Imagine you are at a restaurant with your parents. Your father, as always, handles the bill, but you notice it is taking longer than usual for him to sign the credit card slip. A quick peek at the check reveals that he has drastically undertipped (and it’s not just that he is being cheap). Your father has accurately tipped many times before, but this time, he failed to calculate a simple percentage and made an unintentional financial error. Once his back is turned, you quickly drop some cash on the table, but you leave wondering whether there are bigger financial mishaps waiting to happen.

It can be unsettling when you first recognize that a family member is having difficulty with financial tasks where once there was none. But this isn’t an isolated occurrence. In just 15 years, one in five Americans will be age 65 or over, and there are currently more Americans over 65 than the entire population of Canada. This demographic shift is already in motion and as we consider the financial health of our nation, it is in our best interest to understand and address the specific financial challenges facing older adults. But what characterizes normal aging, how do inevitable changes in an aging person’s cognitive skills affect financial decisions, and most important, what can we do about it?

AGING AND COGNITIVE FUNCTION

As we age, the speed at which we generate, transform, and manipulate new information decreases. This type of mental processing is called fluid intelligence, and research has shown that even the healthiest among us
has less fluid intelligence as we age.\footnote{National Endowment for Financial Education, “Cognitive Capabilities, Decision-Making Ability and Financial Outcomes Across the Lifespan.” (New York: Columbia University, 2014).} But that is only part of the story. \emph{Crystallized intelligence}—the accumulation of knowledge and experience—increases until about age 60, when it plateaus until about age 80, and eventually drops off. Although fluid intelligence might enable you to more quickly calculate a tip on the fly, your father’s crystallized intelligence might help him outperform you when analyzing stock performance and market trends.

There is a lengthy sweet spot where older adults perform comparably to younger adults using different amounts of both intelligences. This is good news because Americans over 65 collectively manage 43 percent of household wealth and 47 percent of stocks and mutual funds.\footnote{Ye Li et al., “Sound Credit Scores and Financial Decisions Despite Cognitive Aging.” \textit{Proceedings of the National Academy of Sciences}, 112 (1) (2015): 65–69.} With the increasing transfer of complex financial and health care decisions (such as allocating retirement savings in defined contribution plans) to individuals, it is now more important than ever that financial education, products, and services be intentionally designed to limit the strain of normal cognitive decline and play to older people’s strengths—namely that the longer you live, the more you know.

**Early Warning Signs of Financial Decline**

1. Slowness in completing financial tasks
2. Missing key details in financial documents
3. Problems with everyday arithmetic
4. Decreased understanding of financial concepts
5. Trouble identifying risks in investment opportunities

**BREAKING THROUGH THE BARRIER OF DENIAL**

As a society we cannot afford to delay the conversation about how normal aging affects financial decision making, especially given a tendency for individuals to develop blind spots to their own cognitive decline. “No one thinks they will end up in a nursing home, and everyone thinks they are..."
going to die peacefully in their sleep,” says Merrell Bailey, an Orlando-based attorney who serves on our board of trustees at the National Endowment for Financial Education (NEFE). As a specialist in estate planning, Bailey sees families facing end-of-life challenges every day. She says there are three common misconceptions among her clients:

- People think they will be healthier than they will be.
- They think they have more money than they do.
- They think their families will step up and help when needed.

Regardless of one’s physical condition, everyone will experience health declines by age 80. A 2014 Consumer Reports survey found that one in four people over age 80 has a hard time just getting out of a chair, and more than one-half report having four or more chronic health conditions. The second misconception is troubling, given the obvious consequences of having a generation of older Americans run out of money when they no longer can work. Although the third misconception potentially presents the biggest challenge, it also is the best opportunity to avert worst-case scenarios.

Many aging adults put off important conversations about their finances despite the desire for their family members to take charge when they become unable. But finding ways to engage family members early on is one of the most significant ways to ensure the overall financial health of aging adults. Not having a plan is a plan. It is important to respect the older adult’s independence, emphasizing that discussing contingencies and laying out clear accountabilities is not handing over the keys. It simply enables the family to support the older adult in ways that meet everyone’s needs.

THE FINANCIAL CAPABILITY TRIPOD

According to NEFE-funded research from Columbia University, increased financial knowledge positively relates to real-world financial behaviors and can help offset the effects of declining fluid intelligence. But knowledge alone is insufficient to strengthen and secure the financial health of older Americans. The “financial capability tripod” recognizes that the financial challenges facing older adults are complex and that our response

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3 Consumer Reports, “Healthy Aging into your 80s and Beyond.”
should be similarly multifaceted, encompassing some aspect of all three legs of the tripod. There is no evidence that general crystallized intelligence leads to better financial decision making; just because a person has lived longer does not inherently mean that he or she makes better financial decisions. Effective financial literacy requires understanding financial products, not just experiencing them.

The three legs of the tripod are below.

**Leg 1: Financial Education Must Be Delivered Frequently and Regularly through All Stages of Life.**

Financial knowledge should be gained through real-world experience, and relevant information should be presented with enough time to guide and inform decision making. Passive, one-off financial education is not as effective as targeted jolts of financial education offered within the context that a person needs it. For example, a person might not need to understand the ins and outs of 401(k) plans until they are electing workplace benefits.

**Leg 2: Consumer Protection Must Be Built into Financial Systems and Products, Voluntarily and through Regulation.**

With their declining fluid intelligence, seniors might make decisions in the moment, such as signing a contract, that on reflection with their crystallized intelligence are bad decisions. Consumer protections with cooling-off periods provide aging adults with the time they need for further reflection and analysis, and they help mitigate any pressure on older adults’ diminished fluid intelligence when they are hustled into signing something quickly. For example, to help safeguard funds prepaid for funerals, Minnesota law requires a funeral director or cemetery operator to place all prepaid funds in a trust account in a bank or other financial institution and allows the customer to request a full refund at any time.

Seniors are also more vulnerable to fraud and scams. We need to help seniors protect themselves, but we must punish bad actors in the industry and diligently prevent abusive practices. This must be carried out by appropriate state authorities and is a priority for regulatory and judicial agencies such as the Consumer Financial Protection Bureau and the Financial Industry Regulatory Authority.
Finally, financial institutions and advisors should use familiar financial terminology so as not to confuse older adults (and to help them tap into their crystallized intelligence). It might seem obvious, but financial institutions can also help by presenting information clearly and in large, legible print.

**Leg 3: Smart Defaults Must Be Implemented to Help Consumers Easily Do What They Need to Do.**

One of the best ways we can help aging adults is to anticipate what they want to do and help them do it (or at least help them avoid damaging mistakes) by building in “nudges” and defaults. For example, going back to the opening example, many restaurants now include suggested tip amounts on the bill. Automating monthly bill pay is another way to limit potential mistakes and to ensure bills are paid on time, in the proper amounts, to the right creditors.

**EMPOWERED FINANCIAL DECISION MAKING (AT ANY AGE)**

Empowered financial decision making doesn’t just happen. People make the best financial choices when they understand the underlying financial concepts, possess the relevant competencies to weigh the risks and rewards of disparate options, and have the confidence to choose the right option for them on the basis of their lifestyles and values. At the same time, we can prepare younger generations both to assist their elders and fare well as they age by helping them build their own experiential financial knowledge and store of crystallized financial intelligence.

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NEFE 5@50: 5 FINANCIAL STEPS TO TAKE IN YOUR 50s

1 Come to agreement with your significant other and/or trusted allies or family members. If you have a spouse or partner, don’t assume that you are on the same page. Make sure that there is not only awareness, but agreement about the current and future handling of your money, as well as about who will step in when necessary. If you do not have a significant other, you still have to own your plan and make sure your wishes are known and understood by a trusted ally or family member.

2 Get your financial house in order. Consolidate financial resources (bank accounts, retirement assets, investments) and set up automatic payments for regular bills.

3 Check your paperwork. A will is important, but a durable power of attorney is perhaps the most important document to have in order. If you become incapacitated without one, often the only way to handle your affairs is to have you named a ward of the court with a court-appointed guardian. And if you designated financial power of attorney in one state, but subsequently moved to another, double check that it is still valid in your new state of residence.

4 Assign roles. Communicate clearly within the family who will be responsible for what. Consider delegating financial, medical and social roles to different people based on their strengths. Set a regular time to check in. Continually assess whether retirement and other investment accounts are at the appropriate risk levels and examine credit reports for errors or potential fraud. Also use this time to get a gut check from your inner circle on any offers or sales pitches you might be receiving. One of the early warning signs of financial cognitive decline in normal adults is an overemphasis on potential benefits and a diminished awareness of risk.

5 Seek professional assistance. Assemble a trusted team that might include your lawyer, financial professional and, later, a geriatric care manager—particularly if you don’t have family members willing or able to step in.