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Annuities in the Eleventh Hour – Enhanced Regulatory Scrutiny in Sales to Seniors

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I. INTRODUCTION

In October 2009, Anthony D. Marshall, the son of New York philanthropist Brooke Astor, was convicted “on charges that he defrauded his mother and stole tens of millions of dollars from her as she suffered from Alzheimer’s disease.”¹ Marshall’s crime is just one well publicized example of a widespread problem. Seniors, whether or not they have a diminished capacity for controlling their finances, aren’t only potential victims of fraud by family members. Senior investors² are also vulnerable to unscrupulous financial advisers, estate planners, insurance brokers, and other financial agents.

Financial fraud involving the elderly can lead to heightened regulatory scrutiny and enforcement. For example, in a recent arbitration, the Financial Industry Regulatory Authority (“FINRA”) “cited elder abuse in tripling the damages [for a total of \$1.6 million] a discount securities firm must pay a 95-year-old client.”³ “According to FINRA CEO Mary Schapiro, ‘research shows that almost one in five seniors who lost money on an investment attribute that loss to being misled or defrauded ... [t]his concern is real – and confronting it will require a focused regulatory effort that includes vigorous regulatory examination and enforcement programs and investor education.’”⁴

This paper provides an overview of current major initiatives, including enhanced regulatory schemes and state and federal legislation, aimed at protecting seniors from financial abuse with respect to the financial services industry. Of particular significance are statutes and regulations that address the marketing and sales of annuities and other products, as well as financial services companies’ supervisory requirements. Given these initiatives, financial services companies must be aware of their regulatory and statutory obligations in this area and must continue to review and update their corresponding internal policies and procedures.

II. RECOGNIZING DIMINISHED CAPACITY AND FINANCIAL ABUSE OF SENIOR INVESTORS

Any discussion of this subject area requires an understanding of what the indications of a senior investor’s diminished capacity and the financial abuse of such investors are. Although one need not have a diminished capacity for understanding or exercising control over one’s finances to be vulnerable to financial abuse, it is important to be able to recognize the major signs of such diminished capacity, which include the following.

1. “The investor appears unable to process simple concepts”;
2. “The investor appears to have memory loss”;
3. “The investor appears to have difficulty speaking or communicating”;
4. “The investor appears unable to appreciate the consequences of decisions”;

5. “The investor makes decisions that are inconsistent with ... current long-term goals or commitments”;
6. “The investor’s behavior is erratic”;
7. “The investor refuses to follow appropriate investment advice”;
8. “The investor appears to be or is concerned or confused about missing funds in his or her account, where reviews indicate there were no unauthorized money movements or no money movements at all”;
9. “The investor is not aware of, or does not understand, recently completed financial transactions”;
10. “The investor appears disoriented with surroundings or social setting”; and
11. “The investor appears uncharacteristically unkempt or forgetful”.⁵

Any senior investor, however, could become the victim of financial abuse. FINRA has noted that financial abuse of seniors “is difficult to define, and therefore, difficult to recognize. In general terms, it is the misuse of an older adult’s money or belongings by a relative or a person in a position of trust.”⁶ FINRA and other organizations have identified several specific red flags of financial abuse. They include sudden, atypical, unexplained, or unwise withdrawals, drastic shifts in investment style, a financial professional’s inability to contact the senior customer, signs of intimidation or reluctance to speak in the presence of a caregiver, isolation from family and friends, the new use of power of attorney to gain access to financial accounts, recent change in beneficiaries, or new authorized signers on accounts, or a change in address on account statements.⁷

Firms’ education of their professionals in this area is crucial. In September 2008, the SEC’s Office of Compliance Inspections and Examinations, FINRA, and NASAA reported on practices used by financial services firms and securities professionals in serving senior investors.⁸ As part of their report, which “does not create or modify existing regulatory obligations with respect to senior investors,” they noted that many firms are training their employees on how to identify diminished capacity and elder financial abuse.⁹ Specifically, the report recommended that firms establish internal procedures for their professionals, such as documenting suspected diminished capacity or elder abuse. Also, firms should appoint an appropriate person or group, to whom the professional can report the suspected abuse and diminished capacity as soon as it is identified. Once the professional reports the suspicions to the appointed person or group, the legal department should identify any legal reporting requirements, whether the firm should contact any family members, and evaluate any privacy concerns. In addition, the legal department should conduct an internal review of the client’s accounts, to identify any problematic transactions. Similarly, firms should establish procedures for the professional to follow regarding future dealings with the client.¹⁰

III. THE “SENIOR INITIATIVE”

Key to a financial company’s development of internal policies and supervisory procedures regarding financial abuse of seniors is an understanding of the current regulatory and statutory environment. For example, much of the enhanced regulation of sales of financial services to seniors is being developed under the aegis of the “Senior Initiative.” This project has been described as a “multifaceted coordinated national initiative” to “protect seniors [and those nearing retirement] from investment fraud and sales of unsuitable securities.”¹¹ The Senior Initiative includes “targeted examinations, enforcement of the securities laws in cases of fraud against seniors, and active investor education and outreach,”¹² as well as input from “interested parties, including the National Society of Compliance Professionals (NSCP), the Securities Industry and Financial Markets Association (SIFMA), the Investment Company Institute (ICI), and the Investment Adviser Association (IAA).”¹³ Involved in this “Senior Initiative” are the U.S. Securities and Exchange Commission (“SEC”), the North American Securities Administrators Association (“NASAA”), and FINRA.¹⁴ These regulators caution that there is no “one-size-fits-all” approach to addressing the protection of senior investors: “[t]he goal of the initiative is not to impose new regulatory requirements, but to help firms better meet their current obligations to, as well as more generally to serve, their senior customers.”¹⁵

As part of the Senior Initiative, FINRA issued a Regulatory Notice urging its “[member] firms to review and, where warranted, enhance their policies and procedures for complying with FINRA sales practice rules, as well as other applicable laws, regulations and ethical principles, in light of the special issues that are common to many senior investors.”¹⁶ In addition, FINRA highlighted for its member firms “some of the steps that firms, as a matter of sound business practice and as a way of serving their senior customers, are taking to address them.”¹⁷ Those steps include the following:

1. “Designating ... a central advisory contact for questions about senior issues, as well as a repository of available resources”;
2. “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”;
3. “Asking, either at account opening or at a later point, whether the customer has executed a durable power of attorney”;
4. “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”;
5. “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”;

6. “Informing the customer (where appropriate) that, in the firm’s view, a particular unsolicited trade is not suitable for the customer”;
7. “Reminding registered representatives that it is important when dealing with customers, particularly seniors, to base recommendations on current information”; and
8. “Offering training to help registered representatives 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.”¹⁸

Acknowledging that it does not have separate rules governing its member firms’ relationships with senior customers, FINRA reminded its member firms to consider the important factors of their customers’ age and stage of life, such as whether they are “pre-retired, semi-retired or retired.”¹⁹ In particular, FINRA focused on marketing to senior investors, as well as the suitability of recommendations to them.

Various state statutes also address financial abuse of senior investors. “The U.S. Supreme Court has held that the state has an interest in protecting vulnerable groups from abuse, including the elderly.”²⁰ “Many state statutes are patterned after the Older Americans Act of 1965.”²¹ Some of these state statutes directly address financial abuse or exploitation, and many of them have mandatory reporting requirements for suspected elder abuse.²² However, commentators have noted that:

A major difficulty in applying civil law to combat elder abuse is that the victims must bring the suit. Those who are unable to do so receive no guidance in this area of the law. Victims may be overwhelmed by the abusive situation and embarrassed to acknowledge it. Even if sham and embarrassment would not prevent them from acting on their own behalf, they are unlikely to know how to sue or even that laws exist to help them. The burden is even greater because they often lack the financial resources or emotional stamina to initiate an action, much less face the possibility of a lengthy court battle.²³

These statutes are nonetheless generating lawsuits against financial services companies and brokerage firms.

California provides a good example of the potential litigation that financial services companies face as a result of these statutes. California’s “Elder Abuse and Dependent Adult Civil Protection Act” (“Elder Abuse Act”)²⁴ provides, in part, that:

‘[f]inancial abuse’ of an elder²⁵ or dependent adult²⁶ occurs when a person or entity does any of the following: (1) [t]akes, secretes,

appropriates, obtains, or retains real or personal property of an elder or dependent adult for a wrongful use or with the intent to defraud, or both[,] (2) [a]ssists in taking, secreting, appropriating, or retaining real or personal property of an elder or dependent adult for a wrongful use or with intent to defraud, or both[,] (3) [t]akes, secretes, appropriates, obtains, or retains, or assists in taking, secreting, appropriating, obtaining, or retaining, real or personal property of an elder or dependent adult by undue influence, as defined in Section 1575 of the Civil Code.²⁷

Also, “[a] person or entity shall be deemed to have taken, secreted, appropriated, obtained, or retained property for a wrongful use if, among other things, the person or entity takes, secretes, appropriates, obtains, or retains the property and the person or entity knew or should have known that this conduct is likely to be harmful to the elder or dependent adult.”²⁸ Further, “[f]or purposes of this section, a person or entity takes, secretes, appropriates, obtains, or retains real or personal property when an elder or dependent adult is deprived of any property right, including by means of an agreement, donative transfer, or testamentary bequest, regardless of whether the property is held directly or by a representative of an elder or dependent adult.”²⁹

Financial services companies will likely see increased litigation resulting from this and other states’ statutes. In some relatively recent cases, claims under the Elder Abuse Act have survived motions for summary judgment and motions to dismiss. For example, in *Sakai v. Merrill Lynch Life Ins. Co.*,³⁰ a trustee sued for alleged violations of the Elder Abuse Act, claiming that the trust settler was “improperly encouraged in 1995 to exchange a fixed annuity for a variable annuity and thereafter, in 1999, to allow that contract to annuitize.”³¹ In *Sakai*, the court granted the insurer’s Motion for Summary Judgment regarding the trustee’s claim for enhanced damages and attorney’s fees under the Elder Abuse Act, as well as the trustee’s claim for punitive damages. The court, however, denied the insurer’s motion regarding the trustee’s claim for compensatory damages, and therefore allowed the claim to go forward to trial.³²

In addition, in *Negrete v. Fidelity & Guar. Life Ins. Co.*,³³ a conservator alleged that the insurer “defrauded class representative Everett E. Ow [who was 84 years old at the time of purchase] ... into purchasing a deferred annuity that matured after his actuarial life expectancy.” The deferred annuity matured when Ow would have been 98 years old. The conservator further alleged that the insurer aggressively marketed unsuitable annuities to seniors, beginning in 2000, “after F&G abandoned internal supervisory policies limiting the issuance of annuities to seniors.” In addition, the conservator alleged the insurer had a “churning” scheme pursuant to which it depleted the accumulated values of existing annuities. While F&G argued that it could not “take” or “secrete” Ow’s real or personal property, as required by the Elder Abuse Act, the court disagreed and denied F&G’s motion to dismiss. Specifically, the court held that the “churning” allegations, such as using deceptive and misleading illustrations, were “sufficient to state a claim for wrongful ‘taking’” under the Elder Abuse Act.³⁴

Financial services companies must also keep abreast of relevant federal legislation. Congress is currently considering three bills related to the protection of senior investors: (1) the

“Senior Investment Protection Act of 2009” was introduced on April 28, 2009 by Sen. Kohl (D-WI), co-sponsored by Sen. McCaskill (D-MO);³⁵ (2) Senate Bill 1661, introduced on September 10, 2009 by Sen. Kohl (D-WI), and co-sponsored by Senators Casey (D-PA), Franken (D-MN), Gillibrand (D-NY) and McCaskill (D-MO);³⁶ and (3) House Bill 3551, introduced on September 10, 2009, by Rep. Hodes (D-NH), and co-sponsored by Representatives Baldwin (D-WI), Hirono (D-HI), Kaptur (D-OH), Moore (D-WI), and Schakowsky (D-IL).³⁷ The proposed legislation would allow the Attorney General to establish a program to provide grants to states for the investigation and prosecution of misleading and fraudulent marketing practices to seniors, or to “develop educational materials and training aimed at reducing misleading and fraudulent marketing of financial products toward seniors.”³⁸ The legislation would require states, in order to receive the grants, to adopt: “rules on the appropriate use of designation in the offer or sale of securities or investment advice, which shall meet or exceed the minimum requirements of the NASAA Model Rule of Senior-Specific Certifications and Professional Designations;” “rules on the suitability requirements in the sale of securities;” “rules on the appropriate use of designations in the sale of insurance products;” “rules governing insurer supervision of, suitability of, and insurer and insurance producer conduct relating to, the sale of annuity products, including fixed and index annuities”³⁹

Congress is also focusing on long term care insurance. On August 6, 2009, the “Long Term Care Insurance Integrity Act of 2009” was introduced by Sen. Klobuchar (D-MN).⁴⁰ The proposed legislation would require “an insurance issuer that offers a long term care insurance plan [to] develop and implement claims dispute resolution procedures”⁴¹ Those procedures would be required to “expeditiously resolve disputes concerning claims under the plan involved,” involve “third-party review,” and “ensure that an enrollee is eligible to obtain claims review only to the extent and in the manner provided for in the applicable insurance contract.”⁴² The proposed legislation also provides for an appeal of the decision of an independent reviewer.⁴³

IV. MARKETING AND SALES OF ANNUITIES AND OTHER PRODUCTS

A. Professional Designations

Given this regulatory and statutory environment, financial services companies must monitor the marketing and sales of annuities and other products. Marketing and sales begin, of course, with how financial professionals present themselves to potential customers. With respect to member firms’ communications with the public, FINRA expressed concern over “the proliferation of professional designations, particularly those that suggest an expertise in retirement planning or financial services for seniors, such as ‘certified senior adviser,’ ‘senior specialist,’ ‘retirement specialist’ or ‘certified financial gerontologist.’”⁴⁴ Specifically, “[f]irms that allow the use of any title or designation that conveys an expertise in senior investments or retirement planning where such expertise does not exist may violate NASD Rules 2110 and 2210, NYSE Rule 472, and possibly the antifraud provisions of the federal securities laws. In addition, some states prohibit or restrict the use of senior designations.”⁴⁵ Further, “FINRA notes that some third-party vendors are marketing ghostwritten books on senior investing to registered representatives as tools to establish credibility. Holding oneself out as the author of a

book on senior investing, and therefore an expert, could violate a number of rules, including NASD Rules 2110, 2120 and 2210, and NYSE Rule 472.”⁴⁶ Similarly, FINRA expressed concern regarding “the use of aggressive or misleading sales tactics aimed at seniors, particularly the use of ‘free lunch’ seminars that use high-pressure sales tactics to promote products that may not be suitable for all persons in attendance.”⁴⁷

Some brokers and financial planners use professional designations, some legitimate, and some less so, to target senior investors. These designations include “Accredited Investment Fiduciary,” “Chartered Senior Financial Planner,” and “Personal Retirement Planning Specialist,” as well as more general terms such as “Senior,” “Elder,” “Retirement,” or “Retiree” specialist.⁴⁸ While FINRA and the SEC do not recommend, or endorse the use of any particular professional designations, the use of such designations is monitored. For example, “FINRA maintains a database of such designations and the qualifications, if any, that are needed to obtain them ... [but] does not approve or endorse any professional designation, and it maintains the list solely to assist in the evaluation of the listed designations.”⁴⁹

Misuse of professional designations or claims of specialization targeting senior investors is addressed by both FINRA and the NAIC. Specifically, NASD Rule 2210 prohibits brokerage firms and brokers registered with FINRA from referencing nonexistent or self-conferred degrees or designations, or from referencing legitimate degrees or designations in a misleading manner. NASAA’s Model Rule on the Use of Senior-Specific Certifications and Professional Designations, adopted on March 20, 2008, provides a means to separate credible from fraudulent designations, and outlines exactly what constitutes an unusable designation. Further, it explains how organizations can become accredited to legitimize the certifications they offer. Certifying entities can seek accreditation through The American National Standards Institute (ANSI), the National Commission for Certifying Agencies (NCCA), or by any organization listed on the U.S. Department of Education’s “Accrediting Agencies Recognized for Title IV Purposes.”⁵⁰ Many states have adopted rules or legislation aimed at senior designations based on the model approved by NASAA.⁵¹

Similarly, the NAIC’s Model Regulation on the Use of Senior-Specific Certifications and Professions Designations in the Sale of Life Insurance and Annuities prohibits the use of senior-specific certifications or professional designations in advising or servicing seniors in the purchase of life insurance or annuities. Under the Model Regulation, producers who misrepresent their level of expertise in marketing and sales activities will be subject to penalties under state law, and insurers that allow their producers to use misleading designations will also be subject to penalty under state law. In addition, by a ratio of 17 to 1, National Association of Independent Broker-Dealers (NAIBD) members prohibit the use of “senior designations,” and a few of its members have imposed marketing prohibitions particular to senior investors.

B. Marketing Presentations

1. Investment “Seminars”

According to the AARP, close to 6 million senior citizens in the United States receive invitations to so-called “Free Lunch Seminars,” every year.⁵² FINRA Investors Education Foundation research data showed that 78 percent of seniors received one invitation to an investment related seminar and 60 percent of seniors received six or more invitations to an investment related seminar over a three-year period.⁵³ FINRA, NASAA, and the SEC conducted 110 on-site examinations of broker-dealers, investment advisors and other financial services firms between April 2006 and June 2007, looking, in part, at these types of seminars.⁵⁴ The examinations occurred in areas with large populations of retirees, such as Florida, California, Texas, Arizona, North Carolina, South Carolina and Alabama.⁵⁵ The examinations reviewed firms offering sales seminars targeted to seniors and retirees for compliance with securities laws and rules.⁵⁶ They also examined advertisements, seminar materials and sales literature for any misrepresentations, exaggerations or omissions of material information; the customer transactions engendered by these seminars to evaluate the suitability of investment recommendations that were made; and supervisory systems, policies and procedures used to detect and prevent violations of the securities laws.⁵⁷

The results of the examinations, which were reported by the SEC,⁵⁸ revealed that 100 percent of the “seminars” marketed to seniors were in fact merely sales presentations. Even though many of the so-called seminars were advertised as educational workshops with promises that nothing would be sold, they were structured to encourage attendees to open new accounts and to purchase investment products either on the spot or by follow-up contact. In addition, 59 percent of the examinations found weak supervisory practices by firms; the examinations exposed firms that not only poorly managed the seminars, but failed to review seminar materials or presentations as required. Similarly, 50 percent of these seminars exaggerated claims or included misleading information in the advertisements, 23 percent involved possibly unsuitable recommendations, and 13 percent appeared fraudulent and were referred for possible enforcement or disciplinary action.

In addition to the examinations summarized above, AARP and NASAA joined FINRA, NASD and the SEC in launching the “Free Lunch Seminar Monitor Program” in October 2008. The program’s goal is to help protect senior investors from and educate them about fraudulent investment practices.⁵⁹ The program monitors and supervises the so-called “free lunch” seminars to determine whether investors are being pressured into buying unsuitable investments. To do this, AARP and NASAA survey volunteers who attend the seminars and complete check lists containing information about the securities laws and regulations. Individual state securities regulators then evaluate both the products promoted at the seminar, as well as the promoters’ conduct and adherence to securities laws and regulations.⁶⁰ The monitor program included over 1000 individuals age 55 and older.

The survey revealed that 39 percent of seminar attendees were solicited to buy financial products, and 50 percent stated they were asked to supply their financial information. Forty-six percent reported that the presenter attempted to make a follow-up appointment at their residence. The survey also revealed that 39 percent had been encouraged to purchase an annuity. Of the “Free Lunch Seminar” monitors, 48 percent indicated that the presenter never discussed the risks related to annuities, 67 percent stated that the presenter never notified them of the costly surrender charges and penalties of early cancellation of the annuities, and 43 percent reported that the annuities had been recommended as “low risk.” Finally, 54 percent of the attendees were promised investments with returns of 7 percent or higher.⁶¹

Marketing presentations billed as “Retirement Seminars” are also prevalent. “Regulators are also focusing on uncovering registered representatives who improperly advise baby boomers to retire early, cash in their company retirement plans and reinvest the funds in risky investments.”⁶² FINRA has informed corporate human resource directors and unions about such seminars targeting their senior employees and members.⁶³ FINRA has also issued warnings to senior investors, via Investor Alerts, cautioning: “(1) that taking earlier retirement only makes sense if they have saved enough money to begin with, (2) to make smart investment choices during their retirement years and (3) to not withdraw money at a rate which will deplete their savings too early.”⁶⁴ As a commentator has observed, “[w]hile this advice may seem obvious, the number of regulatory actions against such schemes suggests many such investors – blinded by the promise of an early retirement – fail to recognize that it may not be possible for them to do so.”⁶⁵ Much of the concern about such seminars “is based, at least in part, on facts similar to those in a” June 2007 enforcement action, in which the “NASD ordered a large broker-dealer to pay over \$15 million to settle charges relating to failure to supervise a team of brokers who used misleading sales materials during dozens of seminars and meetings for hundreds of employees at a large telephone company.”⁶⁶

Although many of the “Free Lunch” and “Retirement” seminars are designed to sell non-securities products, i.e., insurance, or unregistered securities, a firm that sells securities products, i.e., mutual funds, variable annuities, must be registered as a broker-dealer. Furthermore, NASD Rule 1031 states that in order to discuss investments at a seminar sponsored by a broker-dealer, the presenter must be a licensed registered representative. As stated in Rule 1031, all persons who are already or will be involved in the investment banking or securities business need to register with NASD under the appropriate category. In order for the registration to become effective, all seeking to be registered must pass a Qualification Examination specific to the category of registration they are applying for. Rule 1031 also provides specific procedures for a representative whose license has been revoked or lapsed.⁶⁷ NYSE Rule 345 supplements NASD Rule 1031 by prohibiting any member or member organization from allowing any unregistered person to perform the duties usually performed by a registered person. Furthermore, Rule 345 also prohibits unregistered persons from engaging in the duties of an officer.⁶⁸

2. Sales Materials

Moreover, financial services companies must be aware of the content of the sales materials given to investors at such seminars. As stated in a FINRA Regulatory Notice, member

firms should make certain that all advertisements and sales materials are impartial and accurate. These materials should not contain exaggerated or deceptive information, including self-conferred designations or other unnecessary claims of specialty in the senior investment sector.⁶⁹ Moreover, broker-dealers are required to provide advertising and sales literature concerning mutual funds and variable annuities to FINRA for review and approval within 10 days of the time it is first used or published.

Further, NASD Rule 2210 provides that: “[a] registered principal of the member must approve by signature or initial and date each advertisement, item of sales literature and independently prepared reprint before the earlier of its use or filing with NASD’s Advertising Regulation Department (‘Department’).”⁷⁰ That also includes maintaining a separate file, which must include the name of the registered principal responsible for its approval, with all of the sales literature for three years.⁷¹ Additionally, if the materials involve mutual funds, variable annuities, variable life insurance, unit investment trusts and or public direct participation programs, such material must be filed with NASD’s Advertising Regulation Department.⁷² Furthermore, NASD Rule 2210(d)(1) regulates and prohibits exaggerated and misleading endorsements of investments or the returns thereof. The Rule states in part that advertisements and or its literature containing any testimonial relating to the investment advice or investment performance of a member or its products must make known (1) “the fact that the testimonial may not be representative of the experience of other clients”; (2) “the fact that the testimonial is not indicative of future performance of success”; and (3) “if more than a nominal sum is paid, the fact that it is a paid testimonial.”⁷³ In the context of sales to seniors, compliance with these rules is particularly important, given the enhanced scrutiny these sales can receive.

3. Suitability of Recommendations and Sales of Annuities and Other Products

Firms’ recommendations to investors also receive scrutiny. Regarding the suitability of recommendations, NASD Rule 2310 provides that in recommending “the purchase, sale or exchange of any security, a member shall have reasonable grounds for believing that the recommendation is suitable” for the customer, based on “the facts, if any, disclosed by such customer as to his other security holdings and as to his financial situation and needs.”⁷⁴ FINRA has also noted that Rule 2310 requires firms to make reasonable efforts to gather information regarding customers’ “financial status, investment objectives and ‘such other information used or considered to be reasonable by such member or registered representative in making recommendations to the customer.’”⁷⁵ In addition, it listed several common-sense considerations, such as the customer’s employment status, primary expenses, mortgages, sources of income, retirement savings, the liquidity of the customer’s “income-generating assets,” financial and investment goals, and existing health care insurance.⁷⁶

Moreover, FINRA has noted that its “examiners are focusing on recommendations to seniors, particularly recommendations of: “[p]roducts that have withdrawal penalties or otherwise lack liquidity, such as deferred variable annuities, equity indexed annuities, some real estate investments and limited partnerships; [v]ariable life settlements; [c]omplex structured products, such as collateralized debt obligations (CDOs)⁷⁷; [m]ortgaging home equity for

investment purposes; and [u]sing retirement savings, including early withdrawals from IRAs, to invest in high-risk investments.”⁷⁸ FINRA also noted that a customer’s net worth, all by itself, does not determine suitability: “eligibility does not equal suitability.”⁷⁹

Regarding variable annuities, the SEC approved NASD’s Rule 2821. A FINRA Regulatory Notice explains the limitations of NASD Rule 2821 and also deals with broker-dealers’ compliance and supervisory responsibilities for deferred variable annuities. The principal objective of Rule 2821 is to adhere to particular “recommendation requirements” prior to actually recommending the acquisition or exchange of a variable annuity. In other words, the rule calls for the registered representative to have a reasonably grounded belief that the recommendation will be beneficial to the investor, and to conduct a required determination of suitability.⁸⁰ The Rule also requires that no later than seven business days after the customer has signed an investment application, a registered principal must review and approve the purchase prior to submitting it to the issuing insurance company. In order to ensure that the reviewing registered principals are qualified and in compliance with Rule 2821, member firms will be required to increase specific training policies and or programs. The Rule requires that this review process take place in the time allowed, regardless of whether it was solicited or not. Additionally, the Rule requires that member firms implement specific guidelines for achieving compliance within the standards provided in Rule 2821.⁸¹

Regulators investigate life settlements, or “senior settlements.” “A life settlement involves selling the right to receive the death benefit of an existing life insurance policy to a third party for more than the policy’s cash surrender value, but less than the net death benefit amount.”⁸² “Because the purchasers of the policies are often not subject to (or knowledgeable of) the particular duties a brokerage firm owes its clients, FINRA cautions member firms to conduct thorough due diligence of the suitability of the transaction, the disclosures made concerning the costs and risks associated with the transaction, and the policies of the purchasing organization.”⁸³ FINRA advises seniors that “[a] life settlement might make sense for you if you no longer want or need your current policy – or if you can no longer afford the expense of paying insurance premiums and are willing to give up or replace the coverage.”⁸⁴

The sale of complex structured products, such as “principal only, interest only and” collateralized mortgage obligations (“CMOs”) to senior investors can be the subject of regulatory scrutiny as well.⁸⁵ “Given the fact that they are among the most complex and intricate securities, CMOs are generally reserved for sophisticated investors. Moreover, because of the current sub-prime mortgage and real estate crisis, these investments are particularly risky [to senior investors] and subject to default.”⁸⁶

V. CONCLUSION

Regulations and statutes regarding senior investors will most likely increase as the population of Americans at or near retirement age increases. Given the current regulatory and statutory environment, financial services companies must continue to review and revise their internal policies and procedures regarding their relationships with, and education and supervision of their insurance producers, with respect to the producers’ professional designations presented

to seniors, marketing and sales practices of various products to seniors, and recognizing diminished capacity and elder financial abuse. Such companies must also continue to review their claims practices regarding products, such as long term care insurance, sold to seniors.

¹ John Eligon, *Brooke Astor's Son Guilty in Scheme to Defraud Her*, N.Y. TIMES, Oct. 9, 2009, available at <http://www.nytimes.com/2009/10/09/nyregion/09astor.html?pagewanted=print>. Mrs. Astor died at the age of 105 in 2007. Mr. Marshall, who is 85, was sentenced to one to three years in prison, and will appeal the conviction. James Barron, *Brooke Astor's Son is Sentenced to Prison*, N.Y. TIMES, Dec. 22, 2009, available at http://www.nytimes.com/2009/12/22/nyregion/22astor.html?_r=1&pagewanted=print.

² The term "senior investor" is not limited to people of a specific age or older, but rather applies to those "who have retired or are close to retiring." *Protecting Senior Investors: Compliance, Supervisory and Other Practices Used by Financial Services Firms in Serving Senior Investors*, 3, Sept. 22, 2008, available at <http://www.sec.gov/spotlight/seniors/seniorspracticesreport092208.pdf>. In any event, as one commentator noted, "[f]ar surpassing the rate at which the rest of the American population is growing, the number of those sixty-five and older grew from 3.1 million (4.1 percent of the total population) in 1990 to 35 million (12.4 percent of the total population) in 2000 and is projected to grow to twenty percent of the total population in 2030." Lara Queen Plainsance, *Will You Still ... When I'm Sixty-Four: Adult Children's Legal Obligations to Aging Parents*, 21 J. AM. ACAD. MATRIM. LAW 245 (2008).

³ Bruce Kelly, *FINRA Slaps Discount Broker with Triple Damages in Rare Elder-Abuse Award*, InvestmentNews, Jan. 4, 2010, <http://www.investmentnews.com/apps/pbcs.dll/article?AID=/20100104/FREE/100109950&ht=bruce%20kelly%20discount>.

⁴ Randall J. Fons & Stephanie L. Forbes, *Securities Regulators Take the Initiative in Protecting Older Investors*, 41 REV. SEC. & COMMODITIES REG. 105 (2008).

⁵ *Protecting Senior Investors: Compliance, Supervisory and Other Practices Used by Financial Services Firms in Serving Senior Investors*, *supra* note 2, at 7-8.

⁶ *Id.* at 8.

⁷ *Id.* at 8-9.

⁸ *Id.* at 1.

⁹ *Id.* at 2.

¹⁰ *Id.* at 9-10.

¹¹ Current NASAA Headlines, *SEC and NASAA Launch Program to Protect Senior Investors*, May 8, 2006, http://www.nasaa.org/NASAA_Newsroom/Current_NASAA_Headlines/4677.cfm.

¹² FINRA News Release, *SEC, NASAA and FINRA Announce New Steps to Help Protect Senior Investors*, Feb. 8, 2008, <http://www.finra.org/Newsroom/NewsReleases/2008/P037969>.

¹³ *Id.*; Alston + Bird LLP Securities Litigation Blog, <http://securities.litigation.alston.com/blog.aspx?entry+366>.

¹⁴ Formerly the National Association of Securities Dealers (“NASD”) and the New York Stock Exchange (“NYSE”). “FINRA ... is the largest non-governmental regulator for all securities firms doing business in the United States.” It was “[c]reated in 2007 through the consolidation of NASD and NYSE Member Regulation ...” FINRA News Release, *FINRA Announces Major Regulatory Sweeps at Seniors Summit*, Sept. 10, 2007, <http://www.finra.org/Newsroom/NewsReleases/2007/P036809>.

¹⁵ FINRA News Release, *supra* note 12. “FINRA continues to pay close attention to sales practices aimed at senior investors and baby boomers. FINRA’s efforts include educating investors, firms and registered representatives on key issues surrounding investors in or approaching retirement.” FINRA Letter to Members, Mar. 9, 2009, 5, <http://www.finra.org/web/groups/industry/@ip/@reg/@guide/documents/industry/p118113.pdf>. As part of the Senior Initiative, there have been five major targeted investigations, or “sweeps,” seeking information about certain sales practices on which regulators have been focusing. These “sweeps” have investigated (1) “free lunch” seminars for seniors, (2) professional designations or titles implying an individual has special expertise, certification or training in advising or servicing seniors, (3) early retirement seminars designed to entice older workers to retire early, liquidate their retirement funds, and invest them with a particular registered representative, (4) sales of principal only, interest only, and” collateralized mortgaged obligations to seniors, and (5) marketing life settlements to seniors. Thomas A. Roberts, *The New Frontier: Retiring Baby Boomers and the Senior Market*, from PLI’s Course Handbook, *Securities Arbitration 2008: Evolving and Improving* #14310, 4, 9 (2008), <http://www.sec.state.ma.us/sct/sctpropreg/propreg.htm>.

¹⁶ FINRA Regulatory Notice 07-43, at 1, <http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p036816.pdf>.

¹⁷ *Id.*, at 7.

¹⁸ *Id.* at 7-8.

¹⁹ *Id.* at 2.

²⁰ Shelby A.D. Moore & Jeanette Schaefer, *Remembering the Forgotten Ones: Protecting the Elderly From Financial Abuse*, 41 SAN DIEGO L. REV. 505, 512 (May-June 2004).

²¹ *Id.* at 521; Older Americans Act of 1965, 42 U.S.C. §§ 3001-3058ff (1965).

²² For a review of states’ relevant civil and criminal statutes, see Moore & Schaefer, *supra* note 20, 505.

²³ *Id.* at 524. “States have begun to criminalize acts directed at the elderly, but protection is often limited. [citation omitted]. Florida, for example, has criminalized the abuse of elderly or disabled adults ... as well as financial abuse.” *Id.* at 526.

²⁴ CAL. WELFARE & INSTITUTIONS CODE §§ 15610. – 15610.65 (2010).

²⁵ “‘Elder’ means any person residing in this state, 65 years of age or older.” *Id.* at § 15610.27.

²⁶ Section 15610.23 provides:

(a) ‘Dependent adult’ means any person between the ages of 18 and 64 years who resides in this state and who has physical or mental limitations that restrict his or her ability to carry out normal activities or to protect his or her rights, including, but not limited to, persons who have physical or developmental disabilities, or whose physical or mental abilities have diminished because of age.

(b) ‘Dependent adult’ includes any person between the ages of 18 and 64 years who is admitted as an inpatient to a 24-hour health facility *Id.* at § 15610.23(a),(b).

²⁷ *Id.* at § 15610.30(a)(1) – (a)(3).

²⁸ *Id.* at § 15610.30(b).

²⁹ *Id.* at § 15610.30(c).

³⁰ No. C-06-2581 MMC, 2008 WL 4193058 (N.D. Cal. Sept. 10, 2008).

³¹ No. C-06-2581 MMC, 2008 WL 4193058, at *1.

³² *Id.*

³³ 444 F. Supp. 2d 998 (C.D. Cal. 2006).

³⁴ See also *Labrador v. Seattle Mortgage Co.*, No. 08-2270 CS, 2008 WL 4775239 (N.D. Cal. Oct. 29, 2008) (motion to dismiss class action (including Elder Abuse Act claim) arising out of a reverse mortgage transaction

denied). In Minnesota, the Attorney General has settled with several insurance companies (Great American Life, Allianz Life Insurance Company of North America, American Equity Life Insurance Company, AmerUS Life Insurance Company, American Investors Life Insurance Company and Midland National Life Insurance Company) regarding their sales of deferred annuities to seniors. Minnesota Attorney General Press Release, *Minnesota Attorney General Achieves Settlement with Great American Over Annuities Sales*, Dec. 22, 2009, <http://www.ag.state.mn.us/Consumer/PressRelease/091222GreatAmericanAnnuities.asp>.

³⁵ Senior Investment Protection Act of 2009, S. 906, 111th Cong. (1st Sess. 2009).

³⁶ Senior Investment Protection Act of 2009, S. 1661, 111th Cong. (1st Sess. 2009).

³⁷ Senior Investment Protection Act of 2009, H.R. 3551, 111th Cong. (1st Sess. 2009).

³⁸ E.g., *id.*

³⁹ *Id.*

⁴⁰ Long Term Care Insurance Integrity Act of 2009, S. 1626, 111th Cong. (1st Sess. 2009).

⁴¹ *Id.*

⁴² *Id.*

⁴³ *Id.*

⁴⁴ *Id.* at 5.

⁴⁵ *Id.*

⁴⁶ *Id.* at 6.

⁴⁷ *Id.*

⁴⁸ FINRA Investor Information, *Understanding Professional Designations*, <http://apps.finra.org/DataDirectory/1/prodesignations.aspx>.

⁴⁹ FINRA Regulatory Notice 07-43, *supra* note 16, at 5.

⁵⁰ NASAA Model Rule on the Use of Senior-Specific Certifications and Professional Designations, Adopted Mar. 20, 2008, http://www.nasaa.org/content/Files/Senior_Model_Rule_Adopted.pdf.

⁵¹ *Id.* For example, Massachusetts precludes “an investment advisor from using [a] ‘purported credential or professional designation that indicates or implies that a broker-dealer agent has special certification or training in advising or servicing senior investors, unless such credential or professional designation has been accredited by an accreditation organization recognized by the Secretary by rule or order.’” Roberts, *supra* note 15, at 4, 9 (*quoting* Notice of Final Regulations amending 950 CMR 12.200).

⁵² *No Free Lunch* (Mar. 2009), http://www.aarp.org/money/consumer/articles/_no_free_lunch.html.

⁵³ FINRA Investor Alert, “Free Lunch” Investment Seminars—Avoiding the Heartburn of a Hard Sell, <http://www.finra.org/Investors/ProtectYourself/InvestorAlerts/FraudsAndScams/p036745>.

⁵⁴ Roberts, *supra* note 15, at 6.

⁵⁵ *Id.*

⁵⁶ *Id.*

⁵⁷ *Id.* at 1-23.

⁵⁸ SEC Press Release, “Free Lunch” Investment Seminar Examinations Uncover Widespread Problems, Perils of Older Investors, Sept. 10, 2007, <http://www.sec.gov/news/press/2007/2007-179.htm>.

⁵⁹ AARP Press Release, AARP and NASAA Launch “Free Lunch Seminar Monitor” Program, http://www.aarp.org/aarp/presscenter/pressrelease/articles/Free_Lunch.html.

⁶⁰ *Id.*

⁶¹ Carole Fleck, *A Free Lunch Could Cost You, Survey Finds*, AARP BULL. TODAY, Nov. 13, 2009, http://bulletin.aarp.org/yourmoney/personalfinance/articles/the_high_cost_of_a_free_lunch.html.

⁶² Roberts, *supra* note 15, at 11.

⁶³ *Id.*

⁶⁴ FINRA has urged its member firms to educate customers to avoid financial fraud, through “making investor education materials, prepared by FINRA, the SEC, state regulators, the firm or another source, available to senior investors.” *Id.* On February 8, 2008, the SEC, FINRA, and NASAA broadcasted a combined regulatory program intended to recognize effective practices used by financial firms in examining and managing sales to seniors. FINRA News Release, *SEC, NASAA, and FINRA Announce New Steps to Help Protect Senior Investors*, Feb. 8, 2008, <http://www.finra.org/Newsroom/NewsReleases/2008/P037969>. The program sought to gather information from interested individuals in order to identify strong managerial and compliance performance. Fons & Forbes, *supra* note 4, at 109-10. The regulators were interested in marketing and advertisements targeted towards seniors,

opening of accounts, ongoing review of the relationship and suitability of products, and education and preparation of firm employees. *Id.*

⁶⁵ *Id.*

⁶⁶ *Id.* at 107.

⁶⁷ NASD Rule 1031.

⁶⁸ NYSE Rule 345.

⁶⁹ FINRA Regulation Guidance, *Improving Examination Results*, May 2008, <http://www.finra.org/Industry/Regulation/Guidance/ImprovingExaminationResults/p038526>.

⁷⁰ NASD Rule 2210(b)(1)(A). However, “[t]he requirements of paragraph (A) shall not apply with regard to any advertisement, item of sales literature, or independently prepared reprint if, at the time that a member intends to publish or distribute it: (i) another member has filed it with the Department and has received a letter from the Department stating that it appears to be consistent with applicable standards; and (ii) the member using it in reliance upon this paragraph has not materially altered it and will not use it in a manner that is inconsistent with the conditions of the Department’s letter.” NASD Rule 2210(b)(1)(D). “Effective February 5, 2009, firms may supervise ‘market letters’ as correspondence rather than sales literature, unless the letters are distributed to 25 or more existing retail customers within any 30-calendar-day period and make a financial or investment recommendation or otherwise promote the firm’s product or service.” FINRA Regulatory Notice 09-10, *SEC Approves Rule Relating to Supervision of Market Letters; Effective Date: February 5, 2009*, http://finra.complinet.com/en/display.html?rbid=2403&element_id=7424&print=1.

⁷¹ NASD Rule 2210(b)(2)(A)(i)-(iii).

⁷² NASD Rule 2210(c)(2).

⁷³ NASD Rule 2210(d)(2)(A)(i)-(iii).

⁷⁴ NASD Rule 2310.

⁷⁵ FINRA Regulatory Notice 07-43, *supra* note 16, at 2.

⁷⁶ *Id.* at 3.

⁷⁷ CDOs “are made up of dozens, if not hundreds, of securities, which in turn are backed up by underlying loans, such as mortgages.” The “sudden collapse in [their] price was at the cent of the meltdown of the global banking system.” Jake Bernstein & Jesse Eisinger, Propublica, *SEC Just Now Seeking Key Information on Meltdown*, Dec. 16, 2009, <http://www.npr.org/templates/story/story.php?storyId+121520292>.

⁷⁸ FINRA Regulatory Notice 07-43, *supra* note 16, at 4.

⁷⁹ *Id.*

⁸⁰ NASD Rule 2821.

⁸¹ *Id.*

⁸² Roberts, *supra* note 15, at 13.

⁸³ *Id.* at 13-14 (*citing* FINRA Notice to Members 06-38). States are also enacting legislation regarding life settlements. New York recently became the 27th state to do so. Darla Mercado, *Insurers Cheer Approval of Life Settlement Bill*, *InvestmentNews*, Nov. 22, 2009, <http://www.investmentnews.com/article/20091122/REG/311229977>.

⁸⁴ FINRA Investor Alert, *Seniors Beware: What You Should Know About Life Settlements*, Jul. 30, 2009, <http://www.finra.org/investors/protectyourself/investoralerts/annuitiesandinsurance/p018469>.

⁸⁵ Roberts, *supra* note 15, at 11.

⁸⁶ *Id.*