

Financial Elder-Abuse Law Harms Victims It Should Protect

By Michael A.S. Newman

Political autocrats, Leo Tolstoy observed, invariably comfort themselves on grounds that their acts of oppression are justified in the name of "le bien public:" the hypothetical welfare of other people. The more tyrannical the autocrat, the more likely he is to believe he knows where the public welfare lies, and the more certain he is in such knowledge. Witness the ideologically motivated butchery perpetrated by authoritarian regimes from the French Revolution to the present day.

Of course, uncertainty about the public welfare is not a trait we value in elected representatives. We elect those — as we must — whom we believe to have a clear and correct idea of where the public good lies. But legislators, even elected ones, should be very careful that, in acting to correct a perceived evil, they do not persecute the innocent and guilty alike or, worse still, harm the very victims they try to protect.

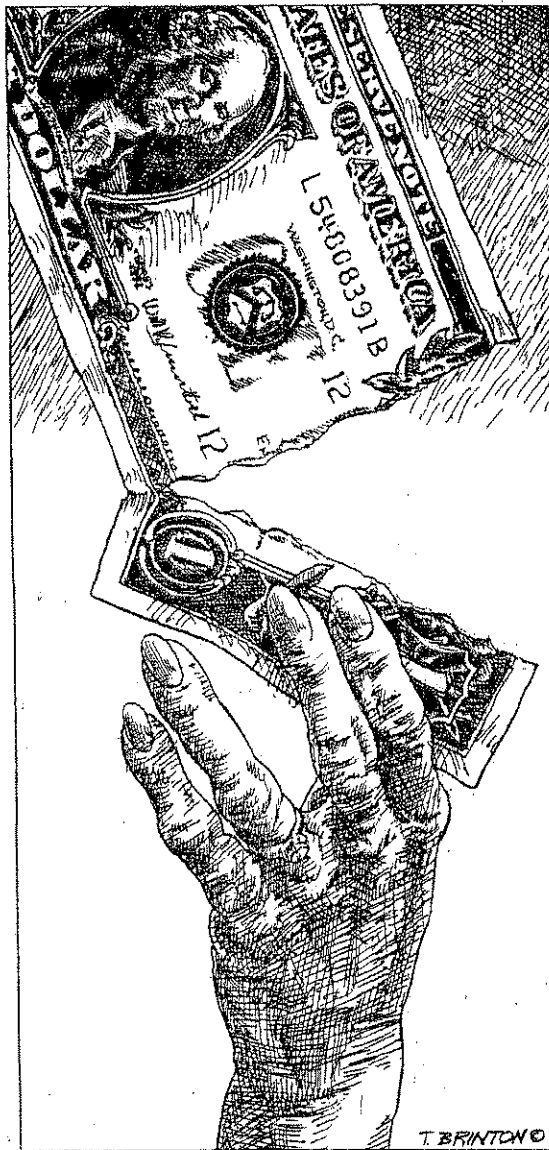
The cliché that "the road to hell is paved with good intentions" applies with surprising cogency to the acts of legislators; when it comes to laws promulgated in a democracy, all roads to hell are so paved.

A case in point is the state's "financial elder abuse" law, which, through the imposition of criminal and civil penalties, punishes those who take economic advantage of seniors. The obvious targets of this law are the out-and-out con artists, such as the caretaker who takes advantage of an elder ward's mental weakness to embezzle his or her life savings, or the huckster who sells the senior citizen a nonexistent product, counting on the senility of the victim to shield him or her from detection.

However, in trying to eradicate the alleged financial abuses of con men and women who prey on the elderly, the state Legislature has drawn a net so wide as to catch those legitimately selling investment products to senior citizens.

The devil is in the details. The financial elder-abuse law, like many laws aimed at curbing purportedly harmful business practices, is vague in describing exactly what it prohibits. The law prohibits "financial elder abuse," which it defines as occurring "when a person or entity" takes or keeps "real or personal property of an elder [that is, a person 65 or older] ... to a wrongful use or with intent to defraud, or both." A "wrongful use" is deemed to occur where there is "bad faith."

The statute defines "bad faith" as occurring where the defendant "should have known" that the elder had a right to have the property transferred to him or her or made readily available. And a defendant "should have known" of such a right if it is "obvious" to a "reasonable person" that the elder had such a right. Thus, having retreated fruitlessly through this unsatisfactory series of terms, each term regressively defined by another undefined term, the statute finally settles on that old war horse of common-law tort, the "reasonable person" standard.



The crucial question of what constitutes "wrongful use" where there is no fraud is relegated to the black box of the jury room. Financial elder abuse, in effect, is in the eye of the beholder.

With such loose boundaries, the scope of the financial elder abuse statute has inevitably expanded. In its latest mutation, the elder-abuse law has become the means for targeting the sale of "unsuitable" investments to seniors. Here, where the statute is used to protect seniors from unwise, bad and unsuccessful investments — and to punish the sellers of those products — the slippery slope on which this law precariously sits begins to slant to the near-vertical.

For example, state courts have seen numerous lawsuits attacking the sale of "unsuitable" annuities to elders. Annuities are tax-deferred investment vehicles sold by insurance companies. They are attractive investments for senior citizens because they provide a high level of security, and elders are the chief purchasers of annuities.

Many annuities have long maturity periods — 10 or even 15 years — which, some plaintiffs' attorneys claim, are unsuitable for seniors who likely will not live to enjoy the benefits of maturity. This ignores the fact that the suitability of the investment depends on the goals of the investor. An elder reasonably may wish to preserve the principal of a sum of money and gain interest, only for the sake of providing for heirs after he or she dies.

In that case, a long maturity period does not render the investment "bad," because the elder never intended to draw down the investment.

Another accusation leveled at the sellers of annuities is that they encourage elders to give up their current annuities to purchase new annuities, causing the investors to incur penalties for withdrawing their money before maturity of the original annuity. In November 2003, a Los Angeles man was sentenced to six years in prison for repeatedly selling and reselling new annuities to the same people in a very short time, collecting thousands of dollars in commissions and costing his elderly clients hundreds of thousands of dollars in penalties. Such extreme cases aside, there are certainly many conceivable circumstances under which a senior rationally may choose to incur a surrender charge. A senior may exchange a low-yield annuity for one indexed to the stock market, which has the possibility of creating substantial gain.

Myriad other reasons, having to do with the desires and goals of the individual investor, may make an annuity, even one with a long maturity period or involving the payment of a penalty, a reasonable investment for an elder.

Nevertheless, the state Legislature has acted to prevent the sale of what it considers "unnecessary replacement" annuities. At the beginning of 2004, it amended the Insurance Code, making it a violation of the law for an agent or insurance company to even "recommend" that an insured 65 years or older purchase an "unnecessary replacement annuity." The statute defines an "unnecessary replacement" as "the sale of an annuity to replace an existing annuity that requires the insured to pay a surrender charge" for the earlier annuity where such replacement "does not confer a substantial benefit over the life of the policy to the purchaser so that a reasonable person would believe that the purchase is unnecessary."

As with the original elder-abuse statute, this law sets forth no clear definition of what constitutes an "unnecessary replacement." What does it mean for a replacement to confer a "substantial benefit" from the point of view of a "reasonable person?" Once again, the Legislature, unable to provide clear guidelines but eager to punish those whom it perceives to be wrongdoers, has punted all difficult questions into the jury room.

The law steps onto shaky ground when it asks juries to decide what constitutes a "suitable" investment, or one that confers a "substantial benefit." The question that should be asked is not whether an annuity or other investment vehicle is a good or a bad investment for an elder adult (experts indeed disagree on the issue of whether an annuity is the best kind of investment, as experts disagree about the utility of many investment vehicles). The proper question, rather, is whether juries should be deciding that a given investment is "unsuitable."

Investments are inherently risky. The elder-abuse law and provisions like the recent additions to the Insurance Code make every sale to an older adult a possible source of lawsuit. Businesses selling investment vehicles are at a natural disadvantage in courts when sued by their elderly clients. A hapless elderly woman who has lost a substantial portion of her savings in an unsuccessful investment makes an extremely compelling plaintiff. Whether or not the company selling the investment did anything wrong, there is a substantial risk, on the aggregate, that juries will effect rough justice on behalf of such plaintiffs and award damages against such companies. With a statutory scheme that basically leaves the definition of wrong-doing up to the jury, such a result is still more likely.

If lawsuits punishing the sale of unsuitable investments continue, the biggest losers will not be the sellers of investment vehicles; they, after all, have other customers. The biggest losers will be those age 65 and older, the very group that the financial elder-abuse law is ostensibly meant to protect.

Lawsuits arising from failed investments will have a chilling effect on the sale of investment vehicles to elders. Businesses will be more likely to stop selling useful investment products to senior citizens for fear of being subject to civil and criminal penalties. In such a situation, senior citizens will be left with fewer choices and a narrower range of products in which to invest their funds.

The apprehension that litigation will restrict choice in the marketplace should be taken seriously. This year, the world is suffering a severe shortage of flu vaccines in part because the threat of lawsuits has discouraged pharmaceutical companies from manufacturing them, leaving the world with only two such manufacturers. Even John Kerry, whose running mate is a well-known plaintiffs' trial lawyer, could not help but acknowledge in the presidential debates that the rising cost of health care is related to increased medical liability litigation (though he tried to minimize its perceived effect).

There is good reason to believe that the threat of lawsuits likewise will depress the availability of investment vehicles for investors older than 65. In the face of continuous suits, litigation-averse businesses simply will abandon the senior market.

Those trying to further the public welfare through the prevention of "unsuitable" investments should therefore ask themselves an important question. If, in aiming to eradicate "elder abuse" the Legislature in fact hinders the choices and possibilities available to the elderly, is the "le bien public" really being served?

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