state's securities division. This information is also available on the Internet at www.nasdr.com. Compare what the broker told you against what the CRD shows.
- **Do Interviews:** Talk to a number of brokers, preferably in person. Consider whether they are working for a firm whose name you recognize. Although large, well-known firms have their share of rogue brokers, the larger firms tend to have better supervisory controls in place to catch improper activity. Ask the broker about his prior work history. Has he been named in any customer complaints, arbitrations, regulatory investigations or disciplinary actions? If yes, ask for details.
- **Be Candid:** Disclose your complete financial condition, including your

income, net worth, debt, future obligations such as your children's college tuition, and other financial circumstances unique to you. Discuss your short- and long-term goals and investment objectives for your investments.

- **Carefully Review All Documents You Are Asked to Sign, and Get a Copy:** These documents should accurately reflect what the broker was told about your financial circumstances, and your investment goals. If the broker has listed your income higher than you said, or listed your investment objectives as "speculation" when you discussed the need for current income or preserving your capital, find another broker. Read and understand all of the fine print. The account opening agreements contain important provisions about how the account will be handled, your rights in the event of a dispute, and other matters. These are not "mere formalities" or "lawyer talk." Avoid any broker who tells you so or suggests you need not read or be concerned with what the documents say.
- **Understand How the Broker Gets Paid:** Brokers earn their living on commissions. Unfortunately, this creates an incentive for an unscrupulous broker to generate lots of transactions. A stockbroker who tells you he is not making money on a trade, or only makes money if you make money, is lying. Even if a stock transaction does not disclose a specific commission, a broker is making money on the "spread" (the difference between the price the broker buys the stock and the price it is sold to the customer).
- **Be Sensitive to the "Bait and Switch:** The initial recommendations of dishonest brokers may be for the purchase of well-known, widely traded blue chip stocks, or other securities consistent with your investment objectives. After you have invested in such companies, they will then suggest that such companies have little growth potential, and pressure you to sell the blue chip stocks and invest in small, unknown companies, which they claim will bring you spectacular profits.
- **Don't Be Pressured into Buying:** Buying stock is not a game where you have to act immediately or the opportunity is lost. If your instincts tell you that you are being pressure into something you are uncomfortable doing, don't do it.
- **Carefully and Promptly Review Statements and Other Papers:** Review each monthly statement and be sure it accurately reflects all the transactions you authorized. Sometimes a brokerage firm will send a "comfort letter," asking whether you are satisfied with the way your account has been handled. If you have a complaint, respond immediately. Do not ignore that letter. If your broker tells you that it is just "paperwork" and there is no need to respond, or that you should just sign-off that everything is OK, you should be very suspicious.
- **Carefully and Promptly Review Each Confirmation:** When a stock is bought or sold in your account, the brokerage firm sends you a "confirmation."

Review it to make sure it is accurate. Confirmations are required to be marked either "solicited," meaning that the broker recommended the investment, or "unsolicited," meaning that the purchase was the customer's idea. A confirmation you receive may inaccurately state that purchases recommended by the broker were "unsolicited." Errors sometimes occur, and a call to the broker may be all that is necessary to correct the inaccuracy. However, if this occurs repeatedly, or if the broker tries to tell you that it is not important what a confirmation says, this is a red flag that improper activity may be occurring in your account.

- **Promptly Object, and Seek Reversal of Unauthorized Transactions:** If you receive a confirmation for a purchase or sale you did not authorize, call the branch manager immediately and clearly state that you did not authorize the transaction and want it reversed. Follow up immediately with a letter. If you wait too long, you may be deemed to have "ratified" the transaction, even if you did not authorize it.
- **Payments Should Be Made by Check, Payable to the Brokerage Firm:** Never send or give cash directly to the broker. A request by the broker for cash, for a check made payable to him, or for a check made payable to a different brokerage firm is a red flag that improper or fraudulent activity may be occurring.

© 2002 Robert C. Port. Robert C. Port, JD, is a Partner in the Atlanta, GA office of Hassett Cohen Goldstein Port & Gottlieb, LLP, where he practices commercial litigation, including securities litigation and arbitration. He can be reached at rcport@mindspring.com.