Green Energy Investment Scams: Do Your Due Diligence

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Last month, the Securities & Exchange Commission ("SEC") took action against a group of boiler-room operators for running a fraudulent green energy scheme that bilked investors out of nearly $11 million. According to the SEC, the owners of Kensington Resources, Inc., two men from Southern California, 51-year old Joseph R. Porche, and 53-year old Larry R. Crowder, were behind the boiler-room operation. The scheme involved the purported sale of $11 million in unregistered shares of American Environmental Energy, Inc. ("AEEI") common stock to unsuspecting investors. Porche, Crowder and their boiler-room sales staff of four led investors to believe that the majority of investment funds were to be used by AEEI to conduct its green energy business. However, according to the SEC, the vast majority of the monies raised simply went to pay sales commissions and to finance the lavish lifestyles of Messrs. Porche and Crowder. At the end of the day, only $335,000 of the $11 million raised went to AEEI. It turns out that Crowder, and one of the boiler-room salesmen, Dale J. Engelhardt, have previous securities law offenses. In 1998, as a result of a similar fraud, Crowder was permanently barred from associating with any broker or dealer, among other censures.

With the government's interest in promoting so called "green energy" – renewable and clean energy solutions – to support US energy demands, large public and private investments are flowing into a wide variety of startups, established companies, joint ventures and other programs to promote the sector. Sadly, the allure of green energy investments has also attracted the attention of fraudsters seeking to make a quick buck. Savvy investors would do well to do their due diligence on these opportunities in order to minimize the risk of fraud and other scams. Consider the following additional recent cases in the news:

> In August 2010, Dorothy Geisler-Tragardh, a principal of Praxis Resources, purportedly a "clean coal" supplier, pleaded guilty to defrauding investors out of as much as $2.5 million in a fraudulent sale of its stock. Geisler-Tragardh sold shares of Praxis to investors for $56 a share when they were worth only 30 cents apiece. Instead of investing the funds, she used the proceeds to enrich herself and to pay for a luxury waterfront home and a Picasso artwork.
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> In June 2010, the SEC halted trading in shares of Green Energy Resources, Inc. as a result of its dubious claim that it would be providing 100,000 tons of "very buoyant and very absorbent" woodchips for the cleanup efforts on the Gulf Oil Spill. The SEC had also ceased trading in another company, ACT Clean Technologies, after it had made dubious claims in press releases about landing clean-up contracts.

In March 2010 *Reuters* reported that investors in Australia had been defrauded out of at least US$3.2 million by a company called WesternField Holdings Inc., purportedly a Tokyo-based "leading developer of high quality greenhouse gas reduction projects" and a carbon offset investment firm. Investors were apparently the victims of an aggressive telemarketing scam. However, claims made on the company's web site were found to be phony, such as credentials, background, associations, certifications and awards it claimed but, in fact, did not have. Even its address in Tokyo appears to have been made up. The Australian Securities and Investments Commission took action and blacklisted the company.

In January 2010 notorious Canadian stock promoter, Stephen Demers, was found guilty of dozens of new fraud charges for the fraudulent sale of unregistered securities of United Environmental Energy, purportedly a green energy company. Demers had previously been found guilty of 435 securities violations in the prior five year period, according to *The Montreal Gazette*.

In November 2009, the SEC accused several individuals, including the principals of Pennsylvania-based Mantria Corp., of multiple counts of investor fraud, alleging they had perpetrated a Ponzi-type scheme which bilked mostly elderly investors out of as much as $30 million. Mantria was purportedly the "world's leading manufacturer and distributor" of biochar, allegedly a clean charcoal energy source, as well as the developer of a "carbon negative" housing community in rural Tennessee. In fact, these claims made to investors were a complete fraud – Mantria sold no biochar, nor had it developed an eco-friendly residential community. Biochar turns out to be an unproven and potentially controversial clean energy source.

These cases and others underscore the need for proactive and thorough due diligence when considering such investments. Indeed, in December 2009, the Financial Industry Regulatory Authority ("FINRA") issued a warning to investors about possible green energy investment scams, such as "pump and dump" and Ponzi-type schemes as noted above. FINRA provided advice to potential investors about how to avoid being scammed, including watching out for the following:

- Unsolicited communication such as faxes, emails, text messages tweets, and strategically placed "opinions" in blogs and message boards, usually related to a very low-priced stock.
- Seminars and webinars that use short-term incentives and bonuses, along with aggressive sales tactics, to encourage you to liquidate your current savings and go "all in" on a new investment initiative.
- Price targets or predictions of swift and exponential growth.
- The use of facts from respected news sources to bolster claims of the size of the market for a new product or technology ("this is a billion dollar market…").
- Mention of associations with or actions by federal and international governments that bolster a company's product or service ("The President wants hydrogen to be part of the solution for Detroit…").

- References to actions by well-known companies used to justify growth of the company being touted. When a large oil company launched a "nitrogen-enriched" gas, this was quickly seized upon to validate the business prospects of a touted company, even though there was no direct link between the two.
- Claims that they're the next big thing. Companies that, despite having not produced any revenue to date, are purported to have a new technology that will allow it to dominate the energy marketplace. ("Company XYZ will be the Exxon of the 21st century…")
- Products that are only in the development stages or that claim "working prototypes" but have no actual products on the market.
- Unverifiable claims of enormous energy efficiency.
- Pressure to invest immediately.

FINRA advised using a healthy dose of skepticism to check out these opportunities and the people pitching them. At Marquet International, we have a simple three step process: verify, verify and verify. As can be seen in some of the examples, there were clear and in some cases glaring warning signs, such as prior history of investment fraud, opulent lifestyles of promoters, unregistered securities and non-existent offices. We recommend taking the following actions as well:

- Check out the *bonafides* of the principals involved in the company in question – some may have prior histories of fraud, criminal activities or checkered backgrounds that may call into question the overall validity of the investment;
- Double check the science – some green energy technologies remain unproven or overblown – make sure it is real and practical;
- Talk to industry experts – get a real-time read on their reputation and track record. Other useful reference sources include other investors, suppliers, vendors and joint-venture partners;
- Be sure company financials are audited and provided by a legitimate accounting firm – we have seen cases where fraudulent investment schemes are supported by phony or disreputable accountants;
- Check to make sure the company and its executives are not the subject of regulatory actions – a prior history of regulatory censures is the best predictor of future actions and should raise red flags for the potential investor; and
- Look for related party transactions and relationships – fraudulent or unsound investment schemes often involve interrelated entities.

International investments are harder to check out given the relative lack of public record, differing accounting standards and less relative regulatory oversight. Be wary of intermediaries – we have found these individuals are often disreputable who may muddy a potential investment that would otherwise be sound. Thorough due diligence in these cases often may rest on developing human intelligence sources who can provide an accurate operational and reputational analysis.

In sum, as these cases illustrate, a careful analysis of potential green energy investments will go a long way toward keeping your greenbacks working for you instead of being scammed.

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