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Financial Exploitation of the Elderly: An Overview of Regulatory Action

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Financial exploitation of the elderly is a significant problem, which is only getting worse over time. A study by MetLife estimated that seniors lost $2.9 billion as a result of financial abuse, recognizing that the number was likely low due to underreporting of abuse.[1] Each year, the elder population increases as the baby boomer generation ages. By the year 2050, it is estimated that 83.7 million people will be aged 65 or older, double what it was in 2012.[2]

Not only is the population aging, more people are suffering from mild cognitive impairment. "Several studies indicate that as many as 10 to 20 percent of people age 65 or older have mild cognitive impairment, and prevalence increases with age. And close to half of the U.S. population between the ages of 80 and 89 have a medical diagnosis of substantial cognitive impairment, according to a 2009 study published in the Brookings Papers on Economic Activity."[3] Mild cognitive impairment may affect a person's ability to make sound financial decisions.[4] Moreover, as one ages, there is also a decline in financial literacy. One study found that "financial literacy declines by about 2 percent a year after the age of 60. People in their 60s achieved an average score of 59 percent on a 16-question test measuring participants' understanding of insurance, investments, credit and other money basics. People aged 80 and older were only able to answer 30 percent of the questions correctly."[5]

A number of entities have examined these issues with an eye towards protecting the aging population. This article will discuss the action that has been taken by FINRA, the SEC, and NASAA since the first Senior Summit was held in 2007.

A. The First Senior Summit

In 2006, the SEC convened its first Senior Summit to examine how the various securities regulators could better coordinate efforts to protect seniors from investment fraud.[6] At the time, the NASD Investor

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[1] *The MetLife Study of Elder Financial Abuse: Crimes of Occasion, Desperation, and Predation against America's Elders*, at 2 (June 2011), available at https://www.metlife.com/assets/cao/mmi/publications/studies/2011/mmi-elder-financial-abuse.pdf.

[2] Jennifer M. Ortman, Victoria A. Velkoff, and Howard Hogan, *An Aging Nation: The Older Population in the United States: Population Estimates and Projections*, U.S. CENSUS BUREAU, at 1 (2014), available at https://www.census.gov/prod/2014pubs/p25-1140.pdf.

[3] *Diminished Capacity Can Place Seniors' Money at Risk,* FINRA (Jan. 20, 2016), available at http://www.finra.org/investors/diminished-capacity-can-place-seniors-money-risk.

[4] *See id.*

[5] *Id.*

[6] *See SEC to Conduct First-Ever Seniors Summit July 17 to Protect Older Americans From Investment Fraud*, SEC (July 10, 2006), available at https://www.sec.gov/news/press/2006/2006-109.htm.

Education Foundation released the findings of its study, which attempted to answer two questions: (1) what persuasion tactics are used by the fraudsters; and (2) how do victims of fraud differ from non-victims.[7] The study found that fraudsters use a variety of tactics, but match their pitches to the psychological needs of the victim.[8] The study also found that victims of fraud tended to score higher on financial literacy tests.[9] When looking at investment fraud victims, the study found that victims had certain characteristics; victims were more likely to: (i) be men, married, higher educated, with higher incomes; (ii) listen to sales pitches; (iii) rely on their own experience and knowledge when making financial decisions; and (iv) have experienced more negative life events, but conversely, have a more optimistic outlook on the future.[10]

B. The Second Senior Summit

The following year, the SEC held its Second Senior Summit, once again bringing together regulators and other interested entities to discuss protecting seniors from investment fraud.[11] The SEC, NASAA, and FINRA issued a report on "free lunch" seminars, documenting their examination of firms which conducted the seminars.[12] The report concluded that the sponsors of the seminars offered attractive inducements to attend the seminars, including door prizes or vacations in addition to the free meal.[13] The seminars were often held at upscale hotels, restaurants, retirement homes, or golf courses. The seminars were often aimed at seniors, with titles such as "Senior Financial Survival Seminar" and "Senior Financial Safety Workshop."[14] Although the seminars were often advertised as educational programs, they were designed to have attendees open accounts or purchase financial products.[15] It was determined that at almost a quarter of the firms, unsuitable investment recommendations were made either at the seminar or following the seminar.[16]

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[7]*Investor Fraud Study Final Report*, NASD Investor Education Foundation (May 12, 2006), available at http://www.sec.gov/news/press/extra/seniors/nasdfraudstudy051206.pdf.

[8]*Id.* at 6.

[9]*Id.* at 5 – 6.

[10]*Id.* at 6 – 7.

[11]*SEC to Convene Summit to Combat Investment Fraud Against Senior Citizens*, SEC (Aug. 7, 2007), available at https://www.sec.gov/news/press/2007/2007-160.htm.

[12]*Protecting Senior Investors: Report of Examination of Securities Firms Providing "Free Lunch" Sales Seminars*, Office of Compliance Inspections and Examinations, Securities and Exchange Commission, North American Securities Administrators Association, Financial Industry Regulatory Authority (Sept. 2007), available at www.finra.org/reports.

[13]*Id.* at 3.

[14]*Id.*

[15]*Id.* at 4.

[16]*Id.* at 5.

i. FINRA Guidance

At about this time, FINRA noted that there may be special concerns related to senior investors and firms may be better served by having policies and procedures in place to address these concerns. FINRA expressed particular concern with the suitability of recommendations to, and communication aimed at, senior investors.[17]

With respect to recommendations, FINRA reminded firms that a customer's investment time horizons, goals, risk tolerance, and tax status may change as the customer ages.[18] FINRA cautioned firms that customers who are at or near retirement may be tempted to "reach for yield to maximize retirement income without the appreciation for the concomitant risk."[19] In particular, FINRA examiners focused on broker recommendations that involved the following:

(i) Products that have withdrawal penalties or otherwise lack liquidity, such as deferred variable annuities, equity indexed annuities, some real estate investments and limited partnerships;
(ii) Variable life settlements;
(iii) Complex structured products, such as collateralized debt obligations (CDOs);
(iv) Mortgaging home equity for investment purposes; and
(v) Using retirement savings, including early withdrawals from IRAs, to invest in high-risk investments.[20]

In addition to suitability, FINRA focused on communications. FINRA expressed concern with the use of professional designations, in particular those suggesting an expertise in retirement planning or financial services for seniors.[21] Some firms ban the use of senior designations, while others require approval before they are used.[22] FINRA did not opine on the best practice.

FINRA was also concerned with "free lunch" seminars that use high-pressure sales tactics under the guise of educational seminars to sell unsuitable products, predominately to senior investors. Generally, the seminars had been conducted in violation of FINRA rules. Accordingly, FINRA reminded firms to review

[17] *See* FINRA REGULATORY NOTICE 07-43, *Senior Investors; FINRA Reminds Firms of Their Obligations Relating to Senior Investors and Highlights Industry Practices to Serve these Customers*, FINRA (Sept. 2007), *available at* http://www.finra.org/sites/default/files/NoticeDocument/p036816.pdf.

[18] *Id.* at 2.

[19] *Id.* at 3.

[20] *Id.* at 4.

[21] *Id.* at 5.

[22] *See id.* at 5. *See also* FINRA REGULATORY NOTICE 11-52, *Senior Designations; FINRA Reminds Firms of Their Obligations Regarding the Supervision of Registered Persons Using Senior Designations*, FINRA (Nov. 2011), *available at* http://www.finra.org/sites/default/files/NoticeDocument/p125092.pdf.

their policies and procedures related to sales seminars to ensure that they are adequate to ensure compliance with the rules and regulations.[23]

Last, FINRA expressed concern regarding dealing with investors exhibiting signs of diminished mental capacity, as well as those who may be suffering from financial abuse by a family member or caregiver. FINRA outlined several policies and procedures a firm may adopt for dealing with these issues:

(i) Designating a specific individual or department, such as the compliance or legal department, to serve as a central advisory contact for questions about senior issues, as well as a repository of available resources.

(ii) Providing written guidance to employees on senior-related issues, such as how to identify and/or what to do if they suspect their customer is experiencing diminished capacity or is being abused, financially or otherwise, by a family member, caregiver or other third party.

(iii) Asking, either at account opening or at a later point, whether the customer has executed a durable power of attorney.

(iv) Asking, either at account opening or at a later time, whether the customer would like to designate a secondary or emergency contact for the account whom the firm could contact if it could not contact the customer or had concerns about the customer's whereabouts or health.

(v) Asking the customer if he or she would like to invite a friend or family member to accompany the customer to appointments at the firm.

(vi) Informing the customer (where appropriate) that, in the firm's view, a particular unsolicited trade is not suitable for the customer.

(vii) Reminding brokers that it is important when dealing with customers, particularly seniors, to base recommendations on current information.

(viii) Offering training to help brokers understand and meet the needs of older investors, including proper asset allocation, liquidity demand and longevity needs, as well as the possible changes in their suitability profiles.[24]

ii. NASAA Adopts a Model Rule Addressing the Use of Senior Designations

In early 2008, NASAA adopted the Model Rule on the Use of Senior-Specific Certifications and Professional Designations (the "Model Rule").[25] The Model Rule prohibits the misleading use of senior and retiree designations, and considers it an unethical business practice. The Model Rule also provides a mechanism whereby a state may recognize the legitimacy of certain designations conferred by an accredited organization.[26]

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[23] *See* FINRA REGULATORY NOTICE 07-43, at 6.

[24] *Id.* at 7.

[25] On April 1, 2008, NASAA's membership approved the rule.

[26] NASAA MODEL RULE ON THE USE OF SENIOR-SPECIFIC CERTIFICATIONS AND PROFESSIONAL DESIGNATIONS, available at http://www.nasaa.org/content/Files/Senior_Model_Rule_Adopted.pdf.

The Model Rule specifically prohibits the "use of a certification or professional designation that indicates or implies a level of occupational qualifications obtained through education, training, or experience that the person using the certification or professional designation does not have."[27] Many designations and certifications are obtained by simply paying a fee to the organization, and the individual using the designation does not have any additional education or expertise. Certain of these designations are used in connection with marketing materials purporting to be written by the individuals using the designations, when in fact, the materials have been written by the organization conferring the designation. "We detected a growing problem for senior investors and have responded to it aggressively with a regulatory solution. I urge all NASAA members to adopt this model rule within their jurisdictions as soon as possible," said Karen Tyler, North Dakota Securities Commissioner and President of NASAA.[28] A number of states have adopted the NASAA Model Rule.[29]

C. The Third Senior Summit

In 2008, the SEC held its third senior summit. In its 2008 report, the SEC, NASAA, and FINRA identified examples of practices that financial services firms had developed with respect to their interactions with senior investors.[30] The report addressed nine different areas:

- how firms are thinking of ways to remodel their supervisory and compliance structures to meet the changing needs of senior investors;
- communicating effectively with senior investors;
- training and educating firm employees on senior-specific issues (such as how to identify signs of diminished capacity and elder abuse);
- establishing an internal process for escalating issues and taking next steps;
- encouraging investors of all ages to prepare for the future;
- advertising and marketing to senior investors;
- obtaining information at account opening;
- ensuring the appropriateness of investments; and
- conducting senior-focused supervision, surveillance and compliance reviews.[31]

The report detailed the varied approaches firms had taken to address each of these areas of concern. For example, with regard to communications with seniors, financial services firms had been increasing the frequency of their contact with senior investors, encouraging the designation of emergency or alternate

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[27] *Id.* at Sec.1(c).

[28] *State Securities Regulators Announce New Model Rule on the Use of Senior Certifications and Professional Designations*, NASAA (Apr. 1, 2008), available at http://www.nasaa.org/NASAA_Newsroom/Current_NASAA_Headlines/8423.cfm.

[29] *See*, *e.g.*, N.H. Rev. Stat. §421-B:6; Va. Admin. Code tit. 21, § 5-20-280.A.26.

[30] *Protecting Senior Investors: Compliance, Supervisory and Other Practices Used by Financial Services Firms in Serving Senior Investors,* Office of Compliance Inspections and Examinations, Securities and Exchange Commission, North American Securities Administrators Association, Financial Industry Regulatory Authority (Sept. 22, 2008), available at http://www.sec.gov/spotlight/seniors/seniorspracticesreport092208.pdf.

[31] *Id.* at 2.

contacts for the firm, and educating investors about the benefits of having a power of attorney, in addition to other steps.[32]

In addition, firms had increased employee training to identify issues such as diminished capacity and elder financial abuse.[33] Firms had also begun to obtain additional information from senior investors at the time of account opening.[34] With this additional information, firms implemented additional review of the accounts of senior investors to ensure the appropriateness of investments.[35]

D. NASAA Adopts a Model Act Addressing Financial Exploitation

In January 2016, NASAA adopted the Model Act to Protect Vulnerable Adults from Financial Exploitation.[36] The Model Act offers comprehensive protections to vulnerable adults. For example, the definition of "eligible adult" draws a bright-line at age 65 for identifying adults who may be in need of the increased protective measures provided by the Model Act while still including other vulnerable adults such as those who qualify for protection under a state's adult protective services statute.[37] "Financial exploitation" is broadly defined to include acts or omissions of someone for the purpose of obtaining control of, or converting, money, assets or property of an eligible adult.[38]

The Model Act defines certain people at broker-dealers and investment advisory firms as "qualified individuals" who have the right or obligation to protect an eligible adult.[39] Additionally, the Model Act is not permissive; it requires action if specific individuals have a reasonable belief that an eligible adult is being, may be, or may have been financially exploited. The Model Act requires prompt notification to Adult Protective Services and the securities commissioner of such belief.[40] The Model Act also permits firms to delay disbursements if the firm reasonably believes such a disbursement may result in financial exploitation of a vulnerable adult.[41] The Model Act provides for immunity in either circumstance,

[32]*Id.* at 5-6.

[33]*Id.* at 6-9.

[34]*Id.* at 13.

[35]Firms are also implementing heightened reviews of specific products and limitations on the sales of certain products and riders, such as those discussed at p.4 *supra. Id.* at 14-16.

[36]*See NASAA Model Act to Protect Vulnerable Adults from Financial Exploitation*, NASAA, available at http://serveourseniors.org/about/policy-makers/nasaa-model-act/.

[37]NASAA MODEL ACT TO PROTECT VULNERABLE ADULTS FROM FINANCIAL EXPLOITATION, Sec. 2(3), http://serveourseniors.org/wp-content/uploads/2015/11/NASAA-Model-Seniors-Act-adopted-Jan-22-2016.pdf.

[38]*Id.* at Sec. 2(4).

[39]*Id.* at Sec. 2(7).

[40]*Id.* at Sec. 3.

[41]*Id.* at Sec. 7.

governmental notification or delay of disbursements.[42] Thirteen states have adopted the Model Act thus far.[43]

E. FINRA Adopts Rules 2165 and 4512

FINRA recently adopted rules to protect senior investors and other specified persons from financial exploitation. FINRA is concerned about the increase in financial exploitation of seniors.[44] FINRA adopted Rule 2165 and amended Rule 4512 to provide firms with tools to address suspected financial exploitation of seniors faster and more effectively.[45] The rules permit, although do not mandate, that firms may contact a trusted contact person and place a temporary hold on disbursements from a customer's account if financial exploitation is suspected.[46]

FINRA Rule 2165 allows a firm to place a temporary hold on disbursements from accounts if the firm believes that financial exploitation is occurring, has been attempted, or will be attempted.[47] To rely on the protections in the rule, the firm must develop training policies or programs that ensure associated persons comply with the requirements of the rule.[48]

FINRA Rule 4512 obligates firms to obtain the "name of and contact information for a trusted contact person age 18 or older who may be contacted about the customer's account" for each account.[49] A firm is permitted to open the account without this information if the firm has made reasonable attempts to obtain the information.[50]

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[42] *Id.* at Sec. 4 and 8.

[43] *See NASAA Model Act to Protect Vulnerable Adults From Financial Exploitation Update Center*, NASAA, available at http://serveourseniors.org/about/policy-makers/nasaa-model-act/update/.

[44] *See* FINRA REGULATORY NOTICE 17-11, *Financial Exploitation of Seniors; SEC Approves Rules Relating to Financial Exploitation of Seniors*, FINRA (Mar. 2017), *available at* http://finra.complinet.com/net_file_store/new_rulebooks/r/e/Regulatory-Notice-17-11.pdf.

[45] *See id.*

[46] *See id.*

[47] FINRA RULE 2165(b)(1) (2018).

[48] FINRA RULE 2165.02 (2018).

[49] FINRA RULE 4512(a)(1)(F) (2018).

[50] FINRA RULE 4512.06 (2018).

F. Additional Resources

In 2013, the United States Senate Special Committee on Aging launched a senior fraud hotline, which was intended to make it easier to report suspected fraud and receive assistance.[51] In 2017 alone, the hotline received a total of 1,463 complaints from across the country.[52] The complaints generally refer to the ten scams the Committee has identified, number eight being elder financial abuse.[53]

In 2015, FINRA established the FINRA Securities Helpline for Seniors, which is a "toll-free number that senior investors can call to get assistance from FINRA or raise concerns about issues with brokerage accounts and investments."[54] In two years, "the helpline has fielded more than 9,200 calls from all 50 states from individuals ranging in age from 17 to 102 years old (the average age of callers is 70 years old), and staff have referred nearly 650 matters to state, federal and foreign regulators, and made more than 130 referrals to Adult Protective Services under the mandatory reporting laws of 16 states."[55] As of its second anniversary in April 2017, the helpline has led to $4.3 million in voluntary reimbursements to callers.[56]

Protecting senior investors remains a priority for FINRA. In 2015, FINRA completed an examination initiative on senior initiatives, and has urged firms to review their procedures to "identify ways they may be able to improve their treatment of senior investors."[57] With respect to its examination priorities in 2017, FINRA stated:

> FINRA will assess firms' controls to protect senior investors from fraud, abuse and improper advice. We are seeing numerous cases where registered representatives have recommended that senior investors purchase speculative or complex products in search of yield. While the quest for higher yield is not per se problematic, FINRA will assess whether such recommendations were suitable given an investor's profile and risk

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[51]*See Senate Aging Committee Launches New Anti-Fraud Hotline, Enhanced Website to Assist Seniors* (Nov. 13, 2013), available at https://www.aging.senate.gov/press-releases/senate-aging-committee-launches-new-anti-fraud-hotline-enhanced-website-to-assist-seniors.

[52]*Fighting Fraud: Senate Aging Committee Identifies Top 10 Scams Targeting Our Nation's Seniors*, U.S. Senate Special Committee on Aging (2018), available at https://www.aging.senate.gov/imo/media/doc/2018%20Fraud%20Book1.pdf.

[53]*Id.* at 5 – 6.

[54]*FINRA Securities Helpline for Seniors*, FINRA, *available at* http://www.finra.org/investors/highlights/finra-securities-helpline-seniors.

[55]*FINRA Senior Helpline Marks Second Anniversary With $4.3 Million in Voluntary Reimbursements to Callers*, FINRA (April 20, 2017), *available at* http://www.finra.org/newsroom/2017/finra-senior-helpline-marks-second-anniversary-43-million-voluntary-reimbursements.

[56]*Id.*

[57]FINRA 2015 Regulatory and Examinations Priority Letter, at 10, available at http://www.finra.org/industry/2015-exam-priorities-letter.

tolerance, and whether firms have appropriate supervisory mechanisms in place to detect and prevent problematic sales practices.[58]

[58]FINRA 2017 REGULATORY and EXAMINATION PRIORITIES LETTER, available at http://www.finra.org/industry/2017-regulatory-and-examination-priorities-letter.