

# Deputizing Financial Institutions to Fight Elder Abuse

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# Motivation

## ▶ Are financial professionals effective monitors?

- ▶ Financial professionals often called upon to monitor for crimes and misbehaviors in societies
- ▶ E.g., money laundering, fraud, terrorism financing
- ▶ Is this an important contribution of finance to society ([Zingales, 2015](#))?

## ▶ Laws are often permissive

- ▶ No explicit carrots or sticks
- ▶ Scale of assignment is too large to reward everyone
- ▶ Problems are often insidious, so it is difficult to hold professionals culpable for not detecting problems

## Deputization as a regulatory design

*Deputization occurs when a principal empowers an agent to carry out a monitoring function without providing explicit incentives.*

## Deputization is Common

- ▶ Individuals are called upon to report suspicious activities at airports and to report the abuse of minors
- ▶ Corporate lawyers witnessing violations of securities laws may (but do not have to) report to the SEC
- ▶ UPS and FedEx identify suspicious packages associated with drug trafficking
- ▶ Facebook and Google assist in flagging communications suspicious of terrorism

## How Successful is Deputization?

- ▶ **Question:** What is the economic and social value of financial professionals as monitors/deputies?
- ▶ **Unclear:** Permissive with no rewards or punishments
  - ▶ In classical agency models, agents must be incentivized to act (e.g. Ross 1973, Jensen and Meckling 1976, Harris and Raviv 1979, and Hölmstrom 1979)
  - ▶ The success of deputization depends on other extrinsic or intrinsic motivations
- ▶ **Difficult to answer:** Not implemented for exogenous reasons
- ▶ **Little is known:** Because large scale, quasi-natural experiments are rare

## Elder financial abuse

*The “improper use of an older adult’s funds, property, or assets”*

- ▶ **Pervasive:** \$21.8 billion in elder financial abuse from 2013-2019 (U.S. Department of Treasury)
- ▶ **Growing** problem as elderly grow from 15.2% to 23.4% of total population in next 40 years
- ▶ **Devastating:** Average theft by family members is 28% of victim’s net worth, excluding home equity

## Financial abuse of the elderly

- ▶ **Pernicious:** difficult to police
  - ▶ Victims are isolated
  - ▶ Mental and physical decline
  - ▶ Perpetrators often family members and caregivers

<b>Suspect Category</b>	<b>Frequency<sup>1</sup></b>	<b>Average (Median) Loss</b>
Stranger	51%	\$17,000 (\$8,500)
Family	25%	\$42,700 (\$24,900)
Fiduciary	7%	\$83,600 (\$33,800)
Non-family caregiver	4%	\$57,800 (\$21,800)

**Table:** Frequency and Financial Loss by Suspect Category (Source: CFPB 2019)

<sup>1</sup>The frequencies do not add up to 100% because approximately 13 percent of reports do not provide enough information to determine the relationship of the suspect to the targeted older adult.

# Our Identification: Staggered Adoption of Rule Changes

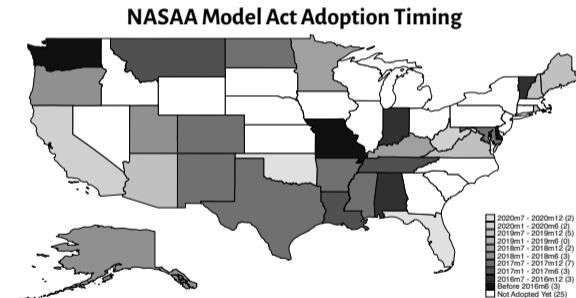
## ▶ NASAA “Model Act”

- ▶ Staggered adoption across 30 states by 2020
- ▶ Applies to advisers, brokers, and (in 5 states) all financial employees

## ▶ Financial professionals can now

1. **Reach out to trusted contacts**
2. **Halt suspicious disbursements**

- ▶ The laws **create no obligations**, and give **no rewards or penalties**





## The New Authorities

### ▶ Halt Suspicious Disbursement

- ▶ May delay a disbursement for 15-25 days if reasonably believe financial exploitation is occurring
- ▶ If delaying a disbursement, an investigation must be initiated and the results must be provided to the state securities division and Adult Protective Services
- ▶ Jim Wrona, vice president and associate general counsel at FINRA, gave the following example:  
*A client will say, "I won the lottery, but I need to pay the taxes upfront before I can claim the award." If the client demands the money even after the broker has explained that it's a scam, he or she can then temporarily pause the disbursement and investigate further.*
- ▶ In conversation with us, the head of Alabama's securities division stated that nine out of ten cases are handled by reaching out to a trusted contact and using the ability to halt a disbursement as a deterrent
- ▶ Imaginably costly: Conducting the investigation takes time (e.g., providing documentation to investigators)

## The New Authorities

- ▶ Trusted Contact System
  - ▶ Before Model Act, unable to reach out due to privacy laws
  - ▶ Unable to view account information (contrasts with Power of Attorney)
  - ▶ While financial institutions have been permitted to disclose consumer information to appropriate regulators in the event of elder financial exploitation since the Graham-Leach-Bliley Act of 1999, these recent rule changes newly allow discussing issues with a trusted contact and also provide clear protections from lawsuits connected to such disclosures
  - ▶ Ex. Widowed elderly man requests a large sum of money for a new long-distance relationship. He has never met this person. A likely “romance” scam. A financial professional may contact the son/daughter, who then reason with the elderly man and often disrupt the request

## Main Findings

- ▶ **Deputization led to a 9% reduction in reports of elder financial abuse by the end of the first year (3% of a standard deviation)**
- ▶ **Deputization also led to a 3.9% reduction in financial crimes against the elderly by the end of the first year (3% of a standard deviation)**
  - ▶ Larger effect for high value crimes
  - ▶ Larger effect for people older than 65 compared to those of age 50-64
- ▶ **Substantial heterogeneity across financial professionals**
  - ▶ Advisers affect outcomes, whereas brokers tend not to cause any change
  - ▶ Larger effect when advisers serve wealthier clients
- ▶ **Weaker effect when there are other safeguards in place**
  - ▶ Weaker effect in more socially connected communities

## Data

- ▶ **County-month counts of elder financial exploitation:** U.S. Department of Treasury's Financial Crimes Enforcement Network Suspicious Activity Report
  - ▶ Reports elder financial exploitation as an individual category since April 2012
  - ▶ Our sample: 2014 - 2020
- ▶ **State-month counts of financial crimes against the elderly:** Federal Bureau of Investigation (NIBRS database)
- ▶ **Adoption dates of elder financial protection laws:** state legislature websites
- ▶ **Location and employment history of advisers:** SEC Investment Advisor Public Disclosure (IAPD)
- ▶ **Location and employment history of brokers:** FINRA BrokerCheck
- ▶ **Social connectedness measures:** Facebook Social Connectedness Index and U.S. Religion Census
- ▶ **Adviser compensation structure:** SEC Form ADV (FOIA)
- ▶ **County demographic characteristics:** U.S. Census

## Dynamic Difference-in-Differences Specification

- ▶ We estimate staggered difference-in-difference models of the following form:

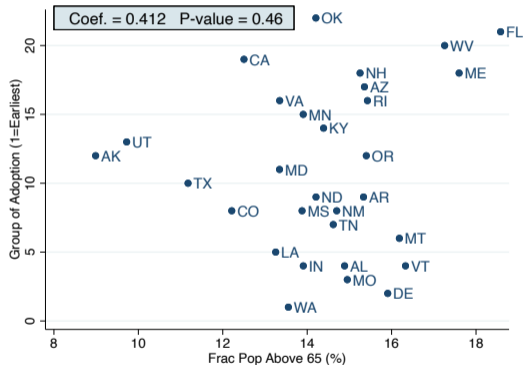
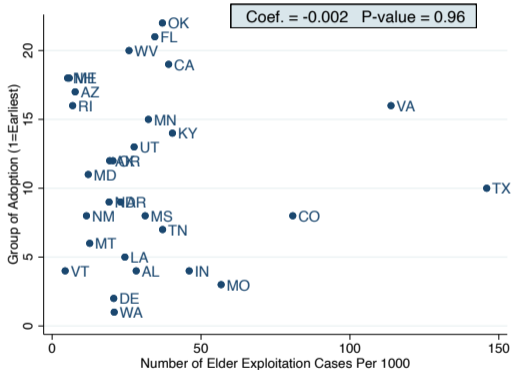
$$OUTCOME_{ct} = \alpha + \beta_h \mathbb{1}(t - \text{Treatment Date}_s = h) + \gamma' \mathbf{X}_{ct} + \eta_c + \eta_t + \epsilon_{ct} \quad (1)$$

- ▶  $c$  denotes county,  $s$  denotes state,  $t$  denotes month,  $h$  denotes event time
- ▶  $\mathbf{X}_{ct}$ : log (pop above 65), % male, % married, income, average age, credit score, debt-to-income ratio, % subprime, % with bachelor's degree or higher
- ▶ Standard errors double clustered at the **state** and **month** levels

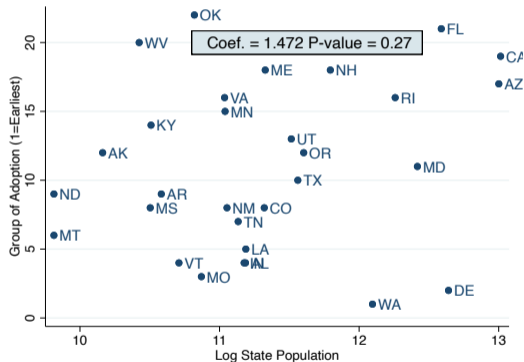
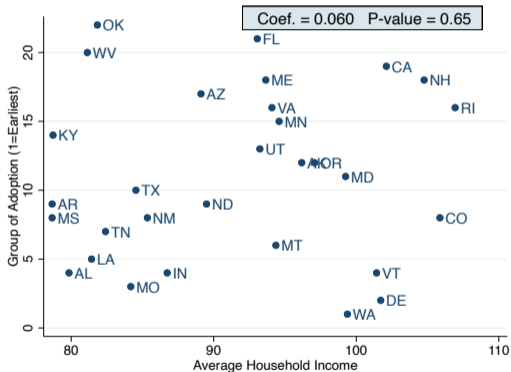
## Outcomes

- ▶ **# of Trusted Party Contacts and Halts:** An analysis of these actions may mischaracterize the effectiveness of deputization because the ability to halt disbursements and reach out to trusted contacts interacts with other hidden actions that are helpful in curbing abuse.
  - ▶ Ex. Financial professionals may deter exploitation when they roll out a trusted contact system and communicate with clients and potential perpetrators the new safeguards. Such hidden actions prevent egregious activity before it is attempted, eliminating the need to make reports to regulatory agencies.
- ▶ Also, data on halting activity is fraught with error because documentation is often incomplete or unavailable.
- ▶ **Reports of suspicious activity and actual crimes:** The observable equilibrium outcome that best captures the deterrent role of deputization is the frequency of elder abuse cases.

# Do state characteristics predict the timing of adoption?



# Do state characteristics predict the timing of adoption (cont'd)?





## Group of Adoption (1 = Earliest)

	(1)	(2)	(3)	(4)
Number of Elder Exploitation Cases Per 1000	-10.067 (6.835)			-4.110 (12.084)
Fraction of Population 65+		0.412 (0.551)		0.760 (0.996)
Log State Population			0.984 (1.090)	-0.155 (1.845)
Average Credit Score 65+				-0.331 (1.047)
Subprime 65+				-46.301 (223.770)
Low Income 65+				37.592 (126.308)
Age 65+				2.706 (3.342)
Male 65+				1.075 (2.232)
Married 65+				0.133 (0.700)
Average Household Income 65+				0.533 (0.604)
Debt-to-Income 65+				0.556 (4.696)
Bachelor or Higher 65+				-18.217 (74.895)
R <sup>2</sup>	0.07	0.02	0.03	0.27
# States	30	30	30	30

# Ever Adopt?

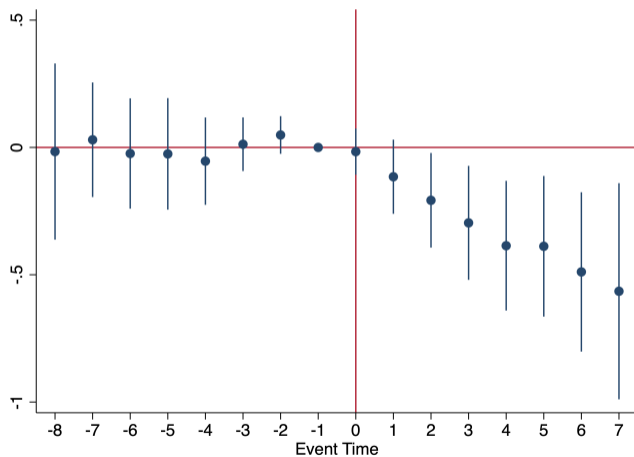
	(1)	(2)	(3)	(4)
Number of Elder Exploitation Cases Per 1000	0.595 (0.554)			0.262 (0.732)
Fraction of Population 65+		0.001 (0.041)		0.021 (0.064)
Log State Population			-0.033 (0.068)	0.030 (0.092)
Average Household Income 65+				-0.035 (0.028)
Average Credit Score 65+				-0.042 (0.057)
Subprime 65+				-10.592 (12.972)
Low Income 65+				-5.272 (6.445)
Age 65+				-0.150 (0.210)
Male 65+				-0.036 (0.135)
Married 65+				-0.003 (0.035)
Debt-to-Income 65+				0.050 (0.240)
Bachelor or Higher 65+				0.331 (3.427)
R <sup>2</sup>	0.02	0.00	0.00	0.16
# States	51	51	51	51

## We predict a drop in reported cases for several reasons:

1. Reporting requirements to FinCEN for financial professionals did not change
  - ▶ However, adoption could increase awareness of elder abuse and increase reporting, working against our finding a drop
2. Abuse above \$5,000 must be reported. The new authorities may allow financial professionals to stop abuse faster, reducing the number of cases reaching the \$5,000 threshold
3. Family members and other perpetrators may learn in conversations with advisors or when enrolling in trusted contact systems about the new protections on the account, which alters the perceived riskiness of fraud and deters them from attempting abuse

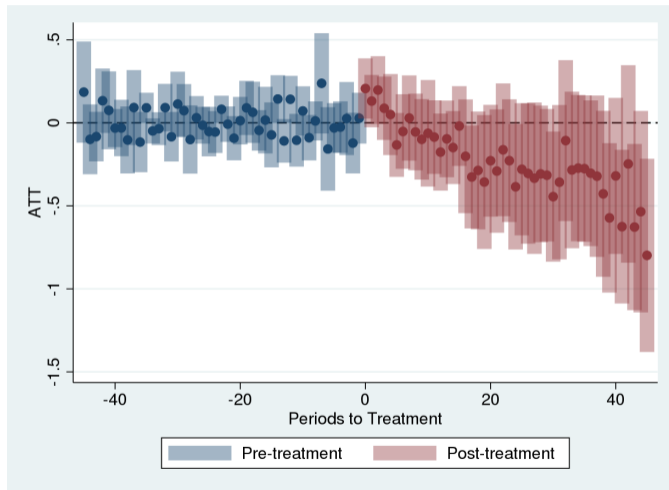
## Dynamic Difference-in-Differences Results

- ▶  $Y$  = # Elder Financial Exploitation Cases in a county month
- ▶  $X$  = Six Month Intervals (Monthly regression)
- ▶ No violation of pre-trends
- ▶ Roughly 9% in reported abuse cases at 1 year. Growing decline after implementation
- ▶ Robust to  $\ln(1+Y)$ ,  $Y/(\text{Pop. } 65+)$ , and Poisson specification
- ▶ Robust to using cases involving fund transfers
- ▶ Deterrent effect unlikely in isolation due to persistence



# Callaway and Sant'Anna (2021) Decomposition

- ▶ Estimation uses never-treated states as controls
- ▶ Compares all pairs of treated (30) and never-treated states (20) and takes an average over time.
- ▶ x-axis in months, y-axis county-month count

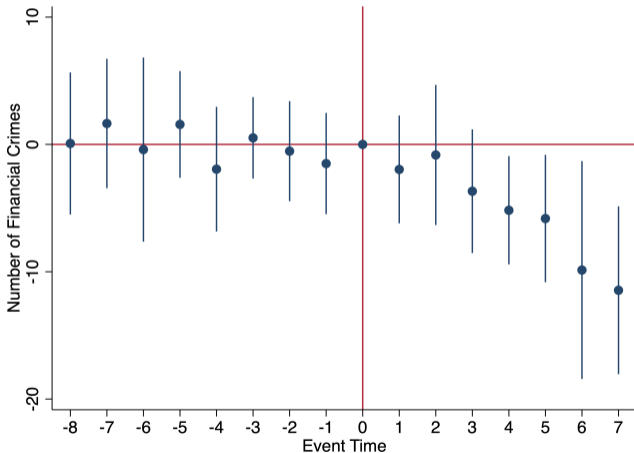


## Drop in reports versus drop in crime:

1. Could quality of monitoring account for decrease in reports
2. Perhaps, reaching out to trusted contacts allowed financial professionals to make sure whether malfeasance is taking place.
3. So, less need for reporting.
4. Data on actual crimes from FBI valuable

# Using data from the FBI

- ▶  $Y = \#$  financial crimes against the elderly in a state-month
- ▶  $X =$  Six Month Intervals (Monthly regression)
- ▶ No violation of pre-trends
- ▶ Growing decline after implementation



## Does the effect vary with the presence of financial professionals?

	# Elder Financial Exploitation Cases			
	(1)	(2)	(3)	(4)
Post	-0.130 (0.089)	-0.114 (0.094)	-0.139 (0.090)	-0.132 (0.090)
Post × Investment Advisers per Capita	-0.888*** (0.140)		-0.578** (0.242)	-0.750*** (0.155)
Post × Brokers per Capita		-0.841*** (0.150)	-0.337 (0.251)	
Post × Pure Brokers per Capita				-0.183 (0.153)
Year-Month FE	Yes	Yes	Yes	Yes
County FE	Yes	Yes	Yes	Yes
County-Linear Trend	Yes	Yes	Yes	Yes
Interacted Controls	Yes	Yes	Yes	Yes
Adjusted R <sup>2</sup>	0.69	0.68	0.69	0.69
# Counties	3139	3139	3139	3139
Observations	245169	245169	245169	245169



## Social Incentives: Substitutes for regulatory interventions?

	# Elder Financial Exploitation Cases				
	(1)	(2)	(3)	(4)	(5)
Post	-0.106 (0.106)	-0.092 (0.102)	-0.074 (0.113)	-0.206** (0.091)	-0.198** (0.090)
Post × Investment Advisers per Capita	-0.890*** (0.152)	-0.791*** (0.156)	-0.982*** (0.172)	-0.995*** (0.159)	-0.796*** (0.139)
Post × Social Connectedness Index	1.031*** (0.185)				
Post × Congregations Per 1000		0.975*** (0.153)			1.303*** (0.186)
Post × Adherents Per 1000			0.223** (0.087)		-0.297** (0.129)
Post × Social Capital Index				0.512*** (0.117)	0.391*** (0.115)
Year-Month FE	Yes	Yes	Yes	Yes	Yes
County FE	Yes	Yes	Yes	Yes	Yes
County-Linear Trend	Yes	Yes	Yes	Yes	Yes
Interacted Controls	Yes	Yes	Yes	Yes	Yes
Adjusted R <sup>2</sup>	0.67	0.67	0.67	0.68	0.68
# Counties	3135	3139	3139	2990	2987
Observations	244887	245169	245169	232985	232787

## Other robustness and placebo tests

- ▶ Minimum distance matching on observables
- ▶ Collapse at state-month or county-year panel (reduce sparsity)
- ▶ Dropping any state and re-estimate specification
- ▶ Start/end sample in different years
- ▶ No effect on abuse involving money services businesses
- ▶ No effect for unrelated financial crime categories
- ▶ Survives controlling for less-affected elder financial exploitation cases (e.g., money service businesses, credit cards)

## Conclusion

- ▶ While financial professionals are often called upon to monitor for crimes and misbehavior in societies, there is little evidence that they are effective monitors
- ▶ We use a quasi-natural experiment to study this topic, in the setting of fighting elder abuse
- ▶ It was unclear whether deputizing financial professionals would be effective in curbing elder abuse. The new rules did not include penalties or monetary incentives, but instead relied on existing social or market mechanisms.
- ▶ Deputization was successful, and its success is likely a *lower* bound given the predatory nature of the financial industry