

Telephone boiler rooms

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In Australia, it is illegal to sell investments, either over the phone or door to door or otherwise. This practice is called "hawking securities". This is not to be confused with securities dealers trying to sell their services, I am referring to someone actually phoning you up and trying to interest you in buying a particular issue.

This doesn't stop people from calling from overseas though, and a number of infamous brokers have set up international telemarketing divisions for selling parcels of stock or investment funds over the phone. There is a good movie about these brokers, Boiler Room, you should rent a copy if ever you are tempted to buy off a telemarketing broker.

Usually if it is a stock it will be some obscure penny stock from the United States or elsewhere. In the US all firms must regularly provide accounting statements to the Securities Exchange Commission (SEC is similar to our ASIC). All firms, that is, except for certain microcap companies that may be quoted on the Over-The-Counter (OTC) Bulletin Board operated by the National Association of Securities Dealers, in the Pink Sheets operated by the National Quotation Bureau, and on the NASDAQ Small Cap Market.

In these markets, independently researched information is very hard to come by and a small number of brokers control the market. The majority of these stocks never trade on an exchange where the general public has an opportunity to create even a semblance of a secondary market. Even when these stocks do appear on a public exchange, more than 80% of these often highly speculative entrepreneurial companies fail and their shares become worthless within 3 to 5 years.

Specialist brokers normally put up the money, taking a huge risk premium to provide venture capital for these new ventures, and then go about selling the newly-issued shares over the phone to members of the public that don't know any better. Usually the broker owns most of the shares, which are not listed on any exchange, and unless the venture actually makes a profit the stocks have no value other than what they quote over the phone.

Some brokers apply their own mark-up to shares over and above the price the firm paid for the stock. Although it is illegal for the broker to charge an excessive mark-up, in this shady industry it is not uncommon for the broker to mark up the price by 100% or more.

There is no market for these shares, other than the price they quote over the phone. If they get you on the phone over several weeks they will report a steadily rising price, and if you are like most people you will want to get in before you miss the boat.

Get this straight though, the reason why they are going up is because the brokers are telling you they are going up, not because of any genuine interest from traders. Once you have bought there is no guarantee at all that the broker will choose to continue quoting you a good price over the phone and no guarantee that they won't just collapse the price on you if you decide to sell. How do you sell? Well as there is no market the most you can do is just ask the nice man for your money back, see how well your stock does following that little bomb shell.

As long as they have you on the hook though, and provided that you don't indicate that you want a cheque back from them, they may well oblige you with enormous imaginary paper profits to keep your interest up. They may start on a program of churning your account, trading your portfolio from one imaginary stock to another while taking large commissions from each trade, you may be persuaded by this "success" to send them even more money, so you are put into more speculative issues owned by the brokers and his associates. Depending on how long they can play you out they may take additional amounts of money from you or simply swindle you out of your first cheque. The party will go on, with your continued imaginary success guaranteed only so long as you are willing to stay in the game.

If you want to know just how much profit you have really made, watch the "market developments" when you indicate your desire to get your money back. The stock will collapse or be suspended, the company will fail outright, your phone calls will be ignored or you will get lame excuses from some "customer service" associate telling you why it is taking so long to get the cheque out.