Managing Investment Risk

I. Introduction

When it comes to risk, here's a reality check: All investments carry some degree of risk. Stocks, bonds, mutual funds and exchange-traded funds can lose value, even all their value, if market conditions sour. Even conservative, insured investments, such as certificates of deposit (CDs) issued by a bank or credit union, come with inflation risk. They may not earn enough over time to keep pace with the increasing cost of living.

While you cannot eliminate investment risk, you can exert some control over what happens to the money you invest by understanding the different types of risks involved in investing and using basic investment strategies to help manage these risks and offset potential problems.

2. Why Take Risks?

The question you might have at this point is, “Why would I want to risk losing some or all of my money?” It’s a fair question. In fact, there may be times when you know it isn’t a good idea to put money at risk. This can happen when you plan to use the money in the short term—to make the down payment on a home, to pay a tuition bill for next semester or to cover emergency expenses—or if you cannot afford to lose the money in the long term.

But by exposing some of your money to risk, you likewise open the door to potentially greater returns, including the potential to earn dividends or interest on your investments. In addition, the value of the assets you purchase may increase over the longer term.

For many people, it’s best to manage risk by building a diversified portfolio that holds several different types of investments. This approach provides the reasonable expectation that at least some of the investments will increase in value over a period of time, outpacing returns from risk-free insured bank savings like a savings account.

3. Types of Investment Risk

There are many different types of investment risk, and in this section we'll discuss some of the most common ways your individual investment or portfolio can either lose money or lose buying power.

Systematic and Nonsystematic Risk

Most investment risk is described as either systematic or nonsystematic. While those terms seem intimidating, what they refer to is actually straightforward.

Systematic risk is also known as market risk, and relates to factors that affect the overall economy or securities markets. Systematic risk affects all companies, regardless of the company's financial condition, management or capital structure, and, depending on the investment, can involve international as well as domestic factors. Here are some of the most common systematic risks:

- **Interest-rate risk** describes the risk that the value of a security will go down because of changes in interest rates. For example, when interest rates overall increase, bond issuers must offer higher coupon rates on new bonds in order to attract investors. The consequence is that the prices of existing bonds drop because investors prefer the newer bonds paying the higher rate.

- **Inflation risk** describes the risk that increases in the prices of goods and services, and therefore the cost of living, can reduce your purchasing power. Let's say a can of soda increases from $1 to $2. In the past, $2 would have bought two cans of soda, but now $2 can buy only one can. In terms we're all familiar with, your money doesn't go as far as it used to.

Inflation risk and interest rate risk are closely tied, as interest rates generally rise with inflation. Because of this, depending on the type of investment you hold, inflation can also reduce the value of certain investments. For example, to keep pace with inflation and compensate for the loss of purchasing power, lenders will demand increased interest rates. For bond investors, this can lead to existing bonds losing value because, as mentioned above, newly issued bonds will offer higher interest rates. Inflation can go in cycles, however. When interest rates are low, new bonds will likely offer lower interest rates.

- **Currency risk** occurs because many world currencies float against each other. That means if money needs to be converted to a different currency to make an investment, any change in the exchange rate between that currency and yours can increase or reduce your investment return. You are usually only impacted by currency risk if you invest in international securities or funds that invest in international securities.

As with most types of investment risk, currency risk can be managed by allocating only a limited portion of your portfolio to international investments and diversifying this portion across various countries and regions.

- **Liquidity risk** is the risk that you might not be able to buy or sell investments quickly for a price that is close to the true underlying value of the asset. Sometimes you may not be able to sell the investment at all if there are no buyers for it. Liquidity risk is usually higher in over-the-counter (OTC) markets and small-capitalization stocks. Liquidity can also be a factor in securities like non-traded REITs, which invest in real estate and may put restrictions on an investor's ability to sell some or any of the investment until approved by the REIT company that issued the shares. Foreign investments can pose liquidity risks as well. The size of foreign markets, the number of companies listed and hours of trading may limit your ability to buy or sell a foreign investment.

- **Sociopolitical risk** is the possibility that instability or unrest in one or more regions of the world will affect investment markets. New leadership, a change in national policy, terrorist attacks, war and pandemics are examples of events, whether actual or anticipated, that impact investor attitudes toward the market in general and result in system-wide fluctuations in stock prices. International-focused investments such as emerging market funds might be particularly impacted by sociopolitical risk.

Nonsystematic risk affects a much smaller number of companies or investments than systematic risk and is associated with investing in a particular product, company or industry sector.

Here are some examples of nonsystematic risk:

- **Management risk**, also known as company risk, refers to the impact that bad management decisions, other internal missteps or even external situations can have on a company's performance and, as a consequence, on the value of investments in that company. Even if you research a company carefully before investing and it appears to have solid management, there is typically no way to know in advance that a competitor is about to bring a superior product to market. Nor is it easy to anticipate a financial or personnel scandal that undermines a company's image, its stock price or the rating of its bonds.

- **Credit risk**, also called default risk, is the possibility that a bond issuer won't pay interest as scheduled or repay the principal at maturity. Credit risk may also be a problem with insurance companies that sell annuity contracts, where your ability to collect the interest and income you expect is dependent on the claims-paying ability of the issuer.

We discuss ways to help manage these and other risks in Section 5 below.

The Risk of Investment Fraud

Investment fraud is real, and the risk that you could lose some or all the money you have saved and invested in an instant can, and unfortunately does, happen.

You can minimize the risk of losing money to a fraudster or scam by performing two very important actions:

Check Out Investment Professionals. Always ask whether the promoter of an investment opportunity is licensed to sell you the investment—and confirm which regulator issued that license, and if and when the license has ever been revoked or suspended. A legitimate securities salesperson must be properly licensed, and his or her firm must be registered with FINRA, the SEC or a state securities regulator—depending on the type of business the firm conducts. An insurance agent must be licensed by the state insurance commissioner where he or she does business.

Independently verify the salesperson's or promoter's answers as follows:

- For a broker or brokerage firm, use FINRA BrokerCheck at *www.finra.org/brokercheck* or call toll-free: (800) 289-9999. BrokerCheck allows you to confirm not only licensing and registration, but also whether an individual or firm has a history of complaints or regulatory problems.
- For an investment adviser, use the SEC's Investment Adviser Public Disclosure website at *www.adviserinfo.sec.gov* or call toll-free: (800) SEC-0330.
- For an insurance agent, check with your state insurance department. You will find contact information through the National Association of Insurance Commissioners (NAIC) at *www.naic.org* or call toll-free: (866) 470-NAIC. For all sellers, be sure to call your state securities regulator. You can find that number in the government section of your local phone book or by contacting the North American Securities Administrators Association at *www.nasaa.org* or (202) 737-0900 for the state's number.

Check Out Investments. Ask whether the investment is registered and, if so, with which regulator. Most investors will want to buy securities products that are registered with the SEC or with state regulators. With very few exceptions, companies must register their securities before they can sell shares to the public. You can find out whether a product is registered with the SEC by using the EDGAR database (*www.sec.gov/edgar.shtml)*.

Other Investment Risks

Sometimes investment risk comes not from external factors we can't totally control, but from our own decision-making. The investment decisions you make—and sometimes those you avoid making—can expose you to certain risks that can impede your progress toward meeting your investment goals.

For example, buying and selling investments in your accounts too frequently, perhaps in an attempt to take advantage of short-term gains or avoid short-term losses, can increase your trading costs. The money you spend on trading, paying commissions and other fees, reduces the balance in your account or eats into the amount you have to invest. If you decide to invest in something that's receiving a lot of media attention, you may be increasing the possibility that you're buying at the market peak, setting yourself up for future losses. Or, if you sell in a sudden market downturn, it can mean not only locking in your losses but also missing out on future gains.

You can also increase your investment risk if you don't monitor the performance of your portfolio and make appropriate changes. For example, you should be aware of investments that have failed to live up to your expectations, and shed them when you determine that they are unlikely to improve, using the money from that sale for another investment.

Time, specifically the timeframe in which you might need the money you have invested, also affects risk, and with it investment selection.

Based on historical data, holding a broad portfolio of stocks over an extended period of time (for instance a large-cap portfolio like the S&P 500 over a 20-year period) significantly reduces your chances of losing your principal. However, the historical data should not mislead investors into thinking that there is no risk in investing in stocks over a long period of time.

For example, suppose an investor invests $10,000 in a broadly diversified stock portfolio and 19 years later sees that portfolio grow to $20,000. The following year, the investor's portfolio loses 20 percent of its value, or $4,000, during a market downturn. As a result, at the end of the 20-year period, the investor ends up with a $16,000 portfolio, rather than the $20,000 portfolio she held after 19 years. Money was made—but not as much as if shares were sold the previous year. That's why stocks are always risky investments, even over the long-term. They don't get safer the longer you hold them.

This is not a hypothetical risk. If you had planned to retire in the 2008 to 2009 timeframe—when stock prices dropped by 57 percent—and had the bulk of your retirement savings in stocks or stock mutual funds, you might have had to reconsider your retirement plan.

4. Assessing Risk

It's one thing to know that there are risks in investing. But how do you figure out ahead of time what those risks might be, which ones you are willing to take and which ones may never be worth taking? There are three basic steps to assessing risk:

- Understanding the risk posed by certain categories of investments
- Determining the kind of risk you are comfortable taking
- Evaluating specific investments

You can follow this path on your own or with the help of one or more investment professionals, including broker-dealers and registered investment advisers with expertise in these areas.

Step 1: Determining the Risk of an Asset Class

The first step in assessing investment risk is to understand the types of risk a particular category or group of investments—called an asset class—might expose you to. For example, stock, bonds and cash are considered separate asset classes because each of them puts your money to work in different ways. As a result, each asset class poses particular risks that may not be characteristic of the other classes. If you understand what those risks are, you can generally take steps to offset those risks.

Stock. Because shares of equity securities, often referred to as stock, don't have a fixed value but reflect changing investor demand in the marketplace, one of the greatest risks you face when you invest in stock is volatility, or significant price changes in relatively rapid succession. In fact, in some cases, you must be prepared for stock prices to move from hour to hour and even from minute to minute. However, over longer periods, the short-term fluctuations tend to smooth out to show a gradual increase, a gradual decrease or a basically flat stock price.

For example, if a stock you bought for $25 a share dropped $5 in price in the following week because of disappointing news about a new product, you suffered a 20 percent loss. If you had purchased 200 shares at a cost of $5,000, your investment would now be worth just $4,000. If you sold at that point—and there might have been good reason to do so—you would have lost $1,000, plus whatever transaction fees you paid.

While some gains or losses of value seem logical, others may not, as may be the case when a company announces increased earnings and its stock price drops. If you have researched the investment and believe that the company is strong, you might hold on to the stock. In that case, you might be rewarded down the road if the investment then increases in value and perhaps pays dividends as well. While positive results aren't guaranteed, you can learn to anticipate when patience is likely to pay off.

Bonds. Bonds have a fixed value—usually $1,000 per bond—or what is known as par or face value. If you hold a bond until maturity, you will get that amount back, plus the interest the bond earns, unless the issuer of the bond defaults, or fails to pay. In addition to the risk of default, you also face potential market risk if you sell bonds before maturity. For example, if the price of the bonds in the secondary market—or what other investors will pay to buy them—is less than par, and you sell the bonds at that point, you may realize a loss on the sale.

The market value of bonds may decrease if there's a rise in interest rates between the time the bonds were issued and their maturity dates. In that case, demand for older bonds paying lower rates decreases. If you sell, you must settle for the price you can get and potentially take that loss. Market prices can also fall below par if the bonds are downgraded by an independent rating agency because of problems with the company's finances.

Some bonds have a provision that allows the issuer to "call" the bond and repay the face value of the bond to you before its maturity. Often there is a set "call date," after which a bond issuer can pay off the bond. With these bonds, you might not receive the bond's original coupon rate for the bond's entire term. Once the call date has been reached, the stream of a callable bond's interest payments is uncertain, and any appreciation in the market value of the bond may not rise above the call price. These risks are part of call risk.

Just like a homeowner seeks to refinance a mortgage at a lower rate to save money when loan rates decline, a bond issuer often calls a bond after interest rates drop, allowing the issuer to sell new bonds paying lower interest rates—thus saving the issuer money. The bond's principal is repaid early, but the investor is left unable to find a similar bond with as attractive a yield. This is known as reinvestment risk.

Cash. The primary risk you face with cash investments, including U.S. Treasury bills and money market mutual funds, is losing ground to inflation. In addition, you should be aware that money in money market funds offered by investment companies usually is not insured. While such funds have rarely resulted in investor losses, the potential is always there.

Other asset classes, including real estate, pose their own risks, while investment products, such as annuities or mutual funds that invest in a specific asset class, tend to share the risks of that class. That means that the risk you face with a stock mutual fund is very much like the risk you face with individual stock, although most mutual funds are diversified, which helps to offset nonsystematic risk.

Step 2: Selecting Risk

The second step is to determine the kinds of risk you are comfortable taking at a particular point in time. Since it's rarely possible to avoid investment risk entirely, the goal of this step is to determine the level of risk that is appropriate for you and your situation. Your decision will be driven in large part by:

- Your goals and your timeline for meeting them
- Your financial responsibilities
- Your other financial resources

In general, the younger you are, the more investment risk you can afford to take over long periods of time. This is because you have more time to make up for any losses you might suffer in the short term or during shorter periods of market volatility.

On the other hand, having a long time to recover from losses doesn't mean you can ignore the importance of managing risk and choosing investments carefully and selling them when appropriate.

As you get closer to retirement, managing investment risk generally means moving at least some of your assets out of more volatile stock and stock funds into income-producing equities (those that pay a dividend) and bonds. Determine what percentage of your assets you want to transfer, and when. That way you won't have more exposure to a potential downturn than you've prepared for. The consensus, though, is to include at least some investments with growth potential (and therefore greater risk to principal) even after you retire since your retirement may last for quite some time. Without growth potential, you're vulnerable to inflation.

Keep in mind that your attitude toward investment risk may—and probably should—change over time. If you are the primary source of support for a number of people, you may be willing to take less investment risk than you did when you were responsible for just yourself.

In contrast, the larger your investment base, the more willing you may be to take added risk with a portion of your total portfolio. In a worst-case scenario, you could manage without the money you lost. And if your calculated risk pays off, you may have even more financial security than you had before.

Many people also find that the more clearly they understand how investments work, the more comfortable they feel about taking risk.

Step 3: Evaluating Specific Investments

The third step is evaluating specific investments that you are considering within an asset class. There are tools you can use to evaluate the risk of a particular investment—a process that makes a lot of sense both before you make a new purchase and as part of a regular reassessment of your portfolio. It's important to remember that part of managing investment risk is not only deciding what to buy and when to buy it, but also what to sell and when to sell it.

For stocks and bonds, the place to start is with information about the issuer, since the value of the investment is directly linked to the strength of the company—or in the case of certain bonds, the government or government agency—behind them.

Company Documents

Each public company must register its securities with the Securities and Exchange Commission (SEC) and provide updated information on a periodic basis. The annual report on Form 10-K contains audited financial statements as well as a wealth of detailed information about the company, the people who run it, the risks of investing in the company and much more. Companies also submit to the SEC three additional quarterly reports called 10-Qs and interim reports on Form 8-K. You can access these company filings using the SEC's EDGAR database (www.sec.gov/edgar). While they aren't always exciting reading, SEC filings can be a treasure trove of information about a company.

When you're reading a company's financial statements, don't skip over the footnotes. They often contain red flags that can alert you to pending lawsuits, regulatory investigations or other issues that could have a negative impact on the company's bottom line.

The company's prospectus, especially the risk factors section, is another reliable tool to help you evaluate the investment risk of a newly issued stock, an individual mutual fund or exchange-traded fund (ETF) or a real estate investment trust (REIT). The investment company offering the mutual fund, ETF or REIT must update its prospectus every year, including an evaluation of the level of risk you are taking by owning that particular investment.

You'll also want to look at how the fund, ETF or REIT has done in the past, especially if it has been around long enough to have weathered a full economic cycle of market ups and downs—which might be as long as 10 years. Keep in mind, however, that past results cannot predict future performance. Also verify that the fund managers have not changed. In actively managed funds, it is the managers' picks that determine returns and the level of risk the fund assumes. Past returns would not reflect a new manager's performance.

Rating Services

It's important to check what one or more of the independent rating services has to say about specific corporate and municipal bonds that you may own or may be considering. Each of the rating companies evaluates the issuing company a little differently, but all of them are focused on the issuer's ability to meet its financial obligations. In general, the higher the letter grade a rating company assigns, the lower the risk you are taking. But remember that ratings aren't perfect and can't tell you whether or not your investment will go up or down in value. You can find a list of the rating agencies registered with the SEC on its website at: https://www.sec.gov/ocr/ratingagency.html.

Research Reports

Companies, including financial firms and independent research providers, also rate or rank stocks, mutual funds and other investments based on specific sets of criteria. For example, brokerage firms that sell investments often provide their assessments of the performance of specific equity investments with reports that issue a buy, hold or sell rating. Before you rely on ratings to select your investments, learn about the methodologies and criteria a research provider uses in its ratings and remember that some companies have relationships with the companies for which they provide a rating. You might find some research companies' methods more reliable than others.

A Broad View

While the past performance of an investment never guarantees what will happen in the future, it is still an important piece of information. For example, a historical perspective can alert you to the kinds of losses you should be prepared for—an awareness that's essential to managing your risk. A sense of the past can also tell you which asset class or classes have provided the strongest return over time and what their average returns are.

Another way to assess investment risk is to stay tuned to what's happening in the world around you. For example, investment professionals who learn that a company is being investigated by its regulator may decide it's time to unload such company's securities from their clients' portfolios or that they hold in their own accounts. Similarly, political turmoil in a particular area of the world might increase the risk of investing in that region. While you don't want to overreact, you don't want to take more risk than you are comfortable with.

5. Investing to Minimize Risk

While some investors assume a high level of risk by going for the gold—or looking for winners—most people are interested in minimizing risk while realizing a satisfactory return. If that's your approach, you might consider two basic investment strategies: asset allocation and diversification.

Using Asset Allocation

When you allocate your assets, you decide—usually on a percentage basis—what portion of your total portfolio to invest in different asset classes, usually stock, bonds and cash or cash equivalents. You can make these investments either directly by purchasing individual securities or indirectly by choosing funds that invest in those securities.

As you build a more extensive portfolio, you may also include other asset classes, such as real estate, which can also help to spread out your investment risk and so moderate it.

Asset allocation is a useful tool in managing systematic risk because different categories of investments respond to changing economic and political conditions in different ways. By including different asset classes in your portfolio, you increase the probability that some of your investments will provide satisfactory returns even if others are flat or losing value. Put another way, you're reducing the risk of major losses that can result from over-emphasizing a single asset class, however resilient you might expect that class to be.

Financial services companies make adjustments to the asset mix they recommend for portfolios on a regular basis, based on their assessment of the current market environment. For example, a firm might suggest that you increase your cash allocation by a certain percentage and reduce your equity holdings by a similar percentage in a period of rising interest rates and increasing international tension. Financial services companies frequently display their recommended portfolio mix as a pie chart, showing the percentage allocated to each asset class.

Modifying your asset allocation modestly from time to time is not the same thing as market timing, which typically involves making frequent shifts in your portfolio holdings in anticipation of which way the markets will turn. Because no one knows what will happen, trying to time the market rarely produces positive long-term results.

Using Diversification

At its most basic, diversification is not putting all your financial eggs in one basket by choosing a mix of different types of investments, which is called diversification. When you diversify, it's important to divide the money you've allocated not only into different asset classes, but also within those particular asset classes. For example, within the stock category you might choose subclasses based on different market capitalizations: some large companies or funds that invest in large companies, some mid-sized companies or funds that invest in them and some small companies or funds that invest in them. You might also include securities issued by companies that represent different sectors of the economy, such as technology companies, manufacturing companies, pharmaceutical companies and utility companies.

Similarly, if you're buying bonds, you might choose bonds from different issuers—the federal government, state and local governments and corporations—as well as those with different terms and different credit ratings.

Diversification, with its emphasis on variety, allows you to manage nonsystematic risk by tapping into the potential strength of different subclasses, which, like the larger asset classes, tend to do better in some periods than in others. For example, there are times when the performance of small company stock outpaces the performance of larger, more stable companies. And there are times when small company stock falters.

Similarly, there are periods when intermediate-term bonds—U.S. Treasury notes are a good example—provide a stronger return than short- or long-term bonds from the same issuer. Rather than trying to determine which bonds to buy at which time, there are different strategies you can use.

For example, you can buy bonds with different terms, or maturity dates. This approach, called a barbell strategy, involves investing roughly equivalent amounts in short-term and long-term bonds, weighting your portfolio at either end. That way, you can limit risk by having at least a portion of your total bond portfolio in whichever of those two subclasses is providing the stronger return.

Alternatively, you can buy bonds with the same term but different maturity dates. Using this strategy, called laddering, you invest roughly equivalent amounts in a series of fixed-income securities that mature in a rolling pattern, perhaps every two years. Instead of investing $15,000 in one note that will mature in 10 years, you invest $3,000 in a note maturing in two years, another $3,000 in a note maturing in four years and so on. This approach helps you manage risk in two ways:

- If rates drop just before the first note matures, you'll have to invest only $3,000 at the new lower rate rather than the full $15,000. If rates behave

in traditional fashion, they will typically go up again at some point in the ten-year span covered by your ladder.
- If you need money in the short term for either a planned or unplanned expense, you could use the amount of the maturing bond to meet that need without having to sell a larger bond in the secondary market.

How Much Diversification?

In contrast to a limited number of asset classes, the universe of individual investments is huge. Which raises the question: How many different investments should you own to diversify your portfolio broadly enough to manage investment risk? Unfortunately, there is no simple or single answer that is right for everyone. Whether your stock portfolio includes six securities, 20 securities or more is a decision you have to make in consultation with your investment professional or based on your own research and judgment.

In general, however, the decision will depend on how closely the investments track one another's returns—a concept called correlation. For example, if Stock A always goes up and down the same amount as Stock B, they are said to be perfectly correlated. If Stock A always goes up the same amount that Stock B goes down, they are said to be negatively correlated. In the real world, securities often are positively correlated with one another to varying degrees. The less positively correlated your investments are with one another, the better diversified you are.

Building a diversified portfolio is one of the reasons many investors turn to pooled investments—including mutual funds, exchange traded funds (ETFs) and the investment portfolios of variable annuities. Pooled investments typically include a larger number and variety of underlying investments than you are likely to assemble on your own, so they help spread out your risk. You do have to make sure, however, that even the pooled investments you own are diversified—for example, owning two mutual funds that invest in the same subclass of stocks won't help you to diversify.

With any investment strategy, it's important that you not only choose an asset allocation and diversify your holdings when you establish your portfolio, but also stay actively attuned to the results of your choices. A critical step in managing investment risk is keeping track of whether or not your investments, both individually and as a group, are meeting reasonable expectations. Be prepared to make adjustments when the situation calls for it.

6. Modern Portfolio Theory

In big-picture terms, managing risk is about the allocation and diversification of holdings in your portfolio. So when you choose new investments, you do it with an eye to what you already own and how the new investment helps you achieve greater balance. For example, you might include some investments that may be volatile because they have the potential to increase dramatically in value, which other investments in your portfolio are unlikely to do.

Whether you're aware of it or not, by approaching risk in this way—rather than always buying the safest investments—you're being influenced by what's called modern portfolio theory, or sometimes simply portfolio theory. While it's standard practice today, the concept of minimizing risk by combining volatile and price-stable investments in a single portfolio was a significant departure from traditional investing practices.

In fact, modern portfolio theory, for which economists Harry Markowitz, William Sharpe and Merton Miller shared the Nobel Prize in 1990, employs a scientific approach to measuring risk, and by extension, to choosing investments. It involves calculating projected returns of various portfolio combinations to identify those that are likely to provide the best returns at different levels of risk.

7. Risk Protection

You're not alone in wanting to manage investment risk. In addition to the professionals you work with individually, there are federal, state and private-sector agencies and organizations whose responsibilities help reduce risk by:

- Ensuring you have adequate information with which to make investment decisions
- Providing oversight of the companies and individuals through whom you invest and the companies issuing securities to the public
- Insuring you against specific losses

The Securities and Exchange Commission (SEC) requires all publicly traded companies to register and provide detailed financial information, as well as a description of how the company operates, the management team and risks posed to investors. The SEC doesn't evaluate the merits of an investment or make any judgment regarding the potential profit you can make. Instead, the SEC's role is to ensure that you and all other investors have all the information you need to make a reasonable investment decision. Certain securities are exempt from SEC registration, but must meet the requirements of a given exemption (for instance, a requirement that the security can only be sold to certain investors). Transactions involving exempt securities are not exempt from the antifraud, civil liability, or other provisions of the federal securities laws.

The SEC also has the authority to investigate and take legal action against the companies issuing registered securities, the investment advisers who recommend those securities to you and the investment companies, such as mutual funds, that sell them. In addition, the SEC oversees credit rating agencies that evaluate bond issuers.

You can file a complaint with the SEC or report potential violations of the federal securities laws using one of several methods: visit the online SEC Center for Complaints and Enforcement Tips at www.sec.gov/complaint.shtml; call the toll-free investor information service at 800-SEC-0330 (800-732-0330); or write to the SEC Complaint Center, 100 F Street, NE, Washington, DC, 20549-0213. You can also forward electronic copies of investment-related spam (junk e-mail) or message board postings by using the "Add Attachments" feature at the bottom of the online complaint form.

State securities regulators, whose nationwide organization is called the North American Securities Administrators Association (NASAA), register the securities that are sold only within their borders. They also license the brokers, brokerage firms and small investment adviser firms that do business in their states. Note that "small investment adviser firms" means those with under $100 million in managed assets. Once an adviser has over $110 million under management, it must register with the SEC. State regulators play a major role in protecting investors against all types of fraud, which is one of the major risks that investors face if they aren't diligent about checking the credentials of investment professionals and the registration of specific securities.

You can contact NASAA online at www.nasaa.org, by phone at 202-737-0900, by fax at 202-783-3571, or by writing to NASAA, 750 First Street, NE, Suite 1140, Washington, DC, 20002. The website provides a link to securities regulators in each state that provides the relevant address, phone number and email address.

The Financial Industry Regulatory Authority (FINRA) is the largest, non-governmental self-regulatory organization (SRO) for the securities industry and operates under the jurisdiction of the SEC. Its responsibilities include overseeing the activities of brokerage firms, also known as broker-dealers and registered representatives, also called brokers.

FINRA regularly reviews the communications you receive from its members to help ensure that the information you and other investors receive is not misleading or exaggerated, that conflicts of interest are disclosed to you and that it clarifies the risks as well as the potential rewards of investing.

FINRA also conducts regular reviews of firms and representatives under its supervision. It has the authority to investigate and, if warranted, discipline the firms and individuals it regulates.

FINRA also maintains BrokerCheck, a service where you can review the employment history, disciplinary record and qualifications of brokers and brokerage firms, as well as investment advisers and investment adviser firms. Checking out a broker or brokerage firm helps you avoid the risk of working with an unregistered person or firm, and informs you of those firms and individuals with disciplinary histories and customer complaints. You can find this information by visiting FINRA's website at www.finra.org/brokercheck.

If you have questions about investing or are concerned about interactions with a broker or firm you have worked with, you can reach the FINRA Call Center at 301-590-6500. FINRA also maintains a toll-free number that senior investors can call to get assistance from FINRA or raise concerns about issues with brokerage accounts and investments. Call FINRA's Securities Helpline for Seniors at 844-574-3577.

The Securities Investor Protection Corporation (SIPC) is a non-profit, non-government membership corporation, funded by member broker-dealers that provides limited protections to investors. Specifically, if a firm that clears securities trades (a clearing firm) becomes insolvent or otherwise financially incapable of returning the customer’s property, it is SIPC’s responsibility to make sure the customer’s cash and securities are returned, within limits specified by law. SIPC's coverage also extends to firms that sell stocks and bonds to the public (introducing firms).

Coverage includes limited protection against unauthorized trading in customers’ securities accounts, which can include unauthorized trading by persons associated with the introducing firm, and may be available even if the clearing firm, but not the introducing firm, is still solvent. SIPC does not protect against market risk, such as when the value of a stock declines.