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What You Need to Know About Trusted Contact Persons

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If you are over 65, a recently adopted FINRA rule allows you to designate another adult to be your trusted contact person.

This new rule allows financial institutions that suspect possible fraudulent activity in your account to communicate on a confidential basis with an individual you trust and designate in advance for this purpose. They can also contact the TCP if they believe you may be engaging in meaningless and wasteful activities, such as churning an account, that suggest dementia or similar problems, something that can occur even in the absence of a financial predator.

Why is this important for you to know about? Like it or not, you or someone you love (or even a client) may need this protection in the future.

The extent to which the elderly are targets of fraudulent schemes and abuses is hard to quantify, but it's rampant and out of control. It's estimated that one out of every five seniors is likely to be victimized. Reported losses run close to \$3 billion annually, even though only 1 in 44 losses are believed to be reported, suggesting that the total losses are closer to \$125 billion a year.

Alzheimer's and other forms of dementia, which afflict approximately one half of the population by around age 85, affect

Editorial Purpose

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our ability to handle our financial affairs responsibly and to protect ourselves from predators. Even apart from dementia, as we age, we experience physiological and mental changes that make us less able to discern when we're being victimized. The elderly become increasingly vulnerable to fraud and less able to understand that they're being cheated.

The predators will usually be people you know and trust. More than half of the time (some estimates are as high as 90 percent), the predator will be a relative or caregiver. One study found that one-sixth of the predators are attorneys or other fiduciaries.

DISCLOSURE WAS RISKY FOR BROKER-DEALERS

Before the new FINRA rule was adopted, when a financial institution suspected a problem, privacy laws limited what it could disclose to someone other than you. More important, disclosing information to a third party, even a close relative, might actually result in the very financial disaster you're trying to prevent; the person the financial institution contacted might well be the financial predator, and disclosure might only enhance the predator's ability to take advantage of you.

For example, a financial institution's communication might disclose the existence and other important details of an account the predator wasn't even aware of, information you intentionally wished to withhold from that person.

The new FINRA rule now requires every broker-dealer to allow seniors to designate a TCP to cover these situations. Initially, the rule will apply only to new accounts, but it will be extended to existing accounts at various times over the next year or so. In a few special cases, it may also apply to investors under 65.

In many cases, financial institutions will permit you to designate a TCP for an existing account immediately, but in those cases, you will probably have to initiate the process. After the new rule applies to your existing account, the broker-dealer will have to initiate the process, asking you for the name and contact information of a TCP. There's no penalty if you decline to provide a name, but financial institutions must try.

Designating a TCP to receive confidential information appears to waive any concern about liability for disclosing that information to the TCP.

HOW THE TCP HELPS YOU

The FINRA rule permits, but doesn't require, a financial institution to contact your designated TCP to warn of possible financial abuse or other red flags of suspicious irregularities. In so doing, it may discuss very confidential information about you and your account, including your possible medical issues (such as dementia or other incompetency).

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If the broker-dealer has a reasonable belief that you are being defrauded or otherwise subjected to financial abuse, it's authorized to suspend temporarily any distribution to you while it investigates the situation. If it does suspend distributions, it's required to inform the TCP of that action.

In all other cases, even including clear-cut fraud, it's entirely voluntary whether to contact and warn the TCP. This is a serious shortcoming; reporting to the TCP fraudulent or even highly suspicious activities should generally be mandatory (except, obviously, where the TCP is the suspected bad guy).

After the rule took effect, I contacted several leading financial institutions and was able to designate one TCP at each for my existing accounts. None allowed me to designate more than one TCP, although one permitted me to designate an "alternate" TCP who could be contacted if the primary TCP was unavailable.

Unfortunately, in every case, finding where on the website to make this designation took a great deal of hunting, and it was invariably necessary to contact the institution to locate that option. Nothing on the opening pages of the websites notified investors that the option was now available or how (or why) to take advantage of it. To my knowledge, none have committed to alert the TCP of suspicious activity, such as a change of beneficial interests naming someone not apparently related to you.

WHETHER TO NAME A TCP

Should you take advantage of this opportunity to designate a TCP? If so, whom should you choose? What are the obligations of the TCP? The answers to these questions aren't always obvious.

Most important, you must be comfortable with the idea that the financial institution may disclose to, or obtain from, your TCP confidential information, such as your mental state, competency, and other medical issues. You must also be willing to let the institution provide complete financial information about your accounts.

Surprisingly, the new rule doesn't require that your TCP be notified of that designation or that the TCP agree to serve. Nor does it describe a TCP's duties and obligations or whether the TCP should be compensated. For those reasons, it makes sense that you should consult with any potential TCP to make sure that person understands what's expected and is willing to serve.

You should also advise your TCP to accept communications from your financial institution. There should also be some understanding of what you expect your TCP to do with any information the institution provides.

If your TCP is a professional advisor, such as your attorney, it might be necessary to discuss compensation. You may also wish to pre-authorize that attorney or advisor to exercise discretion to

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discuss confidential matters with others, such as medical personnel, law enforcement agencies, or adult protection agencies. You may also want to specify which family members the attorney or other advisor may contact and which shouldn't be contacted.

You should probably choose someone younger than yourself because of the risk that the person might also become impaired by the problems of aging. For this reason, your spouse or sibling may not be the best choice. There may be ways to avoid alerting TCPs that their interest was reduced, but those methods are rather complicated and not necessarily foolproof.

You may want to think twice before naming one of your account beneficiaries as the TCP because, if there's a chance that you might later change your mind about that future gift, the institution may alert the TCP that the interest has been reduced or even eliminated, something you may not want divulged to that person. There may be ways to avoid alerting TCPs that their interest was reduced, but those methods are rather complicated and not necessarily foolproof.

WON'T A POWER OF ATTORNEY DO THE JOB?

One question often asked is whether you can protect yourself by using powers of attorney. One short answer is that it's too easy for predators to cancel an existing power of attorney, even a durable one, without ever notifying the current holder of the termination.

Another short answer is that a power of attorney may actually enhance the ability of the predator to steal your funds. Remember that one-sixth of the reported losses are to attorneys-in-fact and other fiduciaries.

Moreover, holders of powers of attorney (often spouses or children) rarely have the time or skill to audit the account effectively on an ongoing basis. Even if they faithfully and skillfully review every statement upon arrival (and even if the person reviewing it is a CPA or attorney), just reviewing monthly statements will be insufficient to discover important changes to the account, like a change of beneficial interests or in the passwords or e-mail addresses, or the creation of a new bank account linked to the investment account.

And if the theft occurs on the first day of the month, discovering it when the monthly statement arrives five or six weeks later may be much too late to be helpful. On the other hand, if you have a TCP, it's at least possible that the financial institution may be able to warn the TCP of such red flags.

THERE ARE STILL RISKS

There is one danger with a TCP that's difficult to avoid: While you may wholeheartedly trust the person you designate to be your TCP, there's a clear possibility that you've been misled into trusting that person. There's also a risk that, while trustworthy today, that

person may become less so later on. Even honest people change, especially as the lure of easy money arises and relationships cool over time.

You will need to make periodic reviews of your designations from time to time to make sure that trust is still warranted, that your TCP is still physically and mentally capable of doing the job, and that the specific designation is still your best choice. But even if, at some future time, you perceive that problems are arising with that relationship, you might still be reluctant to let that person know that you are cancelling his or her designation as a TCP.

There's also the risk that giving that TCP confidential information about you may actually enhance that individual's ability to defraud you. It's for this reason that last year, the Senior Lawyers Division approved the submission to the ABA House of Delegates of a proposal that investors be allowed to designate at least three TCPs, with mandatory notices of red flags to each of them.

In that way, each TCP would discover what the other TCPs are doing, which should go a long way toward eliminating the risk that one of them is misbehaving. For a number of reasons, that proposal was withdrawn. But it may be revised, updated, and resubmitted in the future.

Although FINRA didn't require financial institutions to permit naming more than one TCP, FINRA's official comments on the new rule suggested that letting you name more than one TCP was permissible. But with the sole exception noted above involving an "alternate" TCP, I know of no institution that permits naming more than one TCP. So this risk is still significant. Since the financial institution isn't obligated to warn the TCP of signs of fraudulent activities, there's also a risk that designating a TCP will create a false sense of security.

A last point: One participant in a discussion on TCPs said that if she made a gift to a new romantic interest, she didn't necessarily want the financial institution to alert her children. In effect, she thought that would be none of their business and didn't want them trying to interfere in her very private personal affairs. If that's a real concern, you don't have to use the TCP process or name one of your children as your TCP.

But it raises interesting questions: If a 95-year-old resident of a nursing home names one of the home's workers as a prime beneficiary of an account holding a lifetime of savings, shouldn't someone with that resident's best interests be alerted? And if that 95-year-old resident were your parent, would your answer be different? Those are questions all investors have to decide for themselves.

Author's post-publication update: Some broker-dealers are already soliciting investors in pre-existing accounts. Also, in at least one case I am aware of, it was possible to appoint more than one trusted contact person for the account, though it was not easy.