Position Paper for Senate Bill 662 Creating Florida Statutes Section 517.34

Introduction

Proposed section 517.34, Florida Statutes, is a watered-down version of FINRA Rule 2165, which will be effective on February 5, 2018. Both the FINRA rule and section 517.34 are intended to provide safe harbors to "dealers" and "investment advisers", as those terms are defined in section 517.021, Florida Statutes. FINRA Rule 2165's history is discussed in FINRA Regulatory Notice 17-11. One example of how section 517.34 provides even less protection to vulnerable adults than FINRA Rule 2165 is the fact that the FINRA rule only applies to "disbursements" of funds or securities. Section 517.34, on the other hand, allows dealers and investment advisers to place holds on any "transaction", an undefined term. The use of the word "transaction" provides an even greater safe harbor, allowing the financial services industry to place holds on purchases, sales, redemptions, checks, credit card charges, etc. Even FINRA chooses not to provide such a broad safe harbor for its member firms.

Proposed section 517.34 also conflicts with already established Florida law, reducing the protections already in place for vulnerable adults, at the same time increasing the burden on the Department of Children & Families Adult Protective Services with no additional benefit to those it serves, and provides no regulatory mechanism for state regulators to monitor this legislation to be sure it is not used to harm vulnerable adults.

Position

In its current form, this bill is opposed. Changes could be made to this bill to make it more protective and to remove conflicts with Florida Law.

An easier and more comprehensive way to address the concerns this legislation purports to address would be to amend Florida Statutes Chapter 415 to include securities dealers, investment advisors, and associated persons and allow them to temporarily freeze disbursements when an Adult Protective Services report is made.

Securities Dealers, Investment Advisors, and Associated Persons Are Already Mandatory Reporters When They Suspect Exploitation

Proposed section 517.34(2)(a) is unnecessary and in conflict with Chapter 415, Florida Statutes. Section 415.1034(1) requires "any person" in Florida "who knows, or has reasonable cause to suspect, that a vulnerable adult has been or is being abused, neglected or exploited SHALL [emphasis supplied] immediately report such knowledge or suspicion to the central abuse hotline." Any securities dealer, investment advisor, or associated person must already report exploitation if the customer resides in Florida.

There are eight additional categories of professions that have an identified duty to report under 415.1034(1)(a). These include any "bank, savings and loan, or credit union officer, trustee, or

employee." If any securities dealer, investment advisor, or associated person works for any bank, savings and loan, or credit union, they have an identified duty to report.

If the financial services industry's concern is that they wish to make securities dealers, investment advisors, or associated persons a special category, then a ninth group of professionals can be added to 415.1034(a) as follows:

"9. Securities dealers, investment advisors, and associated persons, as defined by Chapter 517, Florida Statutes"

Such inclusion would specifically avail these professionals of the protections of Chapter 415 for reporters and information sources when disclosing information to Adult Protective Service workers, without eliminating existing statutory protections for vulnerable adults.

Securities Dealers and Investment Advisors Already Owe Their Clients a Fiduciary Duty Under Florida Law

We further believe this statute effectively serves to insulate brokers and investment advisers from their statutory and common law fiduciary duties. Assuming the existence of a fiduciary duty owed by a broker or investment adviser, we would argue that not only does there exist a right to refuse a transaction, ***there exists a common law duty to refuse the transaction***. Under Florida law, a fiduciary relationship arises where "a relation of trust and confidence exists between the parties (that is to say, where confidence is reposed by one party and a trust accepted by the other, or where confidence has been acquired and abused)." *Board of Trustees of the City of Lake Worth Employees' Retirement System v. Merrill Lynch Pierce Fenner & Smith, Incorporated*, 2011 U.S. Dist. LEXIS 58156 (M.D. Fla. 2011), citing *Doe v. Evans,* 814 So. 2d 370, 374 (Fla. 2002). In *Gochnauer vs. A.G. Edwards & Sons, Inc*., 810 F.2d 1042, 1049 (11th Cir. 1987), the Eleventh Circuit stated, "[t]he law is clear that a broker owes a fiduciary duty of care and loyalty to a securities investor." Furthermore, "under Florida common law, a stockbroker is charged with the duty of dealing with utmost honesty and good faith in his transactions on behalf of his client. The stockbroker has breached this duty where there is a showing of fraud, deceit or absence of good faith." *Messer v. E.F. Hutton & Co.,* 833 F.2d 909, 920 (11th Cir. 1987); *Brink v. Raymond James & Associates*, 2015 U.S. Dist. LEXIS 182479 (S.D. Fla. 2015).

With regard to the history of the law of fiduciary duty in Florida, the court in *McCoy v. Durden*, 155 So. 3d 399 (Fla. 1st DCA 2014), stated,

> Under Florida's common law, the Florida Supreme Court has defined the concept of fiduciary duties broadly reflecting its historical origin in equity. In *Quinn v. Phipps*, 93 Fla. 805, 113 So. 419 (1927), a case involving allegations that a real estate broker had violated his fiduciary duty, the Court explained the basis of the duty:
>
> > The term 'fiduciary or confidential relation,' is a very broad one. It has been said that it exists, and that relief is granted, in all cases in which

> influence has been acquired and abused—in which confidence has been reposed and betrayed. The origin of the confidence is immaterial. The rule embraces both technical fiduciary relations and those informal relations which exist wherever one man trusts in and relies upon another.
> * * *
> Stripped of all embellishing verbiage, it may be confidently asserted that every instance in which a confidential or fiduciary relation in fact is shown to exist will be interpreted as such. The relation and duties involved need not be legal; they may be moral, social, domestic or personal. If a relation of trust and confidence exists between the parties (that is to say, where confidence is reposed by one party and a trust accepted by the other, or where confidence has been acquired and abused), that is sufficient as a predicate for relief. The origin of the confidence is immaterial.

Id. at 420-21; *see also* ***Doe v. Evans*, 814 So. 2d 370, 374 (Fla. 2002)** (quoting Restatement (Second) of Torts § 874 cmt. a) ("A fiduciary relation exists between two persons when one of them is under a duty to act for or to give advice for the benefit of another upon matters within the scope of that relation.").McCoy v. Durden, 155 So. 3d 399, 402-403, 2014 Fla. App. LEXIS 20981, *7-8, 40 Fla. L. Weekly D 81 (Fla. Dist. Ct. App. 1st Dist. 2014).

Separate and apart from the Florida common law fiduciary duty, brokers and investment advisers owe statutory fiduciary duties with certain types of accounts. That fiduciary duty generally exists in fee based accounts (as opposed to commission based accounts). The SEC states on its website,

> As an investment adviser, you are a "fiduciary" to your advisory clients. This means that you have a fundamental obligation to act in the best interests of your clients and to provide investment advice in your clients' best interests. You owe your clients a duty of undivided loyalty and utmost good faith. You should not engage in any activity in conflict with the interest of any client, and you should take steps reasonably necessary to fulfill your obligations. You must employ reasonable care to avoid misleading clients and you must provide full and fair disclosure of all material facts to your clients and prospective clients. Generally, facts are "material" if a reasonable investor would consider them to be important. You must eliminate, or at least disclose, all conflicts of interest that might incline you — consciously or unconsciously — to render advice that is not disinterested. If you do not avoid a conflict of interest that could impact the impartiality of your advice, you must make full and frank disclosure of the conflict. You cannot use your clients' assets for your own benefit or the benefit of other clients, at least without client consent. Departure from this fiduciary standard may constitute "fraud" upon your clients (under Section 206 of the Advisers Act).

https://www.sec.gov/divisions/investment/advoverview.htm ***We would argue that where this statutory fiduciary duty exists, an investment adviser is obligated to refuse a transaction when the investment adviser believes that exploitation is occurring.***

Proposed section 517.34 (6) is intended to eliminate this federally imposed statutory duty and immunize investment advisers who ignore or fail to detect exploitation when they should reasonably be expected to detect it. Section 517.34 (6) clearly does not serve to protect elderly or vulnerable adults.

The Relationship Between Dealers (or Investment Advisers) and Clients Should be Governed by the Parties' Contracts

Section 517, Florida Statutes, regulates dealers, investment advisers, and those individuals who work for these entities. When dealers and investment advisers initiate a new relationship with a client, a written contract is signed by the client. These contracts are long and complex. Among the most publicized provisions of these contracts are the arbitration clauses that require clients to resolve their claims in arbitration, rather than court. Dealers and investment advisers rely on the enforceability of these contracts to stay out of court. It is our belief that there is nothing in this statute that cannot or should not be addressed privately in the broker/client contract. The statute serves to codify a broker's right to refuse a transaction under certain circumstances. Why can't a broker acquire that right contractually? We believe that a broker's acquisition of this right should be acquired contractually, not statutorily. Whether such contractual provisions would violate Florida public policy is a separate issue, not addressed in this memorandum.

This Statute Creates a New Class of Individuals Based Upon Age and May Therefore Be Discriminatory

Section 517.34(1)(d) defines "specified adult" as "a natural adult who is 65 years of age or older or a vulnerable adult as defined in s. 415.102." The inclusion of anyone who is 65 years or older regardless of their vulnerabilities would be new to Florida law, and arbitrary by nature. Section 415.102 (28) defines the phrase "vulnerable adult." Nowhere in the definition is any specific age mentioned. Rather, age is only referenced in the context of one suffering "the infirmities of aging." Proposed section 517.34 specifically applies to able-bodied, competent adults age 65 and older. This extraordinarily broad definition will inadvertently provide a safe harbor to bad actors who want, for instance, to stop the transfer of account assets when a competent adult simply wants to fire the former adviser.

When revised, this legislation should adopt the definition of "vulnerable adult" as defined in Florida Statutes 415.102. It is comprehensive and includes all adults with impairments, limitations and disabilities making them vulnerable to exploitation. If this legislation was part of Chapter 415, there would be no need for additional definitions of any kind since all the necessary definitions are contained in that Chapter.

Proposed Section 517.34 (6) Conflicts with Section 415.1036

Section 415.1036 (1) provides immunity to mandatory reporters when certain conditions are met. Importantly, section 415.1036 removes immunity if a "lack of good faith is shown by clear and convincing evidence…." Proposed section 517.34 (6) lacks this critical tool. Under the proposed statute, one receives immunity virtually automatically.

We would note further that section 517.34 is also inconsistent with section 415.1036 (2). The latter statute provides a cause of action to a mandatory reporter who suffers a change in employment status as the result of making a report. Similar remedies should be given to associated persons who suffer a change in employment status as the result of either acting as a mandatory reporter, or refusing a transaction, such as a buy or sell. Not all Series 7 registered associated persons work for major wire houses that have readily accessible compliance departments. The majority of associated persons work from isolated offices where there is no onsite compliance department, or the compliance department may be in a different time zone. These associated persons will not have the luxury of waiting to speak to a compliance officer before taking action (or inaction). As previously noted, they may have a common law duty to refuse a transaction. Appropriate protections should be given to those persons who are truly attempting to protect the vulnerable adult (and not the "specified" adult).

Proposed Section 517.34(6) & (7) Conflict with Fla. Stat. 709.2120

Fla. Stat. 709.2120 requires dealers, investment advisors, and associated persons must honor power of attorney that complies with Florida law. If they refuse to honor the power of attorney, such as refusing to allow a transaction requested by an agent, they must put the reason in writing, unless it is based on one of the following circumstances:

> (a) The third person is not otherwise required to engage in a transaction with the principal in the same circumstances;
> (b) The third person has knowledge of the termination or suspension of the agent's authority or of the power of attorney before exercising the power;
> (c) A timely request by the third person for an affidavit, English translation, or opinion of counsel under s. 709.2119(4) is refused by the agent;
> (d) Except as provided in paragraph (b), the third person believes in good faith that the power is not valid or that the agent does not have authority to perform the act requested; or
> (e) The third person makes, or has knowledge that another person has made, a report to the local adult protective services office stating a good faith belief that the principal may be subject to physical or financial abuse, neglect, exploitation, or abandonment by the agent or a person acting for or with the agent.

Section 709.2120, as shown above also contains the requisite requirements for anyone, including a dealer, investment advisory, or associated person to reject the use of a power of attorney if the person believes there to be exploitation. That individual must call Adult Protective Services, per Fla. Stat. 415.1034(1) to report the exploitation and then can reject the power of attorney because he/she has knowledge a report has been made.

If a dealer, investment advisor, or associated person rejects a power of attorney in violation of Fla. Stat. 709.2021, they can be subject to damages and attorneys' fees. Proposed section 517.34(6) & (7), through their blanket immunity for any "civil, criminal, or administrative liability", would remove the teeth from Fla. Stat. 709.2120, thus removing protections for vulnerable adults who rely on principals taking actions with valid powers of attorney.

Proposed Section 517.34 Has No Enforcement Mechanisms

Proposed Section 517.34 has no requirements for dealers, investment advisors, and associated person to document anything that would lead them to believe the transaction they might suspend is the result of suspected exploitation. There is no requirement that they document the call to Adult Protective Services hotline. There is no requirement they make any report as to the outcome of the suspended transaction.

OFR could not monitor the use of this statute to determine whether it was being abused by dealers, investment advisors, or associated persons. Even if there was some monitor mechanism developed, the blanket immunity of 517.34 (6) & (7) eliminates any government entity, damaged victim, or even law enforcement from holding the wrong-doer accountable.

This lack of documentation requirement coupled with the blanket immunity in 517.34(6) & (7) leaves the victims of potential exploitation or victims of bad acting dealers, investment advisors, or associated persons no way that this could be enforced to protect them.

Proposed Section 517.34 (7) Does Not Protect Vulnerable Adults

Section 517.34 (7) does not appear to serve any purpose other than to expand the financial service industry's newly created safe harbor. The last phrase of the section references the "customer agreement" between the parties. What if there is a conflict between the customer agreement and this section? This section effectively serves as the "we want to eat our cake and have it too" section. This section allows a dealer or investment adviser to refuse a transaction under any circumstances, including a contractual basis that might conflict with section 517.34. Dealers and Investment Advisers should be forced to choose. While the statute should contain a provision voiding any contract that permits the refusal of a transaction under any circumstance not identified in the statute to remedy this issue. Even this suggestion makes no sense. Under Florida law, the dealer or investment adviser owes a fiduciary duty, the fiduciary standard would govern the parties' dealings.

Continuing Education Requirements for Associated Persons and Investment Advisers

As we all know, neither a college degree nor a high school diploma are required to become an associated person or investment adviser under Florida law. Furthermore, obtaining investment licenses is just a matter of studying for an exam over a few weeks. It is more difficult to become an auto mechanic than it is to become an associated person. Given the extraordinary amount of trust placed by the elderly in these people, Florida should consider either statutory or administrative continuing education requirements for issues related to protection of the elderly. Not every associated person is fortunate to work for a firm such as Wells Fargo Advisors, which employs people specifically for elder protection purposes. A quick Google search for "Ariel Hernandez" in Broward County will reveal the story of a Series 7 associated person who for several years stole from his elderly clients. Mr. Hernandez sits in a Broward County jail waiting for his trial. This case illustrates the importance and necessity of continuing education not only for dealers, investment advisors and associated persons, but for compliance personnel as well. Notably, even at large wire houses, compliance employees located outside of Florida may or may

not be registered in Florida. Even Compliance Directors at major firms are often not registered in Florida.

Any legislation authorizing the suspension of a transaction or disbursement based on suspected exploitation should require those who would decide to take such dramatic step know and understand what exploitation is. To further protect Florida's elders, OFR consider requiring anyone with supervisory or compliance responsibilities in Florida to be registered in Florida.

An Alternative Mechanism to Proposed Section 517.34 Already Exists

Florida courts and the Florida Rules of Civil Procedure recognize the right to file an Interpleader action. Rule 1.240, Fla.R.Civ.P. Interpleader is also recognized under section 677.603, Florida Statutes. This section provides,

> If more than one person claims title to or possession of the goods, the bailee is excused from delivery until the bailee has a reasonable time to ascertain the validity of the adverse claims or to commence an action for interpleader. The bailee may assert an interpleader either in defending an action for nondelivery of the goods or by original action.

Analogously, whenever a dealer or investment adviser is uncertain whether to accept a customer's instruction due to concerns about exploitation, the dealer or investment adviser can ask a Circuit Court judge to make the decision. The right to file an Interpleader action is clearly recognized as the fairest mechanism for deciding conflicting claims to a corpus. [1] Furthermore, if the interpleading party is an "innocent stakeholder", attorneys' fees are recoverable. *Reliastar Life Ins. Co. v. Knighten*, 2005 U.S. Dist. LEXIS 26317 (M.D. Fla. 2005) (interpleader recognized by federal statute, 28 U.S.C.S. section 1335); *Zuckerman v. Alter*, 758 So.2d 1172 (Fla. 4th DCA 2000).

Conclusion

Proposed section 517.34 is an unnecessary statute that will only serve to create a safe harbor for the financial services industry. The statute would cause confusion where it conflicted with common law and other Florida Statutes, as well as parties' existing contractual rights. Most important, the proposed statute would not serve to protect Florida's vulnerable adults subject to exploitation.

[1] *See also* Rule 12.240, Fla. Fam. Law R. Proc.; section 475.711, Florida Statutes; section 475.25, Florida Statutes; and section 721.08, Florida Statutes, as examples of Florida rules and statutes incorporating the interpleader mechanism.