Financial Industry Has New Rules to Protect the Elderly

The Financial Industry Regulatory Authority is implementing new rules requiring firms to adopt procedures to address the old problem of elder financial abuse.

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Elder abuse has long been a scourge on society. While most individuals cannot fathom taking advantage of those who rely on them or who are less physically or mentally capable, some individuals show no compunction against exploitation of vulnerable elders. According to the United States Census Bureau, in 2010, more than 40 million individuals were age 65 or over in this country.[1] This statistic equates to more than 13% of the total population of the U.S.[2] The United States Census Bureau projects that by 2035, the population of individuals 65 and over will for the first time outnumber the percentage of the population 18 or younger.[3] This 65-and-over segment of the population is projected to account for a staggering 23.5% of the nation's total population. If abuse of the elderly was a problem in the past, it is a problem that inherently will swell with an aging nation.

For attorneys, accountants, financial advisors, and other such professionals, the difficulty has always been how to handle a situation where there is suspected influence, but no hard proof. Often, adults who are the victims of financial abuse are reliant on the abuser and may even be aware of what is occurring. While diminished capacity may be present, the particular dilemma results from the fact that the victims typically would not be considered legally incapacitated. They are often simply reliant and afraid of being on their own. Even the rich and famous, such as Brooke Astor and Mickey Rooney, are not immune from the emotional vulnerability that breeds the environment for an opportunist to take advantage.

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With an aging population, the risk of elder financial abuse continues to grow. The Elder Justice Act was part of the Affordable Care Act, and was enacted in 2010; however, government funding for the programs designed to reduce and detect elder abuse has been lacking. The current administration has reduced much of the funding that had been allocated to this issue of financial abuse of the elderly.

FINRA implements new rules

Recognizing the growing problem of elder financial abuse and the need for greater ability of financial institutions to take action to protect clients, the Financial Industry Regulatory Authority (FINRA) implemented new rules, which took effect on 2/5/2018, to meet this problem head on with the objective of protecting a vulnerable segment of our society.

Examples of the ways in which this growing segment of the population might be manipulated vary greatly. On the one hand, a financial advisor may put an elderly client in unsuitable investments, churn an account, or put the client into high-risk margin transactions. A financial advisor might also borrow funds from an elderly client, partner with the elderly client in some outside business venture, or get himself or herself named as the client's account beneficiary. A third-party, whether it be a much younger second-spouse, adult child, or new acquaintance, might seek to take advantage of an elderly client.

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For instance, the elderly client may have saved every penny from his adult life and then at the behest of a younger new wife suddenly go on an unending spending spree, substantially reducing the value of an account with a capital maintenance objective. Of course, this example in and of itself does not demonstrate elder abuse. It is possible that the elderly client has decided to spend his money rather than pass away without enjoying the fruits of his labor. And therein lies the problem: Is it an independent wish or a coerced decision resulting from fear and isolation? Regardless, such unusual account activity can and should spur questions about whether the elderly client is making his own decisions. The wrongdoing may, similarly, occur as a result of a greedy sibling. It has been said "[n]ever say you know a man until you have divided an inheritance with him."[4]

News headlines and court files are not lacking in reported cases of financial abuse by employees of financial services institutions, attorneys, or accountants.

Cases on point. In *Haynes v. First Nat. Bank of New Jersey*,[5] the elderly Mrs. Dutrow had worked for many years with attorney Stevens on her estate plan. Following the death of her daughter Betty, with whom she had been very close, she moved in with her daughter Dorcas. Dorcas and her husband quickly got to work on Mrs. Dutrow's estate plan, contacting Stevens and involving their own attorney Buttermore. Stevens was very concerned by the involvement of Dorcas, her husband, and Buttermore with Mrs. Dutrow's planning, and testified that Mrs. Dutrow told him she was receiving enormous pressure from Dorcas and her husband to change the estate plan.

Stevens was careful in sharing information with Dorcas or Buttermore, and resisted pressure from Dorcas and her spouse to "go as fast or as far" as they had suggested, which words were quoted by the court from a letter to Stevens by Dorcas' spouse. Stevens repeatedly encouraged Buttermore to double check revisions with Mrs. Dutrow and even wrote to Buttermore expressing concerns about undue influence.

Buttermore did not respond to Stevens; in fact, he simply took over the handling of Mrs. Dutrow's estate planning without seeing the need to involve Stevens further. Not surprisingly, when Betty's son discovered he had been systematically reduced out of his grandmother's estate plan, he challenged the estate plan on the basis of undue influence. The lower courts found that the presumption of undue influence had been met and also that the no-contest clause was unenforceable as a result.

Despite the steps that Stevens took to protect Mrs. Dutrow, the reliance on Dorcas and fear of being abandoned ultimately drove Mrs. Dutrow away from her long-time trusted advisor into the hands of a less ethical professional. But it is not only professionals who go astray, as the manipulation in *Haynes* was also the result of a greedy daughter and her equally greedy husband.

Whatever the scheme, the result can be financial ruin or substantial financial loss. Elder abuse is no joking matter. According to some estimates, the elderly lose billons annually as a result of financial abuse. Until recently, FINRA, the self-regulatory organization governing the securities brokerage industry, had not truly targeted elder abuse nor empowered its member firms to step in and intervene where exploitation is suspected.

The dissent in *Peter v. Morgan Stanley Smith Barney LLC*,[6] aptly demonstrates the problem with FINRA's rules. In this case, Morgan Stanley Smith Barney (MSSB) and one of its advisors were found liable by an arbitration panel where a third party targeted a cognitively impaired MSSB client. The crux of the claim was that respondents should have stepped in to protect the client from the third party. The dissent took issue with the notion that MSSB or its advisor were required to act "in loco parentis" to protect an elderly client from a third-party. The dis-

1 www.census.gov/prod/cen2010/briefs/c2010br-09.pdf.

2 *Id.*

3 www.census.gov/library/visualizations/2018/comm/historic-first.html.

4 Johann Kaspar Lavater, www.ranker.com/list/notable-and-famous-inheritance-quotes/reference.

5 432 A.2d 890 (N.J. 1981).

6 Docket No. 15-02910, 2017 WL 2591772 at *2-6 (FINRA).

7 *Id.* (emphasis in original) (internal quotations omitted).

8 *Id.*

9 FINRA Rule 4512(a)(1)(F) and Supplementary Material .06.

sent pointed out that the claimant based this claim on "training given by MSSB" with respect to "suspected elder abuse." The training was apparently given as a result of FINRA Regulatory Notice 07-43, which encouraged firms to take steps to curb elder abuse.

MSSB's training largely tracked the suggestions in Regulatory Notice 07-43. The Regulatory Notice, however, was guidance and nothing more, stating "we (FINRA) are **not** suggesting that firms are required to take these steps...."[7] Further, "FINRA characterized its 'guidance' as matter of sound business practice and as a way of serving their senior customers...." The dissent concluded that FINRA Regulatory Notice 15-37, which "propos[ed] certain amendments to FINRA Rules 4512 and 2165," "negat[ed] ... any affirmative duty to protect customers from suspected elder abuse" under the circumstances. That was because Regulatory Notice 15-37 explicitly addressed the possible, although not then required, grant of power to a broker dealer to "prevent funds or securities from being disbursed from a customer account where there is a reasonable suspicion of elder abuse."

As to the facts and circumstances of the arbitration, the dissent observed that the advisor identified a possible problem, addressed the situation with the customer, and encouraged her to seek help from family or the authorities. The dissent concluded that there was effectively nothing more that could be done.[8]

Genesis of new rules. The concept born in Regulatory Notice 15-37 has matured into an amended Rule 4512 and new Rule 2165. While these Rules may not end exploitation of the elderly, they are a positive step forward because they require member firms to develop actual policies designed to prevent elder abuse, empower member firms to take the steps needed to protect these vulnerable adults, and mandate training of employees about elder abuse.

Regulatory Notice 17-11 describes the background and reasoning for these amendments as a way to provide members "with a way under FINRA rules to respond to situations in which they have a reasonable basis to believe that financial exploitation has occurred, is occurring, has been attempted or will be attempted. Members can better protect their customers from financial exploitation if they have the ability to contact a customer's designated trusted contact person and, when appropriate, place a temporary hold on a disbursement of funds or securities from a customer's account."

FINRA Rule 4512

The amendment to Rule 4512 creates a proactive environment for establishing next steps should a concern arise during the life of an account. FINRA Rule 4512 has been amended to require that member firms take reasonable efforts to secure the "name of and contact information for a trusted contact person age 18 or older who may be contacted about the customer's account...."[9] This means that when an account is opened or thereafter, the firm is required to have some trusted person who can be contacted if it believes the elderly client is being exploited.

So what amounts to "reasonable efforts"? Notice 17-11 indicates that asking the customer to provide the contact information generally would be reasonable efforts and would satisfy the requirements of the amended rule. The amendments also require disclosure to the client in writing that the institution is authorized to contact the trusted person and to disclose account information to the trusted person in order to address possible financial exploitation.

FINRA Rule 2165

Having identified a "trusted contact" to be alerted in the event that elder abuse is suspected, FINRA Rule 2165 requires that firms adopt and implement policies and procedures with respect to elder abuse, requires that employees be trained about elder financial abuse, and empowers firms to temporarily refuse transactions in light of possible elder abuse. These steps are now mandated without causing advisors to run afoul of FINRA's other rules, including FINRA Rule 11870 requiring the firm and advisor to follow the client's direction.

Protecting specified adults. FINRA Rule 2165 provides protection for "Specified Adult[s]," which covers those 65 years or older and any person 18 years or older with "mental or physical impairment" that precludes the individual from "protect[ing] his or her own interests."[10] The Rule further provides that "financial exploitation" means: "(A) the wrongful or unauthorized taking, withholding, appropriation, or use of a Specified Adult's funds or securities; or (B) any act or omission by a person, including through the use of a power of attorney, guardianship, or any other authority regarding a Specified Adult, to: (i) obtain control, through deception, intimidation or undue influence, over the Specified Adult's money, assets or property; or (ii) convert the Specified Adult's money, assets or property."[11] A "reasonable belief" that a person over the age of 18 has a physical or mental disability preventing him or her from protecting his or her own interests "may be based on the facts and circumstances observed in the member's business relationship" with the customer.[12]

This means that when an account is opened or thereafter, the firm is required to have some trusted person who can be contacted if it believes the elderly client is being exploited.

Triggering Rule 2165 and implementing a temporary hold. Rule 2165's protections are triggered when a member firm "reasonably believes" that financial exploitation of "[a] Specified Adult has occurred, is occurring, has been attempted, or will be attempted..."[13] In that case, the member firm is permitted to "place a temporary hold on a disbursement of funds or securities from the Account of a Specified Adult...."[14] Following the implementation of the "temporary hold," and within two business days, the member firm is required to provide oral or written notice of the temporary hold "and the reason for the temporary hold" to: "(i) all parties authorized to transact business on the Account, unless a party is unavailable or the member reasonably believes that the party has engaged, is engaged, or will engage in the financial exploitation of the Specified Adult; and (ii) the Trusted Contact Person(s), unless the Trusted Contact Person is unavailable or the member reasonably believes that the Trusted Contact Person(s) has engaged, is engaged, or will engage in the financial exploitation of the Specified Adult."[15]

All the while, the "temporary hold" will remain in place and remain effective for not more than 15 days after the date that the "member first placed the temporary hold on the disbursement of funds or securities, unless otherwise terminated or extended by a state regulator or agency of competent jurisdiction or a court of competent jurisdiction, or extended pursuant to paragraph (b)(3) of this Rule."[16] To be clear, the rule would not apply to an order to sell securities, because it applies only to disbursements. If the client requested a distribution of the proceeds of the sale of the stock, however, Rule 2165 would permit a temporary hold on the disbursement of the sales proceeds.

The required internal review. While the "temporary hold" is in place, the member firm is required to "immediately initiate[ ] an internal review of the facts and circumstances that caused the member to reasonably believe that the financial exploitation of the Specified Adult has occurred, is occurring, has been attempted, or will be attempted."[17]

Extending the temporary hold. If the internal review leads to the discovery of "facts and circumstances" supporting the member firm's "reasonable belief that the financial exploitation of the Specified Adult has occurred, is occurring, has been attempted, or will be attempted, the temporary hold authorized by this

10 FINRA Rule 2165(a)(1).
11 FINRA Rule 2165(a)(4).
12 FINRA Rule Supplementary Material 2165.03.
13 FINRA Rule 2165(b)(1)(A).
14 FINRA Rule 2165(b)(1).
15 FINRA Rule 2165(b)(1)(B).
16 FINRA Rule 2165(b)(2).
17 FINRA Rule 2165(b)(1)(C).
18 FINRA Rule 2165(b)(3).
19 FINRA Rule 2165(c)(1).
20 FINRA Rule Supplementary Material 2165.02.
21 FINRA Rule 2165(d).
22 *Id.*
23 FINRA Rule Supplementary Material 2165.01.

Rule may be extended by the member for no longer than 10 business days following the date authorized by paragraph (b)(2) of this Rule, unless otherwise terminated or extended by a state regulator or agency of competent jurisdiction or a court of competent jurisdiction."[18]

Policies, procedures, and training. To ensure compliance with this Rule, all member firms are required to implement "written supervisory procedures reasonably designed to achieve compliance with this Rule, including, but not limited to, procedures related to the identification, escalation and reporting of matters related to the financial exploitation of Specified Adults."[19] The Rule explicitly requires that member firms "develop and document training policies or programs reasonably designed to ensure that associated persons comply with the requirements of this Rule."[20]

While the amended Rules clearly identify and target the problem, Rule 2615's "reasonably believe" standard is vague and uncertain.

Record retention. Member firms are required to "retain records related to compliance with this Rule, which shall be readily available to FINRA, upon request."[21] "The retained records shall include records of: (1) request(s) for disbursement that may constitute financial exploitation of a Specified Adult and the resulting temporary hold; (2) the finding of a reasonable belief that financial exploitation has occurred, is occurring, has been attempted, or will be attempted underlying the decision to place a temporary hold on a disbursement; (3) the name and title of the associated person that authorized the temporary hold on a disbursement; (4) notification(s) to the relevant parties pursuant to paragraph (b)(1)(B) of this Rule; and (5) the internal review of the facts and circumstances pursuant to paragraph (b)(1)(C) of this Rule."[22]

Safe harbor. Recognizing the importance of Rule 2165, FINRA has explicitly provided a "safe harbor" for its member firms and associated persons from Rule 2010 (observance of high standards of commercial honor and just and equitable principles of trade), Rule 2150 (improper use of a customer's account or funds), and Rule 11870 (requiring customer direction to be expedited). This safe harbor applies "when members exercise discretion in placing temporary holds on disbursements of funds or securities from the Accounts of Specified Adults consistent with the requirements of this Rule."[23]

Conclusion

Recently, the authors' firm assisted a family when an elderly relative was told to move all bank accounts out of the financial institution. The family members were shocked, and further investigation revealed that the client was being asked to leave the institution because activity seeming to be possible elder financial abuse had been flagged on the client's accounts. The institution was squarely on point with its suspicions, and had the amended Rule 4512 and new Rule 2165 existed, the institution may have had a different course of action available to help protect the client.

It remains to be seen whether amended Rule 4512 and new Rule 2165 prove effective in combating elder abuse. It is a multibillion dollar answer that remains to be seen. While the amended Rules clearly identify and target the problem, Rule 2615's "reasonably believe" standard is vague and uncertain. What may lead one firm or financial advisor to identify facts and circumstances as evidence of exploitation may not lead another firm or financial advisor to the same conclusion. But, as it has been said before, perfect is the enemy of good. While certain transactions or account activity may obviously suggest exploitation, others may not—the devil is in the details. In that regard, motivating the industry to be vigilant and supervise for instances of elder abuse is critically important and something that probably is long overdue.

Attorneys, accountants, and other advisors need to be aware of these FINRA rules because they may be listed as the trusted person on an account and may see different or increased outreach from financial institutions on these issues. Giving the client's team a better approach to be made aware of and prevent or stop elder financial abuse should benefit everyone.

The ball is now squarely in the possession of FINRA member firms. They bear the onus of swiftly implementing policies, procedures, and training in order to comply with amended Rules 4512 and 2165. Those firms that slow-foot the implementation of such policies, procedures, and training will undoubtedly attract the ire of regulators. They will also find themselves in litigation concerning, among other things, the supervision of their financial advisors. In the end, an ounce of prevention is definitely worth a pound of cure in terms of avoiding regulatory scrutiny and costly litigation. And time is of the essence. ■