FINRA, the SEC and Congress Aim to Safeguard Senior Investors

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The financial exploitation of seniors is an unfortunate trend in the securities industry that has been exacerbated by the COVID-19 pandemic. Fortunately, securities regulators and Congress have recognized the severity of this trend and taken steps to not only protect the senior citizen population, but also to provide tools to broker-dealers to protect them from liability and guide their conduct when investigating potential financial exploitation of seniors

Over the last two decades, fraudulent activity targeting aging investors has increased significantly in the United States. According to the National Center on Elder Abuse, only self-neglect and neglect by others pose greater threats to older Americans. With baby boomers turning into senior citizens, the protection of this population segment was already an annual focus for securities regulators such as the Financial Industry Regulatory Authority (FINRA) and the Securities and Exchange Commission (SEC). The COVID-19 pandemic intensified the issue. Due to coronavirus-related illness and other health challenges, the death of a spouse or loved one, social isolation, and diminished mental capacity, senior citizens have become even more vulnerable to financial scams. In response, FINRA, the SEC, and Congress have worked diligently to create and strengthen rules and legislation in an effort to protect senior investors.

Amendments to FINRA Rule 2165

FINRA Rule 2165, adopted in 2018, was the first national standard for placing temporary holds on brokerage accounts to allow for investigation into suspected financial exploitation. Specifically, it provides FINRA member broker-dealers the ability to "place a temporary hold on a disbursement of funds or securities" from the account of a person 65 years of age or older, if the broker-dealer "reasonably believes that financial exploitation" of such an adult has occurred, is occurring, has been attempted or will be attempted. Significantly, the rule gives broker-dealers a safe harbor from liability for purported violations of other FINRA rules in connection with the broker-dealers' hold on the disbursement request for a maximum of 25 business days while the firm investigates the potential financial exploitation.

Effective March 17, two amendments to FINRA Rule 2165 give FINRA member broker-dealers additional tools to protect investors while also protecting the broker-dealer from liability for temporarily refusing to honor a transaction or disbursement request while investigating potential financial exploitation. First, while brokerage firms were already permitted to place holds on a disbursement of funds or securities where financial exploitation is suspected, they can now also place a hold on a requested securities buy or sell transaction where there is a reasonable belief of financial exploitation. Second, if the member firm has reported the suspected financial exploitation to a state regulator, agency, or a court of competent jurisdiction, the 25 business day hold can be extended for an additional 30 business days, for a total of 55 business days. The Rule 2165 amendments acknowledge that potentially unauthorized securities transactions in a customer's account may result in consequences that are just as harmful as the disbursement of funds or securities. Further, broker-dealers and state authorities may need additional time to conduct thorough investigations into the suspected financial exploitation in order to reach a conclusion. These amendments provide member firms with the time to conduct investigations of suspected financial exploitation while avoiding liability for temporarily holding transaction or disbursement requests in abeyance.

The 'Empowering States to Protect Seniors From Bad Actors Act'

On Jan. 19, Congress took a proactive approach to assisting financially exploited seniors. In a bipartisan effort, U.S. Sens. Chris Van Hollen (D-Md.), Tim Scott (R-S.C.), Raphael Warnock (D-Ga.) and Cynthia Lummis (R-Wyo.) introduced legislation titled the Empowering States to Protect Seniors from Bad Actors Act. The bill was previously introduced in the House by Rep. Josh Gottheimer, D-N.J. and passed out of the Financial Services Committee by voice vote in November 2021. This legislation would provide $10,000,000 for each of fiscal years 2023 through 2028 in grants to state regulators to support the investigation and prosecution of senior financial fraud cases. Such funds would also provide for investment in technology and training, and the education of American seniors on common financial scams.

The SEC would implement the grant program. Scott, in recognition of the pandemic's acceleration of such abuse, stated, "throughout the pandemic, we have seen a heartbreaking uptick in fraud and scams against our nation's seniors. In 2020 alone, more than $1 billion was stolen … as ranking member of the Senate Aging Committee, I'm proud to join my colleagues in fighting these heinous crimes and protecting older Americans. No senior should have to worry about financial fraud in their golden years." The bill is endorsed by the AARP, Americans for Financial Reform, CFP Board and the Financial Services Institute.

Regulation Best Interest's Application to Senior Investor Issues

Regulation Best Interest (Reg BI), while not drafted to address specific senior investor issues, went into effect for broker-dealers, registered investment advisers, and dual registrants during the pandemic on June 30, 2020. The law established a "best interest" standard of conduct for financial advisors when they make a recommendation to a retail customer of any securities transaction or investment strategy involving securities, including recommendations of types of accounts. Retired or retiring investors are confronted with decisions related to the maintenance of 401(k) accounts held with prior employers. The Reg BI standard is applied to decisions to rollover a 401(k) into an Individual Retirement Account (IRA) with a broker-dealer. Specifically, the preamble to Reg BI, states the following:

> … the decision to roll over a 401(k) into an IRA may be one of the most significant financial decisions a retail investor could make. Thus, a broker-dealer should discuss the basis of such recommendations with the retail customer. Similarly, we encourage broker-dealers to record the basis for their recommendations, especially for more complex, risky or expensive products and significant investment decisions, such as rollovers and choice of accounts, as a potential way a broker-dealer could demonstrate compliance with the care obligation.

Accordingly, Reg BI now applies to 401(k) rollover recommendations and broker-dealers must scrutinize these recommendations to reasonably determine whether the rollover is in the best interest of the investor.

The solutions offered by regulators and Congress are significant. It is anticipated that these initiatives are effective tools that will help protect senior investors from financial exploitation, while providing guidance to broker-dealers and helping to reduce liability exposure for broker-dealers and other securities industry professionals in their investigation of financial exploitation of seniors.

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