Financial Gerontology

LEGAL AND ETHICAL ISSUES IN FINANCIAL GERONTOLOGY

Laura Addington, CFP®, MSFS, Sandra L. Reynolds, PhD, and Ronald F. Duska, PhD

In today's litigious climate, many financial professionals are particularly wary of working with older clients. Dealing with older clients presents additional risks beyond those that arise in dealing with younger clients. Industry periodicals, as well as other consumer-based financial magazines, chronicle the difficulties encountered in dealing with older clients: 1) mental and physical capacity issues are a major concern for the adviser, 2) disputes arise with the client's heirs, and 3) while regulatory bodies focused mostly on disclosure issues in the past, they now focus more on issues dealing with the planner's potential abuse of the elder client. While it is true that there are cases in which disreputable planners intentionally inflict harm on older clients, this is far from the norm.

Despite these difficulties, the potential regulatory intervention, and the threat of negative press, planners should consider working in the senior market. Much of the wealth in this country is owned by older adults, so financial professionals who avoid older clients are losing tremendous opportunities. It can be argued that older clients are not substantially different from younger clients. As investors, older clients want the same thing as younger clients—financial security. In addition, incapacity, or "intermittent capacity," is not confined to older clients. In fact, few of the issues discussed in this article, which are usually associated with the elderly, are exclusive to dealing with older clients. Finally, the financial services profession has a moral obligation to service all clients. To do otherwise would be discriminatory. For these reasons, planners should look upon working with older clients as an outstanding opportunity, rather than fear the legal and ethical issues that might ensue from dealing with the financial problems of the elderly.

But what are those legal and ethical issues? This paper will begin by examining some legal issues that financial planners are likely to encounter when dealing with the elderly. It will then discuss issues that are more ethical than legal. It will conclude by illustrating some situations in which the legal and ethical obligations of financial planners may come into conflict.

This issue of the Journal went to press in February 2004.

Legal Issues

The major legal issues that arise when dealing with older clients include appropriately identifying the client, confidentiality conflicts, and determining the legal or decision-making capacity of the client. Let's take a closer look.

Appropriately Identifying the Client

The financial planner is obliged to look out for the best interest of his or her client, and if there is only one client involved, there is no problem identifying the client. But what happens when a financial planner has to deal with a married couple, or has two members of a family as a client? Technically they are both clients, but quite often their interests diverge. When a financial planner sits down with an older married couple to plan their retirement security, which spouse is the primary client whose interest should be served? Is it the spouse with the most money? Is it the husband, because (traditionally) he was the one who made the money or made the financial decisions? Is it the wife, as she will likely be dependent on the advice and counsel of the planner long after her husband dies? From a strictly legal standpoint, the client is the one who signs the agreement with the financial planner, and it should be spelled out in the scope of the engagement.

Unfortunately, however, this does not always provide sufficient practical guidance. Ideally, the financial planner should know both spouses, their values and goals, and how they typically make decisions on financial matters. This is particularly important with clients who, because of the onset of old age, may change their decision-making methodology. Indeed, such a change may signal problems with the very decision-making ability.

The financial planner needs to make an attempt to know the client's family. If the spouse or the client's family does not take an active part in the financial plan, problems can easily arise through lack of communication or understanding. Knowing the client and his or her wishes and documenting them well can be even more important in a "patchwork" family (one in which spouses have had multiple marriages and have both children and stepchildren) where a number of complicated issues arise.

As the financial planner, you are legally obligated to serve the client, and you are bound under the rules of confidentiality not to communicate the financial plan to anyone not authorized by the client, but there is no reason that you cannot encourage the client to be open with those most concerned. Planners, however, may not take it upon themselves to do that for the client. Problems can be avoided if the planner is successful in convincing the client to be open to the inclusion of the advice of the spouse and family. For example, many advisers were concerned during the market boom of the late 1990s that heirs might sue them for being too conservative, even though such investment conservatism was consistent with their client's goals and risk tolerance. If the heirs were involved in the process (to the extent the central client would permit it), then no such lawsuit would ensue. Still, such involvement by heirs assumes those heirs are looking out for the best interest of the client. But the necessity of the financial planner working with others who may or may not have the best interest of the client in mind raises two issues: what does confidentiality require in cases of diminished capacity, and what constitutes diminished capacity?

Confidentiality

Confidentiality is the cornerstone of the relationship between any professional and his or her client. What information is the financial planner legally obligated to keep confidential? First, the client provides you, the financial service professional, with his or her personal financial information, values, objectives and personal details that you need to keep confidential. But how much must be kept confidential? Is strictly personal information to be kept confidential? What about information regarding the client's physical and/or mental state?

Perhaps an even more complicated question arises when dealing with issues of confidentiality with the elderly. If you are working with a married couple and one spouse asks you to keep information from the other, what are you required by law to do? (And if what you are legally required to do is different from what is ethically required, what do you do?)

To look out for the best interests of the client, a good financial planner should not simply give advice on investing but should be thoroughly involved in most aspects of financial and legal planning, including planning both for death and for mental incapacity. Determining who the client actually is and how much confidentiality is required can be handled proactively early on in a relationship with the client. Plans should be made for handling the situation of incapacity.

Several issues should be addressed. Does the client have a will? Does the client have advance directives, such as durable powers of attorney or living wills? Further, even if these documents exist and the client shares them or their provisions with the financial planner, the planner legally cannot share that information with anyone, not even a spouse, without the consent of the client. So besides wills, advance directives and powers of attorney, the planner needs to get the client to document all these arrangements. Of course, one of the most important permissions to have in writing is the permission to share the provisions of a client's will and financial plans with another party.

The financial professional is not responsible for making sure the client has the appropriate legal documents necessary to plan for the future, but prudence dictates that the planner should encourage the client in that direction. Any financial planner who wants to serve the client completely should certainly encourage the client to put both ante- and postmortem wishes in writing. The beginning of the relationship when the scope of the engagement is being spelled out is probably the most opportune time to request in writing what the client would have you do in the event you suspect a loss of mental capacity. By planning ahead and documenting well at the beginning of the relationship, the chance of any future conflict can be reduced greatly—for the client, the planner, and the heirs. In addition, a well-documented and up-to-date investment policy statement is a very valuable tool. If you have not gotten such arrangements documented by your clients, even the young clients who can suffer an incapacitating episode, it is important for your sake and your client's sake that you revisit the scope of the engagement and get those matters resolved.

It is not hard to imagine a worst-case scenario where an issue escalates to arbitration or civil court, and lack of documentation creates a "he said, she said" situation where no one really wins. The financial planner should not only document changes and revisions to financial plans, goals, and objectives, but document everything else that is pertinent. For the planner's protection, if nothing else, he or she should note phone calls, meetings, etc., and follow up with a letter summarizing those calls and meetings.

Ask the client to review the summary letters to be certain that you are both remembering the meeting or conversation the same way, noting who is responsible for which action item. Be specific about whether or not there is follow-up required by the client and/or the financial planner. Be proactive and thorough—the less left to chance and interpretation the better. We have all joked at times that clients hear what they want to hear; be sure to document the fact that the client received the whole message and concurred with it.

Incapacity[1]

A third major legal issue often faced by financial professionals is the question of whether the older client has the capacity or competence to make decisions. Decision-making capacity is an area that confounds the experts, and very few clients or financial planners are experts in this area. The term "incompetence"[2] is generally regarded as applying to someone who has been judged by a court to lack capacity to make his or her own decisions. If you have a client who is incompetent, then you cannot take that client's direction, either for major financial decisions or for simple stock trade permission. If a person is legally deemed incompetent, he or she must have a responsible party who can make those decisions. Depending on the jurisdiction in which the person resides, that might be a guardian, conservator, surrogate, or some other fiduciary. Since one would not set up a new relationship with someone who is already deemed incompetent, this situation will present itself to the financial planner only in cases where a formerly competent client becomes incompetent. Again, the proactive plan is to make provisions for incapacity, and document it, before the fact.

A much more frequent and vexing situation is one in which a client may be losing the capacity to make financial decisions before reaching the point where the family has acknowledged the problem and/or the court has become involved. Denial tends to run rampant in these situations, and the planner is often among the first to notice the signs but is not qualified to make capacity evaluations. What should be done in such cases? For example, suppose a client of 20 years, known to you to be very conservative, calls and asks you to liquidate his portfolio and put all of the money into an illiquid oil and gas limited partnership that a nice fellow from Florida proposed to him. In this situation, prior knowledge of your client is important. Clearly this is a signal that something is wrong and that perhaps you should not follow your client's direction. However, few financial planners have the training or experience to determine whether the client involved has indeed lost the capacity to make decisions. But sometimes the incapacity is clear. In our example, since the planner knows the request is inconsistent with the client's values as he has known them during the past 20 years, the question arises about what the planner should do. If the client is married, should the planner call the client's spouse and notify her? If the client is not married, should the planner call someone else, such as an adult child or physician? It seems clear ethically that the planner ought to do that. It is not so clear legally. The planner is legally required to act upon the client's direction, but ethically that may not be acting in the client's best interest. If the client was found to be incompetent and you had followed the client's direction, would you be legally liable? While a planner is required to follow the client's direction, the planner is restricted from taking orders from someone mentally incompetent. Sometimes, this may result in a decision by the planner that is the lesser of the two evils, but it puts the planner in a very difficult situation.

If, as in many cases, the client (with or without the financial planner's guidance) has executed advance directives in the form of durable powers of attorney that govern any and all financial matters and durable powers of attorney for health care that govern any and all medical treatment decisions, then legally, the financial planner must deal with the person named as agent. But at what point does that become the case? This is one of the hardest things to determine, and the financial professional must walk a fine line at this point between divulging confidential information about the client's mental state and the desire to protect the client and his or her assets. Fortunately, given the rising number of elderly, provisions and regulations are being put in place to help in these difficult situations. Usually, the client will be referred to a geriatric assessment expert or team depending on the circumstances and resources available. In fact, most enlightened geriatric care teams also include a financial planner so that financial issues are not neglected when assessing an older adult's needs.

Court determination of legal competence is dependent upon expert opinion on whether an older adult is capable of making decisions. The standards differ by state, county, and locality, but most states have laws that specify the people who are authorized to determine the capacity of other people, and under what standards. In many states, once someone's capacity has been called into question, some combination of medical or social service professionals is asked to make a recommendation to the court on the person's mental capacity. In Florida, for example, a three-person committee consisting of two doctors (one of whom must be an MD) and a professional (e.g., gerontologist, registered nurse, social worker, etc.) is asked to evaluate the person's ability to make decisions prior to a guardian being appointed for the impaired older adult.

In order to be a party to a contract, one must be of sound mind, but this has been called into question. Dealing with trustees and other fiduciaries of the incompetent client, though, has its difficulties. For example, assume that the long-standing client has done everything right, executed advance directives, and then became incapacitated. The trustee named for and by the client calls to discuss what to do next with the client's investments and requests transactions at odds with the client's best interest. What is the planner to do? The client hired the financial planner with the expectation that the professional would do what was in his or her best interest. But now someone else—the trustee—is legally calling the shots. The planner has an ethical dilemma because he or she knows that the real intent of the client would have been different from what the fiduciary proposes. Does the planner's legal obligation to follow the instructions of the agent outweigh the planner's moral obligation to the client, even though the client can no longer speak for himself or herself? If there are other parties involved, such as potential heirs, whose interests should the financial planner be most concerned about?

Two Scenarios

The following scenarios illustrate simple situations in which there is a dilemma about the right thing to do.

Scenario #1: Mr. Rich owns a company worth over $10 million as well as $50 million in stocks, bonds, and real estate, but he refuses to execute a will because "They're doing away with estate taxes, anyway." As the financial planner for Mr. Rich and his family, you realize that lack of a will is going to create havoc when he dies, since only some of his children are involved in running the company.

Question: Is Mr. Rich's lack of a will any of your concern?

Answer: Legally, no. Ethically, for the good of the client, you are obligated to point out the havoc this is likely to cause for his family postmortem and give your best advice on how to solve that problem. Having given the advice, it is then out of your hands as a financial planner.

Question: Could you be successfully sued for not making sure that Mr. Rich draws up a will?

Answer: Almost certainly not, as a financial planner cannot insist that a client draw up a will. The wise financial planner will, however, have the conversation with the client and will then document the discussion in both the client file and correspondence to the client.

Scenario 2: You have had Mr. and Mrs. Bellicose as clients for eight years. They have small, individual accounts that you manage, as well as a large joint account in which the bulk of their assets are held in survivorship. One day, Mr. Bellicose comes in and asks you to liquidate all of the holdings and turn the proceeds over to him. You know both Mr. and Mrs. Bellicose well enough to know that this is not something Mrs. Bellicose would want; in fact, you have reason to believe that the marriage is in trouble.

Question: Are you legally obligated to turn the funds over to Mr. Bellicose?

Answer: Ultimately, yes. The funds are as much his as hers.

Question: Are you legally obligated to inform Mrs. Bellicose, prior to or after the withdrawal?

Answer: No, legally you are not obligated to do any such thing—the funds are as much his as hers and the account is established giving either the right to withdraw or contribute. Ethically, however, you may have a problem. In this situation, to protect yourself, you may require the client to make the request in writing as well as have both owners sign. This may not be a popular request with Mr. Bellicose; however, financial planners often have to decide how much of a stand they are willing to take. The ethical dilemma puts financial planners in the position of doing what is "right"—covering themselves legally, and following the legitimate wishes of their clients. But would it be right to ignore the issue, knowing that Mrs. Bellicose (who has as much legal right to the funds as her husband) would be impoverished by this withdrawal?

By their very nature, tough issues do not come with a list of do's and don'ts. In a perfect world, legal obligations and ethics would not conflict. Financial planning and implementation, however, rarely take place in such a world. For those financial planners who are eager to serve older clients, it should be some comfort to realize that most of them, by far, have the mental capacity to make decisions. After all, estimates of dementia in older adults show that in the 65+ population, only 5-10% become demential. In the 85+ population, that figure rises to 50%. Older clients are subject to a number of losses that may make them appear to have decision-making difficulty—difficulties that may be temporary or due more to lack of confidence and knowledge than in actual decision-making capacity. Forced retirement, widowhood, loss of similar-age friends, and declining health are more often found in older clients than with younger clients; these losses can make a difference in the way financial professionals may need to help clients achieve their financial goals.

A good financial planner will be in tune with the developments in clients' lives and will be sensitive to their financial, practical, and personal needs. As with clients of all ages, many adverse situations could be avoided with good, consistent, and timely documentation, but resolution of legal and ethical issues will arise from time to time. Fortunately, the individual financial planner can rely on both legal requirements and ethical codes, but ultimately the planner's conduct must be decided on a case-by-case basis, using his or her best judgment. When you find yourself in situations such as these, alliances with gerontological professionals in other areas can provide a sounding board that may be helpful in providing alternative perspectives and guidance.

More education is also desirable. Many local colleges are now offering courses or degrees in financial gerontology and most areas will have an Area Association on Aging. These are good resources although you may build your list of alliances and experts from across the country (see Table 1). There are a number of "Senior" certifications now available for planners; these programs range from several hours of correspondence coursework to college-type curricula with ongoing continuing education requirements. Many of these programs also carry their own code of ethics.

Summary

Working with elder clients can be extremely rewarding in nonmonetary ways. A planner can have the experience of helping someone ensure his or her financial and emotional security, which is gratifying in itself. ■

Laura Addington, CFP®, MSFS, has been serving clients since 1987, specializing in retirement planning and mature market issues. She is a fee-only adviser with her own firm, Addington Financial Group. Ms. Addington may be reached at laura@addingtonfg.com.

After 20 years as a trust banker, Sandra Reynolds obtained a doctorate in gerontology from the University of Southern California, where her dissertation topic was "Public Guardianship in Los Angeles County, CA." She is a professor of gerontology at the University of South Florida, where she teaches and conducts research on guardianship, advance directives, and trends in health. Professor Reynolds can be reached at SandraRe@usc.edu.

Ronald F. Duska, PhD, is professor of ethics and chair holder of the Charles Lamont Post Chair of Ethics and the Professions at The American College, Bryn Mawr, PA. He received his PhD in philosophy from Northwestern University, and he specializes in ethical theory and business ethics. Dr. Duska can be reached at RonaldD@AmerColl.edu.

(1) Incapacity, adj. 1) Not being able to perform any gainful employment due to congenital disability, illness (including mental), physical injury, advanced age or intellectual deficiency… This is significant in claims for worker's compensation, disability insurance, or Social Security claims under "SSI." 2) Lacking the ability to understand one's actions in making a will, executing some other document or entering into an agreement. A challenge to the validity of a will often turns on a claim that the person (now dead and unable to testify) lacked the capacity to understand what he or she owned, who the "natural objects of his/her bounty" were (close relatives primarily), that no one was able to dominate the testator's (will writer's) judgment so as to exert "undue influence." Mental weakness may show lack of capacity to make a will, as can fear, intimidation or persistent drunkenness. Example: An old lady is kept well supplied with whiskey for several months by her greedy sisters. When she is drunk and fearful they will cut off her supply, her sisters convince her to change her will from benefiting her children to benefiting them. A court would probably find she had lacked capacity to decide to make the latest version of the will. Source for definitions: C.P. Sabatino, "Competency: Refining Our Legal Fictions." In M. Smyer, K.W. Schaie, and M.B. Kapp (Eds.), *Older Adults' Decision-Making and the Law* (New York: Springer Publishing, 1996): 1-28.

(2) Incompetent, adj. 1) Referring to a person who is not able to manage his or her affairs due to mental deficiency (low I.Q., deterioration, illness or psychosis) or sometimes physical disability. Source: *Older Adults' Decision-Making and the Law.* Being incompetent can be the basis for appointment of a guardian or conservator (after a hearing in which the party who may be found to be incompetent has been interviewed by a court investigator and is present and/or represented by an attorney) to handle his or her person and/or affairs (often called "estate").

TABLE 1

Useful Web Sites

www.asaging.org	American Society on Aging
www.aarp.org	American Association of Retired Persons (AARP)
www.naela.org	National Academy of Elder Law Attorneys (NAELA)
www.n4a.org	National Association of Area Agencies on Aging (NAAAA)
www.caremanager.org	National Association of Professional Geriatric Care Managers
www.society-csa.com	Society of Certified Senior Advisors
www.icfs.com	Certified Senior Consultant
www.aifg.org	American Institute of Financial Gerontology