NASAA ENFORCEMENT REPORT

2014 Report on 2013 Data

PREPARED BY:
NASAA ENFORCEMENT SECTION
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About NASAA's
Enforcement Section

NASAA's Enforcement Section tracks and addresses trends in securities fraud and dishonest/unethical behavior among securities professionals, and manages collaborative investigations by NASAA members. The Section acts as a point of contact for federal agencies such as the U.S. Securities & Exchange Commission, the Federal Bureau of Investigation, and the Department of Justice, as well as self-regulatory organizations.

The Enforcement Section oversees the activities of eight Project Groups, including: Enforcement Training, Enforcement Publications, Internet Fraud Investigations, Litigation Forum, Oil/Gas Ventures, Reg D Investigations, Securities Investigation Database and Enforcement Zones.

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Summary

The North American Securities Administrators Association (NASAA) conducts an annual survey of its U.S. members to gather enforcement data and identify trends in securities fraud, regulatory issues and investor protection. This year, 51 U.S. jurisdictions responded to the survey request, a response rate of 96 percent. The data, statistics and trends included in this summary give a general overview of state enforcement efforts for the 2013 fiscal or calendar year. This summary does not include enforcement statistics from every jurisdiction on each survey question posed, thus the numbers provided herein are necessarily conservative.

Highlights

- The survey revealed several important trends in investor protection and securities regulation, including continued reliance upon state regulators to provide front-line enforcement resources in protecting investors from risks created by **both traditional methods of securities fraud and those risks posed by emerging issues.**

- State securities regulators received **9,693 complaints** from aggrieved investors and conducted **5,302 investigations** in the 2013 reporting period.

- **Approximately 2,200 administrative, civil and criminal enforcement actions** involving more than 3,000 **respondents and defendants** were reported by the states.

- The states reported an increase in the sentences imposed in **criminal actions** resulting in **1,816 years of incarceration** and 679 years of probation.[1]

- States **imposed more than $616 million in investor restitution orders** and levied **fines or penalties and collected costs in excess of $75 million.**

Enforcement Statistics at a Glance	
Complaints Fielded by Regulators	9,693
Investigations	5,302
Enforcement Actions (administrative, civil, and criminal)	2,184
Investor Restitution Ordered	$616 million
Fines, Penalties, and Costs Assessed	$ 75 million
Jail Time Sentenced	1,816 years
Licenses Withdrawn, Denied, Revoked, Suspended or Conditioned:	3,657

Table 1: Enforcement Statistics at a Glance

Overview

The North American Securities Administrators Association (NASAA) conducted its annual enforcement survey beginning in March 2014. The survey traditionally gauges the extent and nature of enforcement efforts by state securities regulators, and identifies trends and issues in national investor protection.

51 NASAA members responded to this year's survey request. (Canadian members of NASAA participate in a different enforcement survey and an overview is summarized on page 12). This is a strong response and the numbers generated thereby are an effective portrayal of nationwide enforcement efforts. The data, statistics and trends included in this summary give a general overview of state enforcement efforts.

Each state records and classifies data in accordance with that state's practices; accordingly not all jurisdictions responding have provided input for all questions. The aggregation of the data, however, demonstrates the broad coverage that NASAA member jurisdictions provide in the United States in support of investor protection and in deterring future harm.

Methodology

As noted above, 51 U.S. jurisdictions provided responses for the 2014 Survey.[2]
The 2014 survey requested responses in:

- the number of complaints or inquiries received, and investigations and actions a state has conducted or initiated;
- information on penalties, payments, costs and restitution resulting from enforcement actions;
- the results from state securities regulators' efforts and assistance to prosecute criminal violations, including years sentenced and years of probation; and
- the type of actions brought, the most common products or practices at the core of these actions and the most common type of actors targeted by these efforts.

Key Findings

- State securities regulators continue to pursue and prosecute serious offenders. Activity and assistance in criminal prosecutions resulted in 1,816 years in prison sentences and an average incarceration term of 66 months.

- The state securities regulators continue to report unregistered securities and unregistered investment professionals as the most common problem they face.

- The increased use of the Internet for lawful offerings combined with the lifting of the ban on general solicitation has resulted in additional challenges in differentiating fraudulent and lawful offerings on the Internet.

- State regulators saw an increase in enforcement actions involving broker dealers' sales representatives.

- Regulators are seeing classic threats to investors morph into new or altered dangers fueled by the Internet, such as pyramid schemes (rapidly spreading multi-level marketed Ponzi schemes), new risk areas such as the cybersecurity breach of a digital currency site and the use of the Internet to facilitate the sale of stream-of-income investments and marijuana industry-related investments.

- The jurisdictions noted an increase in the denials and conditioning of licenses reflecting the regulators' continuing push to keep unqualified persons out of the industry or known problem applicants under heightened supervision.

Investigations, Actions, Investor Relief & License Activity

Investigations

In the 2013 reporting period, state securities regulators conducted 5,302 investigations. Based upon the 2014 survey question on this issue, these investigations are supplemented by the thousands of other efforts made to informally resolve complaints, referrals or other items in the enforcement area.

State securities regulators continued to partner with other law enforcement agencies and other securities regulators in 2013, reporting 746 outgoing referrals to sister agencies and 587 incoming referrals from those agencies.

Annual Investigations by State Securities Regulators	
Reporting Year	Number of Investigations
2013	5,302
2012	5,865
2011	6,121
2010	6,356
2009	6,565

Table 2: Annual Investigations

Enforcement Actions

Investigations conducted by state securities regulators led to nearly 2,200 enforcement actions reported by state securities regulators, including administrative, civil and criminal actions against 3006 respondents or defendants.

Annual Reported Enforcement Actions by State Securities Regulators				
Survey Year	Total	Administrative Actions	Civil Actions	Criminal Actions
2013	2,184	1,740	182	262
2012	2,496	1,925	232	339
2011	2,602	1,970	196	436
2010	3,475	2,018	324	1,133
2009	2,294	1,604	306	384

Table 3: Annual Enforcement Actions

Investor Relief & Measures of Accountability, Fines & Penalties

Investor relief and measures of accountability were at the center of these actions. The states levied fines or penalties of $71 million[3]. In addition and most important to investors, the states ordered over $616 million in investor restitution.[4] The states also recovered or collected $4 million in costs or expenses.

Investor Relief & Measures of Accountability			
Survey Year	Investor Restitution	Fines & Penalties	Costs Recovered
2013	$616 million	$ 71 million	$ 4 m
2012	$694 million	$115 million	$ 42m
2011	$2.2 billion	$126 million	$165m
2010	$14.1 billion	$171 million	$ 32m
2009	$4.7 billion	$245 million	n/a[5]

Table 4: Measures of Accountability

In addition to monetary sanctions, jurisdictions reported a strong level of specific and general deterrence by criminal sanctions. Collectively, individuals were sentenced to 1,816 years of incarceration through the efforts of state securities regulators, representing an increase of approximately 31 percent from 2012.[6] In addition, the average length of incarceration increased to 66 months from last year's average of 48 months, an increase of 53 percent.[7]

Years of Incarceration	
Survey Year	Years of Incarceration
2013	1,816
2012	1,134
2011	1,662
2010	1,134
2009	1,786

Table 5: Years of Incarceration

State regulators also took important action to deny unscrupulous actors from the licensed community and limit the activity of licensees. A total of 169 licenses were denied due to state action, a 36 percent increase in denials over last year. In addition 394 licenses were conditioned, a 48 percent increase over last year.

Licenses Withdrawn, Denied, Revoked, Suspended or Conditioned		
Survey Year	Licenses Withdrawn	Licenses Denied / Revoked / Suspended or Conditioned
2013	2,498	1159
2012	3,564	736
2011	2,796	774
2010	2,595	647
2009	3,353	531

Table 6: Licenses Withdrawn, Denied, Revoked, Suspended

Types of Cases

The survey also sheds light on the nature of those actions and the firms or individuals targeted in those actions.[8] The survey requested that states report the "type" of violation that triggered or was at the center of an action. In the relevant reporting period, 802 state enforcement cases involved fraud, traditionally marked by material misrepresentations, false statements or a scheme designed to defraud or deceive an investor, a sharp increase of 16 percent.[9]

While these fraud cases could, and in many instances did, involve registered brokers or investment advisers (or their agents or representatives), it appears that the majority of these fraud cases featured unregistered individuals selling unregistered securities. States reported 583 actions involving unregistered securities, and 667 actions involving unregistered firms or individuals.

The 2014 survey indicates that the states launched hundreds of investigations against registered members of the securities industry. The states reported 521 investigations into dishonest or unethical practices by securities licensees, 154 investigations involving books and records violations, 264 investigation involving suitability, and 177 investigations involving failure to supervise. Dozens of other investigations looked at cases of unauthorized trading, churning, and selling away.

The most common type of actor in or the subject of state securities enforcement actions were unregistered individuals. A total of reported actions involved 810 unregistered individuals and unregistered firms. Actions against licensed individuals and firms are broken down in the following table.

Actions by Type of Industry Participant	
Actor	Number of Reported Actions
Broker-Dealer Firms	219
Broker-Dealer Agents	357
Investment Adviser Firms	174
Investment Adviser Representatives	176
Insurance Firm or Agent	54

Table 7: Actions by Type of Industry Participant

Types of Products & Schemes

State securities regulators also reported the most common products that led to or were at the center of enforcement actions.[10]

Most Reported Products & Schemes 2013 *(In order of frequency reported by states)*
1. Ponzi Schemes
2. Real Estate Investments, including Promissory notes
3. Internet Fraud including, Social Media and Crowdfunding
4. Regulation D, Rule 506 offerings
5. Affinity Frauds
6. Oil and Gas offerings

Table 8: Most Reported Products

Senior Investor Protection

The survey also sought data on the type and nature of enforcement actions involving senior citizen investors. Of the 1,463 enforcement actions initiated by states that track victims by age in 2013, 311 involved abuse of senior citizens. As with many statistics throughout this report, this figure is conservative and the actual number of cases involving senior abuse is undoubtedly greater.

As in last year's survey results, unregistered securities, in the form of promissory notes, private offerings or investment contacts, were clearly the most common product involved in senior abuse cases, accounting for more than half of all reported senior-related enforcement actions and outnumbering the reported cases involving "traditional securities" by more than four to one.

Affinity fraud remains a continuing trend in the types of reported senior abuse cases. Variable annuities, viaticals or life settlement products, and free lunch investment seminars also appear as continuing problems for senior investors.

Enforcement Trends

In addition to requesting statistics on the number of actions related to a list of specified products or practices, administrators also were asked to identify the top five trends or developments most relevant in their state in terms of securities enforcement actions. This was posed as an open-ended, subjective question.

> ***Unregistered securities sold by unlicensed individuals continue to attract the most attention from state regulators. These fraudulent offerings are increasingly being marketed through the Internet.***

The key trend identified was that new 'products' (Digital currency, medical marijuana businesses and other topical industries) were being touted through schemes that used classic fraud techniques. In short, the name of the "next big thing" may change, but the tools used to harm investors remained the same. Continued high risks were unregistered sales, Ponzi schemes and Internet fraud, citing these new products. Binary Options and Stream-of-Income Investments, often reaching investors through the internet, may lack proper registration and licensing. For the first time, NASAA members identified six investigations where crowdfunding was used. This last development is of high concern, given state efforts to improve and support capital formation opportunities. Legitimate capital formation should not be compromised by unrelated fraudulent activity.

Canadian Securities Administrators Enforcement Report Summary

CSA's 2013 Enforcement Report

In early 2014, the Canadian Securities Administrators (CSA) released its 2013 Enforcement Report outlining how Canadian securities regulators actively are working to protect investors and the integrity of Canada's capital markets.

The CSA's 2013 Enforcement Report brings into focus the enforcement work done by CSA members against those who commit wrongdoing in Canada's capital markets. CSA members concluded cases against 382 individuals and companies. Concluded securities fraud cases involved 78 individuals and companies.

Highlights of the 2013 Enforcement Report

- 20% of the concluded cases were in the fraud category and involved 78 individuals and companies.

- 133 concluded cases involved a total of 216 individuals and 166 companies that resulted in:
    - Fines and administrative penalties of approximately $35.4 million.
    - Almost $55 million in restitution, compensation and disgorgement.
    - Jail sentences against eight individuals.

- Concluded matters against 156 respondents following contested hearings, 150 respondents by settlement agreements, and 76 respondents by court decisions.

- 112 matters commenced against a total of 160 individuals and 110 companies.

- Under the 35 interim orders and asset freeze orders issued, trading and other restrictions were placed on 38 individuals and 38 companies.

The full 2013 Enforcement Report is available from the CSA website www.securities-administrators.ca and from the websites of various CSA members. The CSA, the council of securities regulators of Canada's provinces and territories, co-ordinates and harmonizes regulation for the Canadian capital markets.

REFERENCE NOTES

[1] In 2013, member jurisdictions reported that defendants in criminal enforcement actions were ordered to serve 679 years of probation/probated sentences. In 2012, member jurisdictions reported that defendants in criminal enforcement actions were sentenced to serve 347 years of probation/probated sentences.

[2] The survey request asked each state administrator to provide statistics using that state's most recent full reporting year. Some states collect and report data on a calendar basis, while others collect data on a fiscal year basis. For the 2014 survey, 36 responding jurisdictions reported statistics from the 2013 calendar year; and 15 jurisdictions provided numbers from the 2012-2013 fiscal year.

[3] This figure does not include the multi-million dollar penalty amounts paid in the JP Morgan mortgage cases which were paid to five states.

[4] This figure probably understates the total amount of investor restitution ordered. Not all jurisdictions provided a restitution amount. This figure also does not account for unilateral and unreported returns to investors by firms or investigative targets.

[5] States were not asked to report costs recovered in the 2010 survey of 2009 activities.

[6] In 2013, member jurisdictions reported that defendants in criminal enforcement actions were sentenced to serve 1786 years in prison or jail. In 2012, member jurisdictions reported that defendants in criminal enforcement actions were sentenced to serve 1361 years in prison or jail.

[7] In 2013, member jurisdictions reported that each criminal defendant was ordered to serve an average term of 5.512 years (approximately 66 months) of incarceration. In 2012, member jurisdictions reported that each criminal defendant was ordered to serve an average term of 3.572 years (approximately 43 months) of incarceration. The average incarceration term is therefore a comparison of data, and does not necessarily mean that the defendants identified by member jurisdictions are the same defendants that received the sentences reported by member jurisdictions during the same period.

[8] Because state securities enforcement actions are complex and often involve multiple issues, a single case might involve several different types of actions or respondents. Therefore, cases reflected in the states' responses to the 2013 Survey often fit into, and thus were recorded, in more than one category or case type.

[9] Section 501 of the 2002 Uniform Securities Act, titled "General Fraud," states that it is unlawful, in connection with the offer, sale or purchase of a security, to employ a device, scheme or artifice to defraud; to make an untrue statement of material fact; to omit to state a material fact; or to engage in an act, practice or course of business that operates as a fraud or deceit upon another person.

[10] Thirteen of the states that responded to the 2014 Survey did not report any products or practice information.