Stanford Center on Longevity

A **LONGEVITY** BRIEF

FINANCIAL FRAUD

The Basics

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TAKE-HOME POINTS

- The direct cost of financial fraud is upwards of $50 billion a year.
- Fraud schemes are prevalent and diverse, and scams target consumers through many different channels including online, by telephone and by mail.
- There is no typical fraud victim profile: Different people fall for different types of scams.
- Often hard to identify, fraudsters use the same persuasion tactics used in the legitimate consumer marketplace to deceive their victims.
- Fraud schemes are complex crimes to investigate. Many perpetrators operate overseas and use various methods to transfer and hide the money they get from their victims.

INTRODUCTION

Fraud, scams, swindles and schemes—the con is one of the oldest games in the book. And while the players and their solicitation methods have evolved, most persuasion tactics have not. In fact, consumer financial fraud may be more common today thanks to advances in technology that make it easier for con artists to interact with thousands of unsuspecting marks at the same time through email and robodialing methods. The ever-increasing complexity of our financial markets also provide new opportunities for fraudsters to trick unwary consumers.

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This brief provides a breakdown of financial fraud, including popular types of scams, common methods of solicitation, the demographic and psychological profiles of victims and perpetrators, and the cost and consequences of fraud on victims and society.

WHAT IS FRAUD?

The Stanford Center on Longevity defines fraud as "Intentionally deceiving a target by misrepresenting, concealing or omitting facts about promised goods, services or other benefits and consequences that are nonexistent, unnecessary, never intended to be provided or deliberately distorted for the purpose of monetary gain."[1] Schemes are purposely designed to benefit the perpetrator at the victim's expense.

HOW COMMON IS FRAUD?

More than 1.2 million fraud complaints were made to law enforcement and federal agencies in 2015, and over half of these consumers reported losing money,[2] yet fraud is notoriously hard to measure because of under-recognition and under-reporting by victims.[3] The Federal Trade Commission (FTC) published a prevalence study in 2013 that found that in 2011, 10.8 percent of American adults were defrauded.[4] As depicted in Figure 1, the most common scams were bogus weight-loss products, products paid for but never received, unauthorized billing and bogus prize promotions.

In 2016, the Stanford Center on Longevity piloted an online survey and found that 37 percent of respondents lost money in a scam, such as bogus consumer products and services, investment fraud, phantom debt collection and multilevel marketing schemes, in the past year.[5]

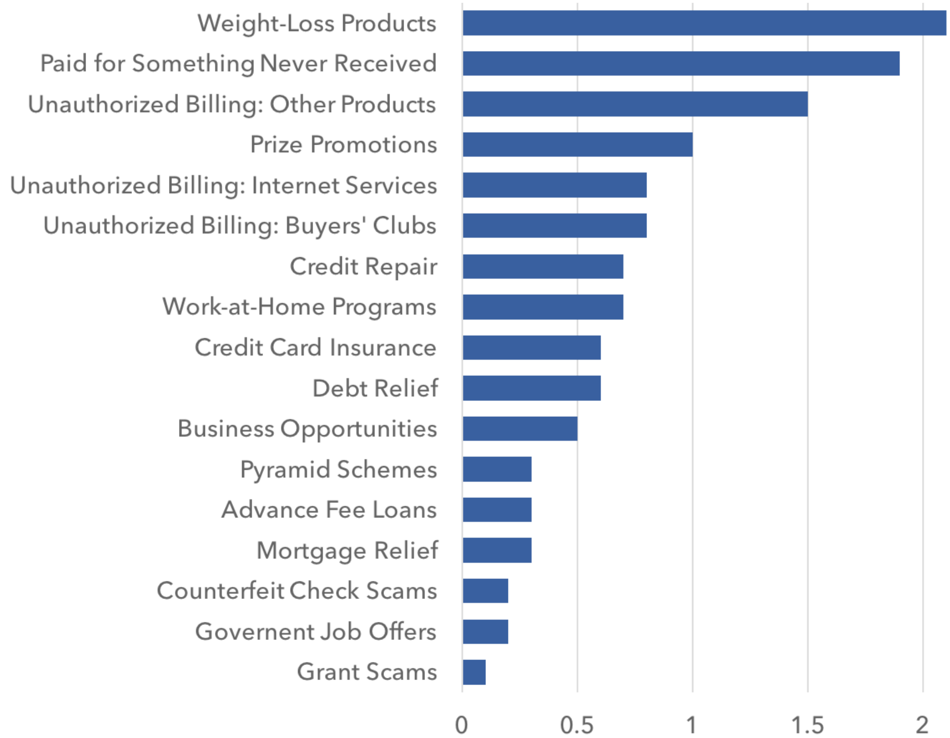


FIGURE 1 Estimated percentage of Americans experiencing fraud types
Source: Consumer Fraud in the United States, 2011: The Third FTC Survey (Anderson, 2013)

HOW DOES FRAUD WORK?

Con artists rely on the same marketing tools, persuasion tactics and money transfer mechanisms used in legitimate commerce. This makes it particularly difficult to spot a scam. An analysis of undercover tape recordings of interactions between scam artists and their marks revealed that fraudsters employed influence strategies like phantom fixation, social consensus, scarcity, friendliness, appeals to fear, threats, source credibility and assertions of authority (Figure 2).[6] Which tactics are used tends to differ based on the social and emotional profile of the target.[7]

Perpetrators also use everyday communication channels to solicit victims. As shown in Figure 3, in cases reported

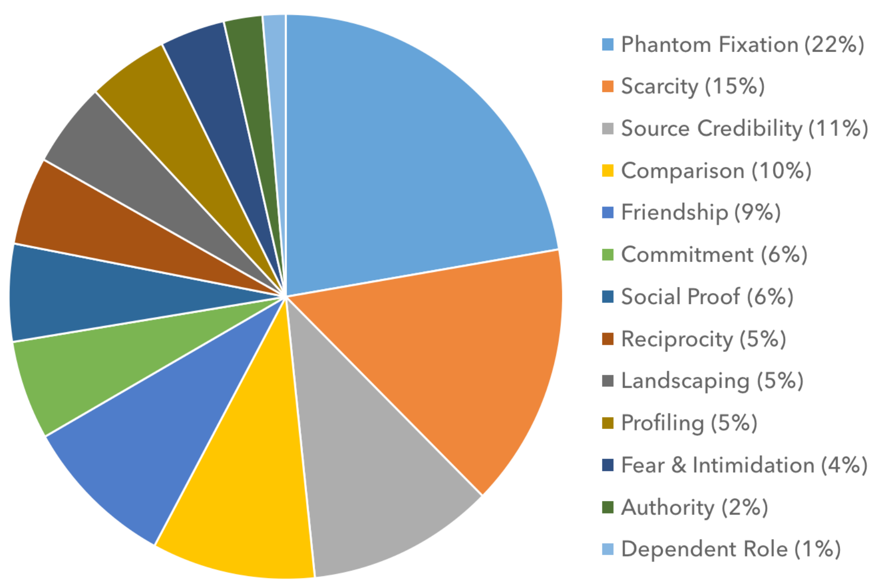


FIGURE 2 Persuasion tactics used by fraudulent telemarketers to influence their marks
Source: Shadel & Pak, 2007, pg. 7. Adapted with permission.

to consumer complaint agencies such as the Federal Trade Commission and Better Business Bureau, the majority of victims report that fraudulent companies contacted them by phone, followed by e-mail and the Internet.[2] Victims are asked to pay using a variety of different transfer mechanisms. Popular methods today are wire transfers and prepaid cards because it's hard for law enforcement to track the funds and nearly impossible to reverse a completed transaction.

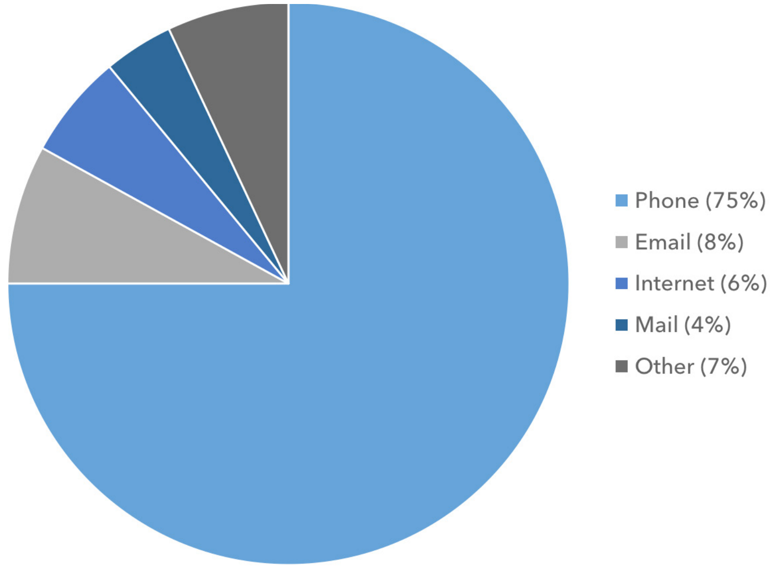


FIGURE 3 Methods fraudsters use to find potential marks
Source: Consumer Sentinel Network Data Book for January – December 2015

WHO ARE THE VICTIMS?

It turns out that we all are potential victims. A popular assumption is that older people are more likely to be fraud victims, but prevalence estimates tell a different story. According to the FTC, adults between the ages of 45 and 54 experience the highest rates of fraud,[4] and Stanford's online prevalence study found that the average age of fraud victims was just 41 years old.[5]

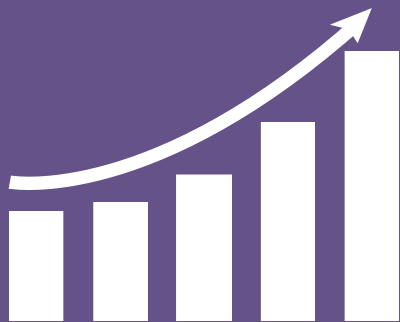
On the other hand, studies that examine particular types of fraud—such as investment fraud and bogus lotteries—have found that most victims are older. So what explains these discrepant findings? For one thing, general surveys rely on self-reports, whereas studies that look at particular scam types often use data sets of known victims that were obtained from fraud investigations. Many of the self-reported victims never reported fraud to authorities. Younger individuals are more likely than older people to acknowledge victimization,[7] which may skew the self-reported fraud victimization data used in the general surveys toward younger ages.

Another explanation is that different scams target different types of people. Demographic groups are differentially exposed to offers because of assumptions about what they care about and how they behave.[3] For example, young people fall for online marketplace scams more often than older individuals because younger people frequently use those sites to buy and sell products. On the other hand, older people more often lose money to bogus lottery scams because fraudsters use telemarketing and mail advertisements, which are communication channels more commonly used by older people. Risk of victimization by gender, race, income and education also vary by scam type.

Aside from demographic characteristics, certain behaviors and personality profiles can put people at greater risk of fraud victimization. These include risk taking,[8] extreme religiosity,[6] increased interest in listening to sales pitches[7] and low self-control/impulsivity.[9] Negative life events also increase susceptibility.[7]

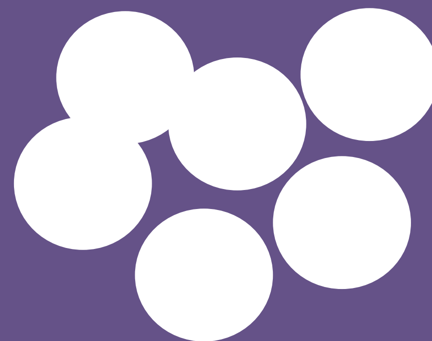
DIFFERENT FRAUD TYPES TARGET DIFFERENT VICTIMS.

Compared to the general public, victims of these fraud types are most likely to be:



INVESTMENT FRAUD

male
wealthy
risk-takers
interested in persuasive statements
open to sales situations
more educated



LOTTERY SCAMS

female
older
single
lower income
interested in persuasive statements
open to sales situations
less educated

Source: AARP Foundation National Fraud Victim Study, 2011. http://assets.aarp.org/rgcenter/econ/fraud-victims-11.pdf

WHO ARE THE PERPETRATORS?

Most of what we know about fraudsters is anecdotal. In the past, the masterminds behind telemarketing scams were largely white, middle-class, young- to middle-aged men.[10] They weren't like typical street criminals; rather, the typical fraudster had an erratic job history and, if anything, a minimal criminal background. Many were young men who were dissatisfied with mainstream occupations and had turned to white-collar crime to achieve more money and power, and the opportunity to live lavishly.

Now that people in West Africa and South American countries have greater access to the internet, the classic profile of a scam artist is changing. Today, perpetrators tend to be enterprising young men who've discovered that tricking Westerners is more lucrative than many of the other employment opportunities in their home countries. And because of the ease and affordability of outsourcing crime online, fraudsters can purchase contact information of thousands of U.S. and European targets, and even pay skilled programmers to develop malware to infect our devices.[11] However, there are still fraudsters who work domestically, often targeting individuals in person to convince them to invest or buy their service.

WHY SHOULD WE CARE?

Fraud exacts a tremendous financial and emotional toll on both victims and society. Losses can amount to as little as $1 or as much as millions of dollars per victim depending on the type of scheme and the wealth of the target. The estimated annual cost of fraud in the U.S. is $50 billion,[3] yet only $765 million in direct losses w reported to complaint agencies in 2015.[2]

In 2015, the FINRA Investor Education Foundation surveyed fraud victims and found that in addition to the financial toll, 65 percent of victims experienced non-financial ramifications, such as severe stress, difficulty sleeping and depression, as a direct result of the incident.[12] These emotional consequences were even more common than the indirect financial costs like late fees, bounced check fees, legal fees and health-related expenses that resulted from the fraud victimization. Fraud also puts a strain on law enforcement agencies, which are often poorly equipped and not trained to investigate complex financial crimes that span international boundaries.

As a society, we must approach all marketing and sales solicitations with a healthy dose of skepticism. If it's too good to be true, it probably is. Avoiding fraud means recognizing that we are all potential victims and developing strategies for staying one step ahead of scam artists.

CITATIONS

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The mission of the Stanford Center on Longevity is to redesign long life. The Center studies the nature and development of the human life span, looking for innovative ways to use science and technology to solve the problems of people over 50 in order to improve the well-being of people of all ages.

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