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Working With Senior Investors

Introduction

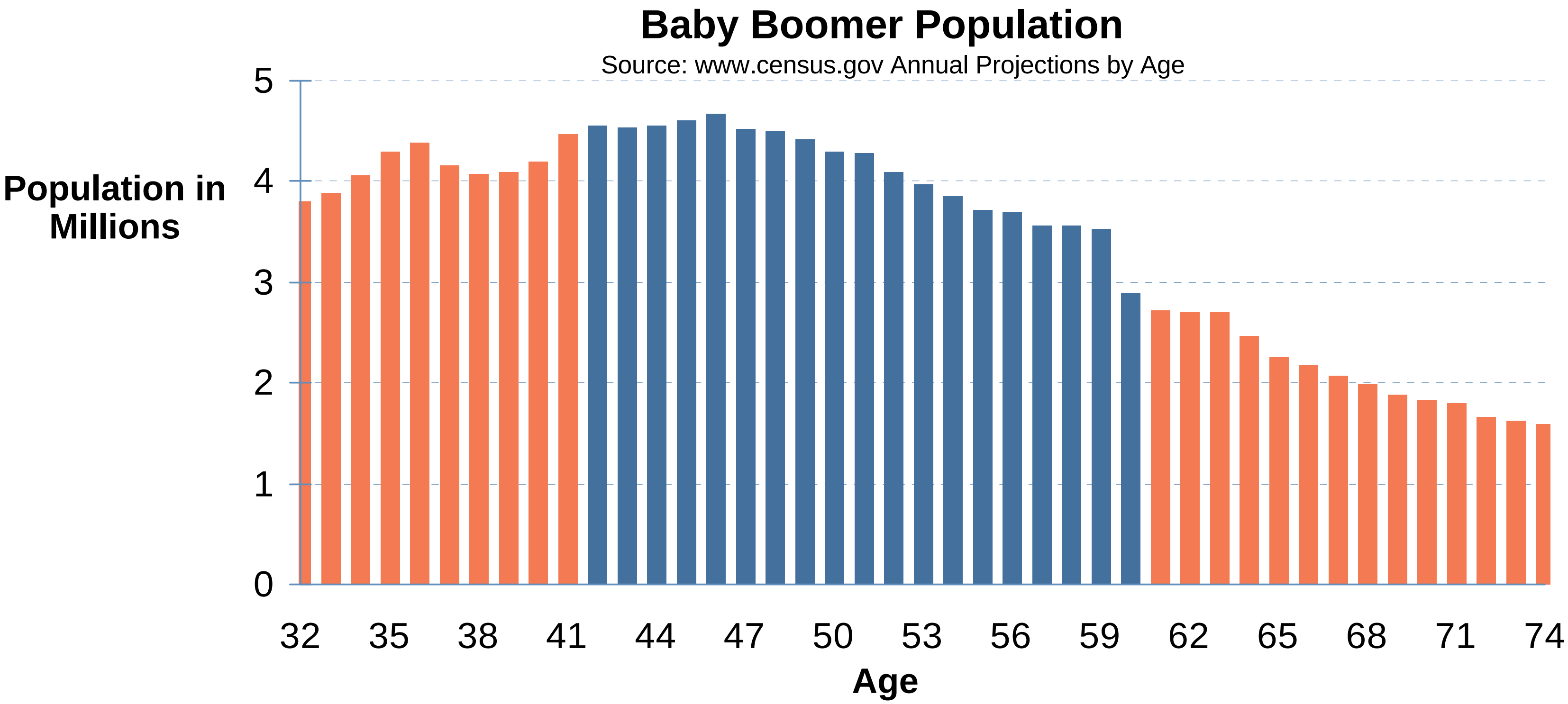
Welcome to the "Working With Senior Investors" training webcast.

- Course highlights key regulations, Firm policies, and best practices for working with senior investors.
- Required training for all branch personnel (*e.g.*, FAs, IRs, CSAs, SAs) and certain other registered and non-registered employees throughout the Firm.
- For registered employees, this course helps to satisfy mandatory continuing education requirements.

  In order to receive credit for this mandatory course, you must complete the entire module and click on the acknowledgment button at the end of the webcast.

Aging Client Base

- 41 million Americans are currently retired
- The first Baby Boomers just turned 60!
- 77 million Baby Boomers are expected to retire within the next 20 years



Training Agenda

- Suitability Considerations for Senior Investors
- Diminished Capacity and Suspected Elder Abuse
- Marketing to Seniors

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Suitability Considerations for Senior Investors

Basic Suitability Rules

- Suitability and Know Your Customer (KYC) rules and policies apply to **all** clients. These include FINRA (NASD & NYSE) rules and GWM policies.
- When recommending a transaction, you must:
  - have reasonable grounds for believing that the recommendation is suitable
  - make reasonable efforts to obtain information about the client’s
    - Financial status;
    - Tax status;
    - Investment objectives; and
    - “such other information used or considered to be reasonable by such member or registered representative in making recommendations to the customer.”

Know Your Customer

- KYC will help you determine suitability.
- Required information at account opening includes:
  - annual income, investment objectives, investment experience, and the client’s employment/retirement status.
- Age, life stage, liquidity needs and other factors are necessary in order to assess suitability of investments for ALL clients.
- See GWM Compliance Manual, Section 7.2 and 8.2. for more information

Suitability Factors Particularly Relevant to Seniors

The following factors may take on greater importance as clients age:

- Investment time horizon
- Investment objectives
- Liquidity needs
- Changes in tax status
- Risk Tolerance

Staying Current with Your Client's Circumstances

- Update KYC information as clients age
- FINRA and Morgan Stanley suggest the following topics should be discussed and evaluated with your senior clients:
  - **Employment:** current status and plans post-retirement
  - **Expenses:** Existing and anticipated expenses in retirement (*e.g.*, mortgage, travel)
  - **Income Needs:** What is needed to meet fixed or anticipated expenses
  - **Savings:** Amount saved for retirement and investment strategy for those assets
  - **Liquidity:** Anticipated and unanticipated needs, and how those needs will be met
  - **Goals:** Customer's financial and investment goals (*e.g.*, preserving capital or accumulating assets for heirs)
  - **Health:** What health care insurance does the customer have and whether the customer will need to rely on investment assets for health costs

Evaluating KYC Information

- Consider all information and goals;
- Do not consider specific factors (*e.g.*, net worth) in a vacuum
- *Eligibility* does not necessarily equal *suitability*
    - Customer net worth alone is not determinative of whether a particular product is suitable for an investor.
    - Even if the client qualifies as an “accredited investor” under Reg D, not all eligible investments are necessarily suitable.
    - Understand your client’s level of financial sophistication

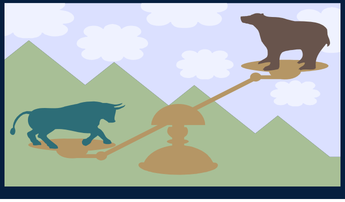
Recommending Certain Products

- FINRA: No product is, per se, unsuitable for senior investors.
- However, a senior's investment time horizon and other factors may impact whether certain products/strategies are suitable.
- Products with the following types of features warrant careful consideration:
  - Products that have withdrawal penalties or otherwise lack liquidity
  - Products with long holding periods
  - Products with features that may not provide their intended benefit to clients during their life expectancy
  - Complex products
- Be mindful of the above product features.

Investment Strategy Considerations

- Using retirement savings, including early withdrawals from IRAs, to invest in high-risk investments.
- Using home equity to invest in securities. You may not recommend this strategy to any client, including seniors.
- Assuming too much risk to maximize retirement income.
- Ignoring inflation risk by investing heavily in low-yielding investments that may not protect an investor's assets over time against inflation.

Customize Advice and Disclose Risks



- Tailor the recommendations you give to the individual circumstances of each client.
- While you cannot shield your clients from all investment risks, you are obligated to:
  - Understand the products and strategies you recommend;
  - Give your clients a fair and balanced picture of the risks, costs and benefits of the products or services you recommend; and
  - Recommend only suitable investments.

Key to successful client relationships = Maintain an open and balanced dialogue

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Diminished Capacity and Suspected Elder Financial Abuse

Diminished Capacity

- The likelihood that you will encounter clients who suffer from diminished mental capacity will increase as the ranks of older seniors grow
- According to a recent study, diminished mental capacity affects approximately 20% of people aged 85 years and older
- Diminished mental capacity may sometimes be difficult to identify, or may have pronounced symptoms

Common Signs of Diminished Capacity

- Memory loss: *is the client repeating orders, instructions, or questions?*
- Disorientation: *is the client confused over time, place, or simple concepts?*
- Difficulty performing simple tasks
- Difficulty speaking
- Difficulty with abstract thinking
- Misplacing items
- Drastic mood swings
- Changes in personality
- Increased passivity
- Poor judgment

How to Help Your Clients

- If your client is showing signs of diminished capacity, you should take the following actions:
  - Check whether an executed trading authorization form or durable power of attorney is on file. If so, consider contacting the agent.
  - If appropriate, suggest that the client bring a close family member or friend to your next meeting.
  - Discuss the situation with your supervisor and/or Legal and Compliance.

What is "Elder Financial Abuse?"

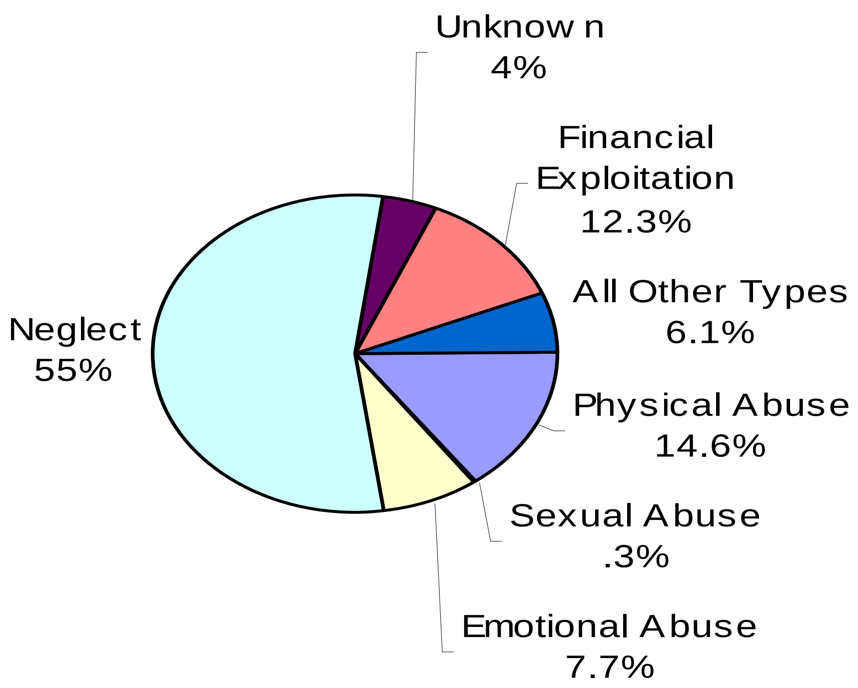
Occurs when somebody exploits a position of influence or trust over an elderly person to gain access to that person's assets, funds or property.

- *Cashing an elderly person's checks without authorization or permission*
- *Forging an older person's signature*
- *Misusing or stealing an older person's money or possessions*
- *Coercing or deceiving an older person into signing a document (e.g. contract or will).*
- *Improper use of conservatorship, guardianship, or power of attorney*

Examples of Elder Financial Abuse

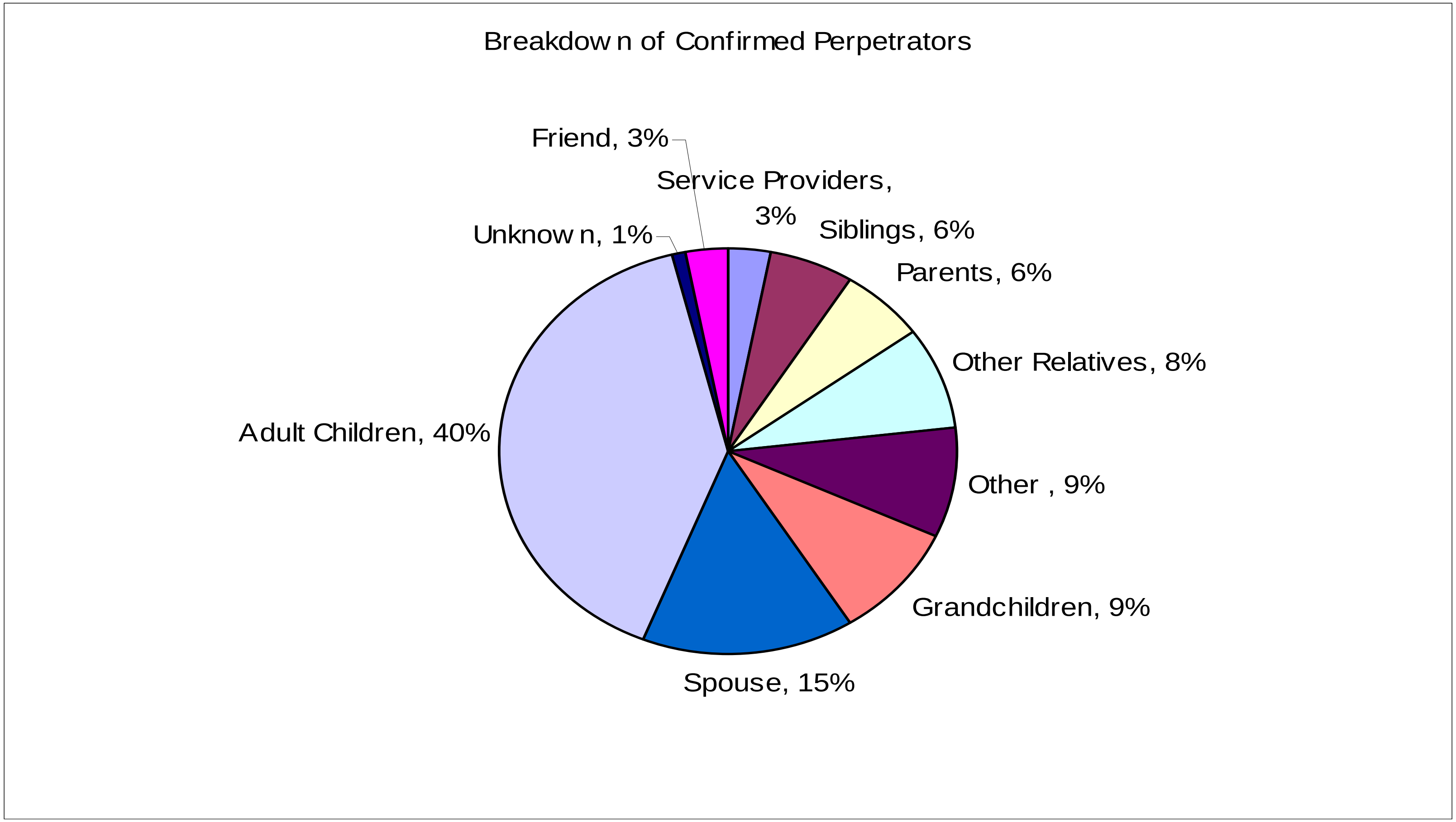
- A caretaker coerces an elderly client to transfer cash to her. The caretaker threatens to have the client committed to a nursing home if he refuses.
- An elderly client grants power of attorney to her son. The son makes speculative investments, hoping to increase his inheritance, but ignoring his mother's need for current income.
- An elderly client requests a large wire transfer to Canada. He explains that he has been notified that he is a winner of the Canadian Lottery.

A Growing Problem



(Source: National Center on Elder Abuse 2001)

Who abuses the elderly?



(Source: National Center on Elder Abuse 2001)

Possible red flags of financial exploitation of seniors

- Sudden reluctance to discuss financial matters
- Sudden, atypical, or unexplained withdrawals or other changes in financial situation
- Abrupt changes in wills, trusts, or power of attorney
- Changes in beneficiaries on insurance policies or IRAs
- Increasing lack of contact with and interest in the outside world
- Admission of financial or material exploitation or suspected exploitation

Possible red flags, continued

- Concern or confusion about missing funds in his or her account.
- Unusual or first-time wire transfers, especially to foreign countries.
- Fear of eviction or nursing home placement if money is not given to a caretaker.
- Appearance of insufficient care despite having money.

How do I report suspected elder abuse?

- Depending on the state, the Firm may be required to report a case of suspected elder abuse.
- Escalate all cases of suspected elder abuse to:
  - your Branch Management Team or
  - Field Services Unit of the Legal Department (914-225-4LAW).

Suspected abuse is sufficient reason to escalate.

Marketing to Senior Investors

General Communications Requirements

- All communications with the public must adhere to the Firm's general standards, which include:
  - Truthfulness and good taste
  - Fair and balanced presentation
  - May not project performance or promise specific results
- For more information, see Chapter 6 of the GWM Compliance Manual.

Seminars: Regulatory Concerns

- FINRA, the SEC, and State regulators are increasingly focused on seminars targeting senior investors.
  - High Pressure Sales Tactics
  - Lavish inducements
  - Misrepresentations regarding the nature of the seminar
  - Exaggerated promises
- **Remember**: All client seminars and related materials must get the required approvals

Additional Seminar Rules

- Use of Door Prizes
  - Compliance Department pre-approval is required.
  - Prizes must be of nominal value.
  - No cash, coins or securities.

- If a product vendor is reimbursing all or part of the expense of the seminar:
  - You must submit a non-cash compensation request, and
  - A representative of the vendor must be present at the seminar

Seminar Rules Pertaining to Outside Speakers

- Use of Outside Speakers
  - Branch Manager pre-approval is required.
  - You may not imply that an affiliation exists between the Firm and the outside speaker.
  - Outside Speaker Disclosure is Required
    - On the seminar invitation
    - Mention at the start of the seminar
    - Make clear where they are from and that they are not associated with Morgan Stanley

Use of Professional Titles

- Morgan Stanley policy, as well as regulatory requirements, prohibit
  - Making false, exaggerated, unwarranted or misleading statements or claims in communications with the public or
  - Claiming to have an expertise that you do not possess.
- Senior investors are more likely to be influenced by claims of expertise and accreditation.

Use of Professional Titles

- In 2007, Massachusetts and Nebraska restricted the use of senior designations
- Other states are expected to follow suit.
- Designations that falsely imply expertise in senior investor issues may violate FINRA rules and possibly the federal securities laws.

Firm Policy on Professional Titles

- FAs/IRs may only use titles that have been pre-approved by the Firm
- The "Retirement Planning Specialist" designation is no longer an approved designation
- Morgan Stanley approved retirement designations:
  - Chartered Retirement Planning Counselor (CRPC)
  - Chartered Retirement Plans Specialist (CRPS)
- For information on retirement designations contact Learning & Development

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Working With Senior Investors Quiz

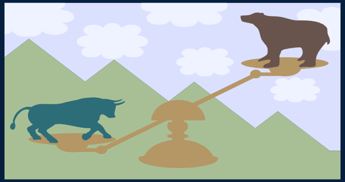
On the next few slides, you will see various scenarios and related questions that will test what you have learned in this course.

After reading the scenarios and questions, click on the circle next to the answer you believe is correct. You will receive a message as to whether the answer is “correct” or “incorrect”.

You must choose the “Correct” answer in order to proceed. You will then be prompted to click “Next Question” in order to move to the next slide.

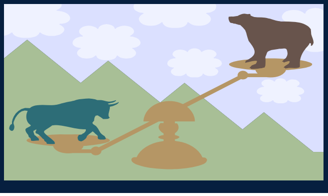
Take the Quiz

Scenario #1



Jessica is an FA in San Diego. One of her clients, Henry, is a 75 year-old retired engineer in poor health. One day, Henry calls Jessica to say that he'd like to invest in a hedge fund. After some questioning from Jessica, it turns out that Henry only recently learned about hedge funds from a friend of his at the American Legion. His friend told Henry that to qualify for some hedge funds, an investor needs to have a net worth of $1 million. Henry is confident that his house, which he purchased in 1965, is worth at least $1 million today. He asks Jessica to recommend some suitable hedge fund investments.

Scenario #1: Question 1



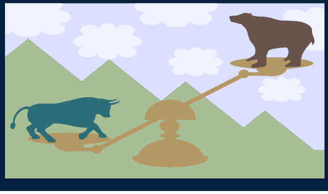
Which of the following best describes Jessica's suitability obligation?

A. She has no suitability obligation because it was Henry's idea to invest in hedge funds.

B. Because she was asked for a recommendation, Jessica *must* recommend at least one hedge fund to Henry, but it must be a suitable one.

C. Jessica must determine whether hedge funds are a suitable investment for Henry, and if not, is under no obligation to recommend specific funds to him.

Scenario #1: Question 2



Henry is able to meet the requirements of an “accredited investor” under Regulation D, thanks to the value of his home. How does this fact affect Jessica’s suitability analysis?

A. Henry’s status as an accredited investor under Reg. D satisfies Jessica’s suitability obligation.

B. Jessica needs to investigate whether Henry has accurately reported his net worth for purposes of Reg. D, but otherwise has no obligation.

C. Henry’s eligibility to purchase certain hedge funds does not satisfy Jessica’s suitability obligations. She must consider whether the investment is suitable for Henry in light of a number of factors, including age, life stage, risk tolerance and liquidity needs.

Scenario #1: Question 3

Jessica identifies some funds with investment styles that might be suitable for Henry; however, those funds all have an initial "lock up" period of two years, plus withdrawals from the funds can only be made quarterly. In light of these factors, what should Jessica consider in performing her suitability analysis?

A. Whether Henry has sufficient income to meet his current expenses.

B. Whether Henry has other sources of liquid assets that could serve as "emergency funds" from which to meet future, unexpected expenses such as medical and nursing home costs that might arise.

C. Whether Henry's age and health status can sustain having this particular portion of his assets locked-up for 2 years, and subject to withdrawal constraints.

D. All of the above.

Scenario #2

Roger Caldwell is a long standing client of New York IR Matt. Roger just turned 79 and is exhibiting signs of memory loss. Roger calls Matt three days in a row asking him to input an identical order. This is out of character for Roger. Matt has reminded Roger with each successive call that Matt has already placed the order but Roger seems to have forgotten about the previous day's call.

Scenario #2: Question 1

How should Matt proceed?

A. Roger is clearly authorizing this trade, and therefore, Matt has nothing to worry about and can proceed to take trade orders from Roger.

B. Matt should discuss Roger’s behavior with his Branch Manager or other supervisor, and then reach out to the Field Services Unit of the Legal Department for further guidance.

C. Check the file to determine whether an executed trading authorization form or durable power of attorney exists and, if so, contact the agent.

D. Answers (b) and (c)

Scenario #2: Question 2

Same scenario, except Roger's son Jim sends in a trading authorization form giving him full authorization on the account, and instructing Matt to have no further contact with Roger. Matt immediately begins noticing checks drawn on the account payable to various high end stores (which have never occurred before) and large amounts of cash funds being transferred to a Morgan Stanley account in Jim's name. Does Matt need to take any action?

A. Yes. The warning signs that potential elder abuse is occurring exist. Further review is necessary. Matt should immediately escalate this matter to his supervisor and the Field Services Unit of the Legal Department.

B. No. While Matt is nervous about what he is seeing, he should wait a few weeks or months to observe more activity on the account before taking action.

C. No. The client signed a trading authorization for the account, so Matt is protected if Jim places trades or takes other actions on the account.

Scenario #3

Felix, an FA in San Francisco, sends a letter to a prospective senior client which states that he has received extensive professional training in retirement planning. Felix does not use a a professional designation when he signs the letter. In reality, the training consisted of a two hour correspondence course.

Scenario #3 – Question 1

Does Felix's letter pose any regulatory concerns?

A. No. It is permissible for Felix to slightly exaggerate his qualifications in order to remain competitive.

B. Yes. Felix's description of his "extensive" retirement planning "expertise" is false and misleading.

C. Yes, an FA is not allowed to solicit senior clients without having first obtained a specific senior-related designation, such as "Retirement Planning Specialist".

D. No, because Felix did not use a senior-related title.

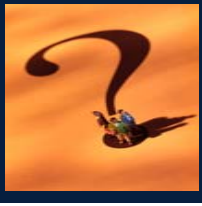
Scenario #3 – Question 2

Same scenario as before, but now Felix's letter also guarantees the client a consistent annual return of 18 – 20% on his or her retirement account with no downside risk. Is it proper for Felix to offer the client a consistent rate of return?

A. No, Felix may not guarantee a rate of return for the account, nor state that there will be no downside risk.

B. Yes, if Felix truly believes he can achieve this rate of return on the client's account.

C. Yes, as long as the account is invested in fixed income investments.



Questions

Please contact your Legal and Compliance coverage team with any questions

To receive credit, please click the acknowledgment button on the next screen

Thank you!

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Acknowledgement

I acknowledge that I have received, reviewed and understand this material.

I Accept　or　< Replay