How to Avoid Fraud with Self-Directed IRAs

- **Avoid unsolicited investment offers** Be very careful when receiving an unsolicited investment offer for an alternative investment in a self-directed IRA, whatever the source. Ask yourself, "Why would I be chosen to receive information on a really great investment opportunity?"
- **Ask questions!** Is the person offering the investment licensed and is the investment registered? Ask questions and then contact the Office of Securities or the U.S. SEC to get unbiased answers before sending money or rolling over an IRA account.
- **Watch out for red flags such as "guaranteed" returns** Every investment carries some degree of risk. Alternative investments in self-directed IRAs, even if legitimate, may be extremely risky and inappropriate and unsuitable for many investors. A red flag of possible fraud is the promise of a guaranteed high return with little or no risk. Don't believe it!
- **Get professional advice** For complex alternative IRA investment opportunities, particularly those involving the opening of a new account outside of a traditional financial institution, brokerage or investment advisory firm, consider getting a second opinion from a licensed unbiased financial professional or attorney.

Who Can Help?

The **Maine Office of Securities** licenses broker-dealers and investment advisers and their representatives and agents in the state of Maine.

Always check *before* you invest-call us!

1-877-624-8551

www.investors.maine.gov

The Office of Securities is part of the **Maine Department of Professional and Financial Regulation,** which encourages sound ethical business practices through the regulation of insurers, financial institutions, creditors, investment providers and numerous professions and occupations.

www.http://www.maine.gov/pfr/

The Office of Securities is a member of the North American Securities Administrators Association: www.nasaa.org/

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A "Take Five" Guide

Self-Directed IRAs: What Every Investor Needs to Know

IRAs or Individual Retirement Accounts are a popular way to save for retirement

*Before you consider contributing to a **self-directed** IRA, read on!*

Take 5 minutes to get sound tips on keeping your finances fit

What are "self-directed" IRAs and how do they differ from traditional IRAs?

An IRA– or Individual Retirement Account– is a popular way for investors to save for retirement with certain tax benefits. There are a number of different kinds of IRAs, including the traditional IRA, Roth IRA, Simplified Employee Pension (SEP) IRA, and Savings Incentive Match Plan for Employees (SIMPLE) IRA.

A traditional IRA may contain mutual funds, stocks of publicly-traded companies, bonds and money market funds, and may be administered by a bank, credit union, stock brokerage firm or investment adviser firm.

A *self-directed* IRA may contain *many other types of investments,* including real estate and unregistered securities.

IRS rules provide a list of the types of assets that may be held in a self-directed IRA and require all IRAs to be held for the investor by a **trustee or custodian**. These may include banks, trust companies, credit unions, broker-dealers *and* other entities that are not regulated as securities firms.

Custodians and trustees of self-directed IRAs have certain duties with respect to tax reporting, but are generally not responsible for making sure your investments earn a profit, and will generally *not* evaluate the quality or legitimacy of an investment and its promoters. Because self-directed IRA custodian and trustee duties are limited to tax rules, fraudsters and speculative promoters often use a self-directed IRA to get access to funds in an IRA account.

How can fraud with Self-Directed IRAs occur?

A promoter of a Ponzi scheme or other fraudulent investment may seek to exploit self-directed IRAs because alternative investments such as unregistered securities or highly speculative investments are permitted under IRS rules.

The promoter/fraudster may misrepresent the duties and responsibilities of the self-directed IRA trustee or custodian, often claiming or implying that the trustee or custodian has evaluated or verified the underlying investment. The investor may mistakenly believe that because the self-directed IRA trustee or custodian is a separate entity, funds deposited into the self-directed IRA are not available to the promoter/fraudster. A self-directed IRA trustee or custodian generally has no duty to verify the value of an investment or protect the investor from fraud.

After the self-directed IRA funds are sent to the custodian or trustee, the promoter/fraudster withdraws the funds and replaces them with the fraudulent investment. The custodian or trustee continues to hold the "assets" provided by the promoter/fraudster, sending the investor regular account statements reporting the assets' value at the purchase price or at the value given by the promoter/fraudster.

Always...Check Before You Invest

IRS rules may discourage investors from reporting fraud promptly

An investor's loss due to a fraudulent investment can be complicated when a self-directed IRA is involved.

Self-directed IRAs, like other kinds of IRAs, are tax-deferred retirement accounts that carry a financial penalty for prematurely withdrawing money before a certain age. This penalty may induce self-directed IRA investors to keep funds in a fraudulent scheme longer than they would because of possible tax consequences.

The prospect of an early withdrawl penalty could cause an investor to become passive with a lesser degree of oversight than a managed account might receive, allowing a fraud promoter to perpetrate the fraud for a longer period of time.

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