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Financial Incapacity and the Aging Boomers: What is the Role of Financial Service Professionals?

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As the boomers march into retirement, the focus of the financial planning world is on retirement income planning. This is evidenced in part by the more than 10,000 advisors who have enrolled in The American College's Retirement Income Certified Professional (RICP®) designation program. Building a comprehensive retirement income plan is complex, as the plan must meet income and other financial needs in this very challenging, low fixed income investment environment. An even harder part of the planning is addressing the many risks faced in retirement. ⁱ

In the coming years, one of those risks - frailty - is going to become front and center as the boomers continue to age. Frailty risk is the risk that, as a result of deteriorating mental or physical health, a retiree may not be able to execute sound judgment in managing his/her financial affairs and/or may become unable to function independently. Think about how this complicates the already complex planning process, as there may become a point when the retiree is no longer able to make optimal decisions about finances, health care, and other areas. All of these decisions can have a dramatic effect on both retirement satisfaction and retirement security.

Cognitive or physical changes in the older client that impair decision-making are especially worrisome for financial advisors, for they raise perplexing regulatory and ethical challenges. Confidentiality requirements make it difficult for the advisors to share information and concerns with family members or other professionals if the client has not provided consent. In addition, the advisor may be put in the difficult position of trying to determine whether the client has the mental capacity to make sound decisions. If the advisor believes that the client lacks capacity, then he or she will not be able to execute the transaction. This might lead to recommending that Adult Protective Services be contacted or a court has to be involved in initiating the guardianship process. On the other hand, if the client is beginning to make worse decisions but the advisor determines that the client still has legal capacity, the advisor

may have the regulatory obligation to execute the transaction to the potential detriment of the client. This poses what Julie Ragatz, Assistant Professor of Ethics and the Director of the Cary M. Maguire Center for Ethics at The American College of Financial Services describes as the central ethical dilemma when working with older clients. That is the conflict between promoting the autonomy of the client and at the same time promoting the good of (or avoiding harm to) the client.

To address the wave of aging boomers, advisors will need to become more aware of signs of cognitive changes and develop a protocol if they suspect their client has cognitive issues. They will also want to understand the planning tools for minimizing issues when a client begins to experience cognitive decline. This article will address a number of these issues:

- Research on the aging brain and the prevalence of cognitive changes in older adults
- The meaning of competency and signs of diminishing capacity
- Prevalence and signs of financial elder fraud
- Steps that can be taken when changes of capacity have been suspected
- Planning for diminished capacity
- Additional Resources

THE AGING BRAIN AND PREVALENCE OF COGNITIVE IMPAIRMENT

It is important to differentiate between the normal changes that occur in an aging brain and changes that result from diseases of the brain like Alzheimer's and other dementias. Brain functions such as the ability to memorize lists, absorbing detailed information and speed in learning new information do decline with age for those with a healthy brain, so care needs to be taken before an advisor assumes that all decision-making capacity automatically declines when a client reaches a certain age. Every individual ages at a different pace, and if a disease is not present, many older adults can maintain the physical and cognitive health well into their 70s and 80s.

That being said, Alzheimer's disease is considered the public health issue of the 21st century as the large number of Boomers move into their later years. Alzheimer's is a degenerative brain disease, and is the most common form of dementia. The Alzheimer's Association estimates that 5.3 million Americans have Alzheimer's disease or other dementias, diagnosed and undiagnosed. Prevalence of these brain diseases

increases with age. One in nine (11%) people age 65 and over and one in three (32%) over age 85 are estimated to have the disease. The number is expected to increase to 16 million by 2050 (Alzheimer's Association, 2015).ⁱⁱ The wake up call for financial advisors now and in the future is that adults who develop this disease gradually lose the ability to handle their finances.

Maybe more disconcerting is that financial capacity is one of the first abilities to decline because of cognitive impairment or dementia (Karp 2012)ⁱⁱⁱ. This is problematic as no other signs of dementia or compromised decision-making may appear in other parts of the client's life and no one has yet noticed signs of diminishing capacity.

There are also studies that show that in general, older adults may still face declining ability to make sound financial decisions. In an article by Annamaria Lusardi^{iv} pointed to research that found that financial literacy of older adults is lower than for other age groups and that financial literacy declines with age. Another study (Korniotis and Kumar (2011)^v evaluated consumer trades at a discount brokerage house and found that older investors are less effective in applying their investment knowledge, with skill level deteriorating sharply at age 70.

Similarly, Michael Finke, in a study using data from the Texas Tech Financial Literacy Assessment project, reports that the ability to understand and apply financial concepts reaches a peak in the early 50s and declines after age 60 by 2 percent a year. The research finds that there is a gradual decline among all those in later life, with no outliers pulling down the average. Finke also found that while competence declines, an older person's confidence in making financial decisions increases, which can present difficult problems for advisors (Finke, 2012)^{vi}

Other research, however, cautions against using age alone as the determinant for cognitive impairment. As a counterpoint to the research showing a decline in the financial skills of all older adults is research from the MetLife Mature Market Institute and the Center for Brain Health at the University of Texas in Dallas (MetLife Mature Market Institute, 2013). The Center recruited adults in their 50s, 60s and 70s, doing in person in depth testing to screen out declines in cognitive function. All were at or above the normal cognitive range. The individuals in each of the age groups were

given a series of exercises and tests. Findings showed that subjects were comparable in their capacity to make logically consistent decisions across the age groups studied; that is, when presented with the same choice described in different ways, their selections were consistent. All three age groups tested the same on strategic learning, which is the ability to sift through information, selecting the important concepts while ignoring the less relevant. The older group in the sample had a higher level of financial conscientiousness and were less likely than those in their 50s to focus on immediate solutions. Men with average cognitive function demonstrated the highest risk-seeking behaviors compared to those of women and those with higher function. ^{vii}

More in-person and in depth research is needed to determine which functions are critical to decision-making in later years, taking into account normal changes in the brain so advisors do not generalize for all older clients. While research does indicate that the very old are more likely to develop cognitive impairment and there are declines in certain brain functions as all of us age, each individual is different and has differing abilities to make decisions. This does not negate the need, however, for all individuals and the advisors who work with them to protect against the possibility of cognitive decline and to make it a part of every retirement planning practice.

THE MEANING OF COMPETENCY AND SIGNS OF DIMINISHING CAPACITY

As clients enter into contracts with financial advisors to provide services and to buy products, financial advisors have to be aware of the legal concept of competency. Under the law, a person is presumed to be competent to enter into a contract, unless it is proven otherwise. If there is a question, a judge must determine that an individual is not competent to make decisions in formal judicial proceedings. It is important to understand that competency is not an either/or condition, rather it is assessed on the match (or mismatch) between an individual's abilities and the decision-making demands that they are facing. Competency is determined by the presence or absence of several factors:

- The ability to communicate a choice
- The ability to understand factual information that is pertinent to a decision
- The ability to appreciate the importance of those facts as applied to one's own situation
- The ability to reach a final decision in a logical manner

Financial capacity has been defined in general terms as “the capacity to manage money and financial assets in ways that meet a person’s needs and which are consistent with his/her values and self-interest” (Marson, Hebert, and Solomon, 2011). In a 2012 article by Triebel and Marson, professors in the Neurology Department at the University of Alabama at Birmingham, identified the following warning signs of dementia which may indicate the beginning of a loss of financial capacity:^{viii}

- Memory lapses—such as missing appointments, not paying bills or paying them twice, asking the same questions multiple times
- Disorganization—losing bills and important documents
- Declines in checkbook management skills—such as forgetting to make entries or getting information incorrect
- Arithmetic mistakes—ability to do computations deteriorates
- Conceptual confusion—difficulty understanding concepts about loans, securities that were not challenging before
- Impaired financial judgment—manifested by a radical change in investment strategy or a new interest in get rich quick schemes

It is important to understand that the loss of capacity is usually a gradual process, and clients generally transition over time. The “Handbook for Lawyers, Assessing Older Clients with Diminished Capacity”^{ix} identifies four different stages of impairment—each stage requiring different responses.

- Intact. No or very minimal evidence of diminished capacity.
- Mild problems. Some evidence of diminished capacity, but insufficient to preclude representation or proposed transaction.
- More than mild problems. Substantial evidence of diminished capacity. Warrants consultation with or referral to mental health professional.
- Severe problems. Client lacks capacity to proceed with the transaction and the representation.

Financial Elder Abuse

One of the consequences of a client’s diminished capacity is vulnerability to elder financial abuse. The National Adult Protective Services Association (NAPSA) defines it as the illegal or improper use of an older person’s or vulnerable adult’s funds, property

or assets. This might include misuse of assets such as guardianship or power of attorney, consumer fraud and scams, theft, or neglect by family, caregivers or by the older person him/herself.

Elder financial abuse is more prevalent than one might think. Researchers estimate that 5 percent of older people are victims. However, this is only the tip of the iceberg (Lifespan, 2011)^x. It is difficult to obtain accurate statistics because this is a crime that is unreported for a variety of reasons--embarrassment, fear of repercussions, or lack of awareness of what has happened.

The typical victim is usually between the age of 70 and 89, Caucasian, female, living alone, frail, cognitively impaired and socially isolated. The perpetrators are often strangers such as workers or caregivers, or almost as prevalent, family members and friends. Financial loss due to elder financial abuse is conservatively estimated at \$ 2.6 billion annually (MetLife Mature Market Institute, 2011)^{xi}.

Some of the signs of financial abuse include the misuse of credit cards, checks that are forged or written without permission, theft of checks that come in the mail, buying financial products that an individual does not understand or cannot afford (such as long-term care insurance), and transferring money to another individual. Once again, advisors are faced with troublesome questions about whether to deny a transaction or to report a client to Adult Protective Services if no previous planning for this type of situation took place.

WHAT TO DO WHEN FACING DIMINISHED CAPACITY

As previously discussed, the issue of capacity to make good decisions is not a bright line issue. Working with senior clients will mean working with clients who are experiencing changes due to the normal aging process. Certain accommodations can be made to make interactions more effective, such as being aware of potential hearing or vision loss, and using adult learning techniques that focus on context first followed by more detailed explanations. In other cases, you have to address cognitive changes due to dementia that pose a serious threat to the decision making process.

It is also important to recognize that some life events for seniors can create temporary symptoms that can look like deterioration. Depression is often misdiagnosed for dementia. For example, a loss of a spouse, family member or close friend can result in grief symptoms. They might include reduced attention span, loss of focus,

hyperactivity, and physical discomforts. Medication or alcohol misuse may also cause drowsiness or lack of concentration. When this occurs, it may be a good time to step back and listen to the client to find out what is happening in his or her life. It is also a good time to suggest a moratorium on making important financial decisions.

However, if an advisor has a client that he or she perceives is having a loss of capacity, certain steps should be taken. The course of action will depend a great deal on if there has been preplanning and the severity of the impairment. Assuming that the client has agreed to share information with a family member or has a power of attorney, then it is time to share what is going on with them. If your company has a protocol for such situations, begin that process as well.

If the client has not agreed to share their personal information with family or other trusted advisors, then the situation is much more difficult. Still some steps should be taken.

- Ask the client if they have a power of attorney (in case you do not know about it)
- Ask the client if they want to bring in a family member or trusted advisor to the next meeting
- Tell the client if you and your firm do not think that the course of action is suitable for them
- Follow your company's protocol—most firms have a process of what to do if you suspect diminished capacity or elder financial abuse
- Document your process

PLANNING FOR DIMINISHED CAPACITY

Building a plan for a time that a client can no longer make decisions requires communication, determining objectives, getting organized and choosing vehicles for transferring control. Let's look at each of these issues.

Communication

Identifying planning goals and objectives starts with having a candid conversation with your clients about issues involving aging and diminished capacity. These conversations are often difficult to initiate, as Alzheimer's is often cited as the disease most feared by older adults. This is especially true if there is a family history of dementia, but even

more reason to begin the conversation sooner rather than later. The advisor needs to raise the issue not only to assure the client's protection if dementia occurs, but also to prevent difficulties down the road in handling a client's affairs. The rule of thumb is that it is better to start a discussion while a client is healthy rather than wait until the advisor begins to suspect that there are signs of cognitive impairment. This may be uncomfortable but necessary.

Many advise that family members be brought into a more general discussion about end-of-life and final wishes, including legal and financial concerns, so that they can be part of the planning process. Planning for diminished capacity can be included in these conversations. While some clients are reluctant to bring up issues like estate planning and financial competence with family members, others may welcome the opportunity but find that their adult children are not interested. In addition, as mentioned earlier, adult children and other family members are often the perpetrators of financial abuse, and a client may have good reason for excluding them from the conversation. There are also growing numbers of older adults who are single, who do not have children, and are part of blended families with stepchildren and step-grandchildren. Each of the situations require individual attention as it may be that a friend or a trusted professional should be the one to be involved.

Advisors can help by providing tools to help their older clients begin a conversation with their adult children, family or trusted friend. Most of the tools focus on discussions of end of life issues, including legal documents, but can serve as a jumping off point. Often, clients are the adult children of aging parents and do not know how to begin a sensitive conversation. They may be the first to notice changes in behavior and symptoms of diminished financial capacity.

Advisors can also be helpful to their older clients or clients who have aging parents by becoming familiar with the resources available to older people and their families in their community, acting as a concierge. Each community has an Area Agency on Aging that supports an information and referral line to help people locate services for older people and navigate the system. They usually have phone counselors on hand to answer questions and can provide lists of resources such as private geriatric care managers, public services such as transportation and social services, and home care services. Since the Area Agencies do not generally offer opinions about which services are best, networking with others and gathering client experiences can be helpful. Area agencies also can provide information about Adult Protective Services should an advisor or family member suspect financial and other abuse. Reports about possible

abuse are anonymous, and, although there is often a backlog of cases, they will trigger an external investigation.

Determine Objectives

Determining the vehicles that should be used and the people who should be chosen for transferring decision-making will depend on the client's unique circumstances.

Specific considerations include:

- The size and composition of the estate,
- The financial, retirement, and estate planning objectives,
- Desire to retain personal control for as long as possible or willingness to delegate some responsibilities earlier to gain a level of comfort,
- Whether to provide agents or trustees a great deal of decision making flexibility or to provide a fairly rigid or limited structure,
- Whether decision-making capacity is already compromised,
- Whether family members or others can step into the decision making role; and
- Concern for costs for professional advice

Getting Organized

As planning generally involves transferring decision making to a third party, good recordkeeping will always facilitate this process. A financial advisor can help a client put together a folder or notebook that includes the following:

- Personal information – include place of birth, addresses of all real estate, and key numbers including Social Security, Medicare and driver's license
- Important contacts – contact information for all immediate family members and others involved in decision making including powers of attorney, trustees, executor, attorneys, financial advisors, accountants, and insurance agents
- Financial records – a recent statement from all investment, retirement, and bank accounts, along with records of beneficiary designations (and contact information). Also copies of insurance policies, records of recurring bills and a copy of the latest tax return

- Medical Information – copies of health care directives and health care powers of attorney, insurance information, health issues and medications
- Legal documents – copies (and location of originals) of the will, trusts, and powers of attorney, beneficiary designations
- Important papers – a copy (and location of originals) of birth certificate, military service records, deeds, insurance policies, stock certificates, a spouse's death certificate, marriage certificates, social security cards, automobile titles, and divorce decrees
- Log-in Information – user names and passwords for all on-line banking and other digital assets, such as personal websites, Facebook accounts, etc.

Vehicles for Transferring Control

When considering the options for formal arrangements for transferring control, the primary tools are powers of attorney and trusts. However, another option is a joint account. This can be appropriate especially with a spouse; however, this alternative gives full control of the assets of the account to the joint owner and means that after death the joint owner inherits the account.

Power of Attorney

With a power of attorney for asset management, the "principal" delegates certain authorities to an agent. To employ this tool, the principal must have the mental capacity to enter into the agreement, and if capacity is in question, it is important to document an individual's competency when signing the document. The most common form is the *durable power of attorney*, which grants an agent broad powers with respect to asset management and decision-making. The power will generally continue until the power is revoked, terminated, or at the principal's death, and it should specifically state that it will survive the principal's loss of capacity.

The durable power is effective when it is first established. Another option is a *springing power of attorney* that becomes effective at the time the principal loses capacity. At first blush, this may seem like a better option, but it is quite difficult to draft the conditions in which the power becomes effective as well as verifying whether the conditions have indeed occurred.

One of the limits of the power of attorney is that the courts - under modern protective statutes to prevent financial elder abuse - typically construe these documents narrowly.

One way to ensure effectiveness is to have the agent use the power with financial institutions involved to see if they have any issues honoring it. Another is to draft the document to be very specific, especially if decisions around special issues may come up.

A key consideration is who should be named the agent, as they are granted broad powers. Be sure that the individual has both the requisite skill and available time to handle the responsibility. There are a number of ways to provide safeguards including:

- Choosing two agents who must act jointly to sign checks and take other actions,
- Choosing a successor agent in case the individual is no longer able to continue the responsibility, and
- Requiring the agent to provide a regular accounting to the principal as well as an independent accountant or attorney.

Revocable Living Trust

The durable power of attorney alone is sometimes not sufficient for transferring control, as actions of the agent may be construed strictly and narrowly by the courts and financial institutions may be reluctant to deal with the agent (both problematic if the principal is incapacitated). An alternative is to have both a durable power of attorney and a revocable living trust. Both the trust and the durable power of attorney can be relatively inexpensive arrangements to set up and administer.

The trust is a much more flexible vehicle with respect to investing assets and making necessary distributions (including distributions to other trust beneficiaries). When structuring the living revocable trust, the trust identifies the grantor's instructions for the property held in trust. Typically, at the time the trust is established, most or all of the personal and financial assets are retitled to be held in trust. Waiting to fund the trust can be problematic if the grantor becomes incapacitated. A way to address this concern is to give the agent with the power of attorney the ability to fund the trust or withdraw assets from the trust as necessary. It may even be appropriate to empower the agent to change the terms of the trust or revoke the trust if necessary.

With a revocable living trust, it is common for the grantor to be the trustee initially, and family members or professionals identified as contingent trustees. The grantor can

simply step down and appoint a contingent trustee or transfer control at incompetency. The trust should require an independent determination (two named physicians) of incompetency.

Choosing Representatives

Many people choose family and trusted friends to take on the role of agent or trustee. There are serious concerns however, that these individuals may not have the available time or requisite skill to properly fulfill these roles.

Another alternative is to work with a corporate trustee from a bank trust department or an independent trust company. Trust officers are experienced in handling such matters and will have an understanding of their impartial role, trust investments, tax considerations, trust accounting, budgeting and managing tax flow. Corporate trustees can take on different roles:

- Sole trustee handling both trust administration and acting as investment manager
- Co-trustee providing similar services but working in cooperation with an individual (who may be the creator of the trust or a trusted representative)
- The financial advisor works with an individual trustee providing investment services
- Successor trustee when an individual can no longer act as trustee—in which case certain trust services may be available

Working with a corporate trustee adds expense, but a professional will minimize problems that could arise when individuals chosen do not have the professional expertise to fill the role or may not have the individual's best interest at heart.

RESOURCES

There are many great resources for advisors wanting to know more about the complex issue of working with older clients who may be facing diminishing capacity. Here is a list:

- A financial planner's guide to addressing the risks faced in retirement, [Retirement Risk Solutions](#)

- [National Institute on Aging](#), for additional information about Alzheimer's disease and its effect on financial skills
- A planning tips document for consumers from the Met Life Mature Market Institute, "[Is Your Decision Making Process Healthy?](#)"
- To see how attorneys look at this issue see the [Handbook for Lawyers, Assessment of Older Clients With Diminished Capacity](#), published by the American Bar Association and the American Psychological Association
- A good resource for addressing financial elder abuse can be found at the [Women's Institute for Secure Retirement](#).
- For advice on addressing diminishing capacity from FINRA listen to the Podcast, "[Considerations for Working with Seniors: Diminishing Capacity and Suspected Financial Abuse](#)"
- The Conversation Project <http://conversationproject.org> is a guidebook that provides a way for families to start a discussion about these issues.
- The Consumer Protection Finance Board has prepared a tip sheet for older people and their families called [Planning for Diminished Capacity and Illness](#)
- For a better understanding of symptoms of depression and comparisons to dementia, see this [Factsheet](#) from Here To Help.
- The Alzheimer's Association has information on [Financial Planning Considerations](#) once an individual has been diagnosed with early stages of the disease that advisors may want to encourage clients to read.
- [Ten Tips for Talking with an Older Parent](#), MetLife Mature Market Institute
- A guide for caregivers from the MetLife Mature Market Institute, [Alzheimer's Disease, Caregiving Challenges](#).
- To find the Area Agency on Aging in a specific locale, go to www.eldercare.gov

CONCLUSIONS

Financial advisors need to get prepared to deal with the challenges of boomers moving deeper into retirement. Relationships with older clients can be extremely satisfying, but they can also be challenging. Dealing with even a single client who is losing the ability to make good decisions can be heart wrenching. As boomers age, multiply this concern, and it becomes clear that it is time to get prepared. Getting clients to plan for this time in their life is a key priority, as is setting up procedures

for what to do when situations arise. Maybe the first step is educating yourself about signs of dementia, and all the resources mentioned in this article are excellent places to start. The solutions also involve getting closer to your older clients, and often involve working closer with their families. All of this can have a positive impact on your practice as well.

There is also room for regulatory solutions. It is interesting that FINRA has just issued a **proposed rule** for addressing a related issue, elder financial abuse. The rule requires registered representatives to request that each new client identify a “trusted person” who will be contacted if the firm suspects that a transaction is suspicious. The rule also allows the firm to put a hold on the account, while a suspicious transaction is investigated. This is a big and welcome shift in regulatory policy. This same approach could be expanded to issues involving a loss of capacity.

ⁱ **Retirement Risk Solutions**, The American College, 2013

ⁱⁱ Alzheimer’s Association. Facts and Figures: Alzheimer’s and Dementia, 2015 Alzheimer’s Disease, 11(3)

ⁱⁱⁱ Naomi Karp, “Protecting Older Investors: The Challenge of Diminished Capacity”, *Generations*, Summer, 2012, Vol 36, No. 2

^{iv} Annamaria Lusardi, “Financial Literacy in Older Adults”, *Generations*, Summer 2012, Vol. 36, No. 2

^v Korniotis and Kumar, “Do Older Investors Make Better Investment Decisions?” *Review of Economics and Statistics* 2011, Vol 93(1): 244–65.

^{vi} Finke, Michael. “Investing and the Aging Brain: What do I do When I Get Stupid?” *Research Magazine*, August 2012.

^{vii} MetLife Mature Market Institute, “Healthy Brain, Healthy Decisions: The MetLife Study of Decision Making Potential”, Mature Market Institute and the Center for Brain Health, University of Texas at Dallas, 2012.

^{viii} Triebel and Marson) “The Warning Signs of Diminished Financial Capacity in Older Adults,” *Generations*, Summer 2012, Vol 36 No 2

^{ix} **Handbook for Lawyers, Assessment of Older Clients With Diminished Capacity**, American Bar Association and the American Psychological Association, 2005

^x “Under the Radar: New York State Elder Abuse Prevalence Study”, May 2011, Prepared by: Lifespan of Greater Rochester, Inc., Weill Cornell Medical Center of Cornell University, New York City Department for the Aging

^{xi} <https://www.metlife.com/assets/cao/mmi/publications/studies/2011/mmi-elder-financial-abuse.pdf>