



**FINANCIAL  
SERVICES  
INSTITUTE**

VOICE OF INDEPENDENT  
FINANCIAL SERVICES  
FIRMS AND INDEPENDENT  
FINANCIAL ADVISORS

## VIA ELECTRONIC MAIL

December 4, 2020

Jennifer Piorko Mitchell  
Office of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington, DC 20006-1506

Re: Regulatory Notice 20-34, Proposed Amendments to FINRA Rule 2165

Dear Ms. Mitchell:

On October 5, 2020, the Financial Industry Regulatory Authority, Inc. (FINRA) published its request for public comment on proposed amendments to FINRA Rule 2165, Financial Exploitation of Specified Adults (Proposed Amendment).<sup>1</sup> The Proposed Amendment seeks to provide additional protections to senior investors from financial exploitation through extending the hold period firms can place on disbursing funds and allowing temporary holds on securities transactions.

The Financial Services Institute<sup>2</sup> (FSI) appreciates the opportunity to comment on this important proposal. FSI supports FINRA's efforts to protect senior investors from financial exploitation and supports FINRA's Proposed Amendment. While the Proposed Amendment provides useful additional tools for firms to employ to protect senior investors from potential instances of financial exploitation, we provide comments below geared toward ensuring that registered representatives and advisors can confidently initiate these measures when they have a reasonable basis to believe there may be potential exploitation without fear that they may subsequently have customer complaints that mar their Form U4. If advisors, and firms, are concerned about adverse consequences from initiating a hold on fund disbursement or a securities transaction, this could have a negative "chilling effect" on the additional safeguards this Proposed Amendment seeks to provide to senior investors. The importance of FINRA's - and the industries'- efforts to safeguard senior and vulnerable investors is only heightened with the isolation many feel as a result of Covid-19 coupled with the increase in bad actors seeking to exploit vulnerable individuals.

In addition, the Proposed Amendment offers an opportunity for FINRA to provide guidance on expectations related to the "internal review" firms should undertake, given that

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<sup>1</sup> FINRA Regulatory Notice 20-34 (Oct. 5, 2020), <https://www.finra.org/sites/default/files/2020-09/Regulatory-Notice-20-34.pdf> (Reg. Notice 20-34).

<sup>2</sup> The Financial Services Institute (FSI) is an advocacy association comprised of members from the independent financial services industry, and is the only organization advocating solely on behalf of independent financial advisors and independent financial services firms. Since 2004, through advocacy, education and public awareness, FSI has been working to create a healthier regulatory environment for these members so they can provide affordable, objective financial advice to hard-working Main Street Americans.

firms routinely report the situation to the appropriate state agency, who initiate their own investigation. FSI also recommends the expansion of the Rule's safe harbor provision.

## **Discussion**

FSI supports the extension of the hold time period for the distribution of funds and the expansion of Rule 2165 to allow holds on securities transactions. While we support the Proposed Amendment, we believe FINRA should better safeguard advisors, and firms, from ill-founded complaints of wrongdoing that could undermine this Rule's full potential to protect senior investors. As FINRA noted, some member firms have declined to use the safe harbor because of "litigation risks associated with placing temporary holds or in evaluating whether a customer is being financially exploited."<sup>3</sup> While the expansion of this Rule to securities transactions is positive, it also heightens potential risk for those who choose to place a hold – a decision no advisor or firm takes lightly. FINRA should also provide additional guidance concerning its expectations relating to a firm's internal review of the facts and circumstances surrounding the potential financial exploitation. Generally, firms promptly report the financial exploitation to the appropriate state agency and that agency, who has specialized knowledge, initiates its own investigation. Firms cooperate with state agencies, but do not want to interfere with their investigation, especially in instances where a criminal investigation is initiated. These concerns are discussed below.

### **I. FINRA's Proposed Expansion of the Hold Time and Extension of Holds to Securities Transactions Promotes Investor Protection and FINRA should take Additional Steps to Ensure Advisors Feel Secure Using Rule 2165 to Maximize the Proposed Amendment's Effectiveness**

#### **A. Introduction**

The Proposed Amendment includes two main changes: 1) it expands the coverage of Rule 2165 to allow a temporary hold on securities transactions; and 2) it extends the time period for temporary holds for up to 30 additional business days, provided that the member's internal review of the facts and circumstances supports the member's reasonable belief that the financial exploitation has occurred, is occurring, has been attempted, or will be attempted and the member has reported their reasonable belief to a state regulator or agency of competent jurisdiction or a court of competent jurisdiction. Rule 2165 would maintain its record retention requirements and "safe harbor" provision, with modification to cover securities transactions.<sup>4</sup>

FSI believes that both changes will enhance investor protection for the reasons outlined by FINRA in Reg. Notice 20-34. FSI applauds FINRA for its ongoing focus on protection of senior investors and vulnerable adults. Recently, the importance of this focus has become amplified because of the increase in fraud associated with bad actors during the Covid-19 crisis.<sup>5</sup> Many of

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<sup>3</sup> Reg. Notice 20-34, at n.12.

<sup>4</sup> FINRA Rule 2165.01 Applicability of Rule. This Rule provides members and their associated persons with a safe harbor from FINRA Rules 2010, 2150 and 11870 when members exercise discretion in placing temporary holds on disbursements of funds or securities from the Accounts of Specified Adults or transactions in securities in the Accounts of Specified Adults consistent with the requirements of this Rule. This Rule does not require members to place temporary holds on disbursements of funds or securities from the Accounts of Specified Adults or transactions in securities in the Accounts of Specified Adults.

<sup>5</sup> See e.g., Seniors face increased risk for financial exploitation associated with COVID-19, Investment News (Apr. 6, 2020), <https://www.investmentnews.com/seniors-face-increased-risk-financial-exploitation-covid-19-191081>; Sadie

the risk factors that make senior investors vulnerable, including isolation, but also fear, are much more prevalent because of the pandemic.<sup>6</sup> A longtime, trusted advisor may serve as a main point of contact for a senior investor and, given that many advisors have long-term relationships with their clients, the advisor may be well positioned to identify instances of financial exploitation.

FSI does suggest additional modifications below for FINRA's consideration, which are based on ensuring that advisors are confident that there will not be negative consequences from flagging instances of possible financial exploitation. Our comments are geared toward ensuring that FINRA Rule 2165 is best positioned to be used to the maximum extent possible.

B. FINRA Should Develop Mechanisms to Ensure that Advisors Are Not Subject to Unfounded Customer Complaints When They Appropriately Use Rule 2165 to Safeguard Investors

FSI is concerned that advisors, acting in good faith and out of concern for a client, could be negatively impacted should a customer (his agents or heirs) complain after-the-fact. If advisors (and firms) perceive possible negative consequences, they may be less likely to flag potential concerns. This may limit, over time, the effectiveness of this Rule and the Proposed Amendment's goal to better protect senior investors. FSI members are cognizant that the placement of a hold should not be taken lightly, but advisors and firms should not feel deterred from placing a hold when appropriate – even in instances where there is a reasonable belief of potential exploitation that later proves not to bear out.

Given the Proposed Amendment's expansion to securities transactions the possibility for after-the-fact dissatisfaction increases. For example, an advisor may identify indications of possible financial exploitation that provide a reasonable basis for the firm to place a hold on a securities transaction. Additional information later shows that the initial causes for concern, while reasonable, were not problematic and the hold on a securities transaction is released. During the hold, the market moves in a direction adverse to the client's interests – the stock price of the security the client wanted to sell declines substantially based on negative news. The client is upset by the delay and files a complaint against his advisor; it is reportable on the advisor's Form U4. Based on these types of scenarios, firms also may experience greater litigation risk.

As FINRA outlined in Reg. Notice 20-34, Form U4 and Form U5 are “public facing” and based on the allegation-based nature of the complaint process, an advisor could be subject to a complaint related to a hold even when the advisor acted in good faith and had a reasonable basis for an initial determination for a hold. FINRA summarized that firm survey results indicated certain challenges, more generally, associated with customers not believing that they were being financially exploited – detecting red flags of potential exploitation can be nuanced and most seniors do not want to believe they are victims. To make this Rule as effective as possible, FINRA should consider additional protections for advisors so they can confidently act when there is possible exploitation that could have long-term negative consequences on a client's financial future and overall well-being. Otherwise, an advisor is left to defend his or her reputation and, as FINRA knows, advisors take all disclosable events very seriously. In fact, advisors don't have unilateral authority, without their firms, to place holds on customers. Yet, customer complaints

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Gurman, Coronavirus Creates an Epidemic of Scams, WSJ (March 30, 2020),

<https://www.wsj.com/articles/coronavirus-creates-an-epidemic-of-scams-11585601885>

<sup>6</sup> See e.g., Grace Smith and Ashley Hunter, Elder abuse is spiraling in age of COVID-19, Tennessean (June 14, 2020)

<https://www.tennessean.com/story/opinion/2020/06/14/elder-abuse-spiraling-coronavirus-fifty-forward/3175138001/>

included on an advisor's U4 may make the advisor appear as though he or she engaged in malfeasance, misfeasance, or serious wrongdoing when, in fact, the advisor took appropriate steps to protect a long-time client – these types of unintended consequences should be avoided.

While FINRA notes “[t]o date, based on FINRA’s review of reported complaints, member firms have not reported a complaint on Forms U4 or U5 or pursuant to Rule 4530 related to placing a temporary hold pursuant to Rule 2165,” the expansion to securities transactions, and extension of the hold period, under the Proposed Amendment increase the likelihood of complaints associated with holds placed in accordance with FINRA Rule 2165. Securities transaction holds introduce a new risk related to the possibility of negative market movements. The extreme market volatility of this past year evidences this risk and economic downturns are often associated with an increase in financial fraud and exploitation. In addition, without a clear problem-code or tracking mechanism tied to Rule 2165 it may be difficult to easily identify complaints that stem from a hold, but are submitted based on claims of conversion, unauthorized trading, failure to follow a customer’s instructions or best-execution-like concerns.

### C. Suggested Changes

As discussed above, a hold could make an investor believe that his advisor (or firm) failed to meet certain obligations especially if there is an adverse stock price movement during a hold. Resulting complaints or litigation may result in a “chilling effect” on initiating holds. FINRA could consider a variety of mechanisms to try to minimize these issues and ensure that the concerns outlined above do not inadvertently undercut the intent of the Proposed Amendment – to protect senior investors. We have included a few suggestions below:

- *FINRA Review Process for Rule 2165-Related Customer Complaints:* While FINRA has indicated that it does not want to “limit a customer’s right to submit a complaint,” Rule 2165’s record retention requirements would make FINRA review of any related customer complaints expeditious. If the complaint is tied to a properly issued hold, FINRA could consider removing the complaint or affixing a code or link to Rule 2165 to alert the public, but also other regulators that use Forms U4 and U5, that the complaint is associated with a hold placed under FINRA Rule 2165. This process would not be overly burdensome for FINRA and it would be fair to the advisor as well as helpful to the public and other regulators who rely on Forms U4 and U5.
- *Waive Expungement Fees:* Should an advisor seek to expunge an erroneous or inaccurate customer complaint stemming from a properly placed Rule 2165 hold, the advisor is left bearing the cost of what is an increasingly expensive expungement process. FINRA could waive expungement fees associated with FINRA Rule 2165 complaints.

We appreciate FINRA’s willingness to “reconsider this issue or develop a specified problem code for reporting any Rule 2165-related complaint to FINRA pursuant to FINRA Rule 4530 if complaints are reported in the future and they appear to have a detrimental impact on the protection of seniors and other vulnerable adults,” but believe steps taken now to address these identified unintended negative consequences will more promptly reduce any detrimental impact. This is of particular importance given the Proposed Amendment’s expansion to holds for securities transactions. More generally, the pressing importance of protecting senior investors from financial exploitation supports taking affirmative steps now so that Rule 2165 is as effective as possible to prevent the devastating consequences that result from financial exploitation.

## II. **FINRA Should Consider Providing Additional Guidance on Firms' Internal Review Obligations and Expand Rule 2165's Safe Harbor**

### A. Additional Guidance on FINRA's Expectations for the Rule's Internal Review Requirement Would Assist Firms Using this Rule to Protect Senior Investors

In identified cases of potential financial exploitation, especially ones that involve possible criminal conduct, it is routine practice for firms to promptly report the situation to the appropriate agency, usually adult protective services (APS) and/or law enforcement. These agencies have the appropriate expertise to conduct these types of investigations and firms work cooperatively to provide them requested information. As outlined above, frequently, when a firm places a hold on an account, the client is upset – not wanting to believe that a new acquaintance or family member is trying to take advantage of him or her – and he or she can be uncooperative in providing additional information. Firms have access to internal records that evidence the client's regular trading and account disbursement activity, but firms do not want to, for example, front-run and jeopardize a criminal investigation by trying to contact and interview witnesses. Firms who seek to protect clients and use Rule 2165's safe harbor would benefit from additional guidance outlining FINRA's expectations as to the scope and nature of the "internal review" identified in the Rule.

### B. FINRA Should Expand the Application of Rule 2165's Safe Harbor

FINRA should expand the application of the safe harbor provided by FINRA Rule 2165.01 to cover both FINRA Rule 3260 (Discretionary Accounts)<sup>7</sup> and FINRA Rule 5310.01 (Execution of Marketable Customer Orders)<sup>8</sup> because of the Proposed Amendment's expansion to securities transactions. If an advisor does not have time or price discretion, and a client submits a market order to sell, for example, an advisor is obligated to follow the client's instructions and also execute (or take steps to execute) the marketable order "fully and promptly." Placing a hold on a securities transaction could implicate these two rules.

## **Conclusion**

We are committed to constructive engagement in the regulatory process and welcome the opportunity to work with FINRA on this and other important regulatory efforts.

Thank you for considering FSI's comments. Should you have any questions, please contact me at [Redacted]

Respectfully submitted,



Vice President, Regulatory Affairs & Associate General Counsel

<sup>7</sup> FINRA Rule 3260(b) (Authorization and Acceptance of Account) states "No member or registered representative shall exercise any discretionary power in a customer's account unless such customer has given prior written authorization to a stated individual or individuals and the account has been accepted by the member, as evidenced in writing by the member or the partner, officer or manager, duly designated by the member, in accordance with Rule 3110."

<sup>8</sup> FINRA Rule 5310.01 states "[a] member must make every effort to execute a marketable customer order that it receives fully and promptly."