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The "Pump and Dump" and "Cybersmear:" An Investigation of Two Cases of Internet-Based Stock Price Manipulation

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This paper examines two cases of stock price manipulation. These explanatory case studies, and the investigative techniques used in their examination, provides a methodology useful to academics, regulators and practitioners, in what is likely to become a growing area of concern and litigation. Both cases involved the creation of hidden or private information, resulting in temporary conditions of information asymmetry. The efficient markets hypothesis provides a theoretical framework for the examination of public and private information. Theory and recent research results predict, and findings suggest, that firms are likely to intervene only in cases where misinformation takes the form of bad news, bashing, or "cybersmear." This is consistent with the firm's economic incentive to reduce the firm's cost of capital.

INTRODUCTION

Stock chat message boards and on-line news services have provided opportunities for greater speed and stock price reactions to information. In at least two recent and highly publicized cases, the Internet has been used to accelerate stock price reactions to information. Both of these cases of stock price manipulation resulted in intervention by the Securities and Exchange Commission (SEC).

This article examines two cases where temporary conditions of information asymmetry were allegedly generated, for apparent personal gain, through the rapid and broad dissemination of false and/or misleading information on Internet stock chat message boards. The first case

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