With the passage of the Dodd-Frank Financial Reform Bill in July 2010, there are now proposed amendments to SEC Rule 17Ad-17 due to be finalized in 2012 that would extend the requirements to the broker/dealer community. As a result, brokerage firms – which have been exempt from the Rule – must now confront a new and potentially burdensome array of operational requirements and costs. Aside from conducting the basic searches necessary to comply with the requirements, brokers must consider its effect on clients and the additional impact of evolving state unclaimed property enforcement that is placing even more accounts at risk. It is also important to understand the benefits being realized by many brokers and financial services firms who go beyond the letter of the law and establish more robust analysis and communications solutions.

Brokerage firms – which have been exempt from SEC Rule 17Ad-17 – must now confront a new and potentially burdensome array of operational requirements and costs.

Since 1997, SEC Rule 17Ad-17 has governed the manner in which transfer agents and other paying agents have handled “lost” securityholder accounts. (These accounts are commonly defined as those for which mailed correspondence has been returned by the post office as “undeliverable.”) The rule was created to establish a minimum standard for attempting to locate new addresses for these shareowners and to re-establish communication with them.

The reason that searching and communicating with “lost” owners is critical is that every U.S. state and territory has unclaimed property laws which require these accounts to be liquidated and remitted (or “escheated”) into state custody if the address on the account is not updated. While the statistics surrounding this process are remarkable – for instance – more than $33 billion is held by the states with a billion more reported each year – it is an inescapable reality that SEC Rule 17Ad-17 has played a significant role in reducing these figures by protecting the owners of securities over the last 15 years. The largest single reason for its effectiveness is that it has helped companies “see” the scope of the lost accounts and inaccurate addresses. This increased awareness has enabled companies across all industries to implement additional best practices regarding dormant and lost accounts that have protected millions of additional investors.

The Dodd-Frank Financial Reform Bill

As custodians of securityholder records, transfer agents and broker/dealers are responsible for disseminating owner communication and dividend interest payments. The proposed changes to SEC Rule 17Ad-17 would obligate “paying agents” to exercise reasonable care in finding securityholders when they become lost. The SEC defines paying agent as “any transfer agent, broker, dealer, investment adviser, indenture trustee, custodian, or other person who accepts payments from the issuer of a securityholder and distributes payments to shareholders.” Broker/dealers will essentially have to follow the same due diligence protocol (outlined later) as transfer agents do today for shareholders. The Dodd-Frank changes also mandate and expand the scope of the Rule to require paying agents to take action when checks remain uncashed. These particular changes are not specific to brokers, but rather introduce a new requirement for all firms that are subject to the Rule. Specifically, an account owner is considered missing if a check sent to the address of record is not negotiated before 1) six months have passed or, 2) by the time the broker sends the next regularly scheduled check.

While broker/dealers, transfer agents, and paying agents will be given the flexibility to create systems that adequately demonstrate compliance with the Rule, they will be required to maintain records to demonstrate compliance with the Rule for at least the previous three years. In addition, paying agents will have to maintain written procedures to describe the methodology that was used to comply.
**Case Study:**  
**Brokerage Firm Maximizes Account Retention While Ensuring Compliance.**

Keane is helping several brokerage firms take a proactive stance with respect to account retention and SEC Rule 17Ad-17. One leading firm engaged Keane in 2010 hoping to reduce their population of RPO accounts by 20%. Keane accepted the challenge and helped the company implement a search process that: 1) meets the compliance requirements and 2) serves as the initial component in a comprehensive owner location and communication program.

**Challenge:**
Help a leading brokerage firm reduce its population of RPO accounts by 20%.

**Solution:**
Keane helped the company implement an SEC Rule 17Ad-17 compliance program with comprehensive owner location and communication. The program combined data analysis, owner searches, and customized mail and telephone outreach.

**Results:**
The volume of escheatable property was reduced by more than 64% in six months, protecting client relationships and retaining tens of millions of dollars in assets.

The customized program combined data analysis, owner searches, and customized mail and telephone outreach. Starting with a search process that is compliant with SEC Rule 17Ad-17, Keane was able to locate valid new addresses for more than 80% of the file. Further, it was confirmed that an additional 5% of the accounts were mis-coded as RPO since the owners were still residing at the original address. A series of mailings and telephone calls were conducted by Keane on behalf of the client to contact the owners, generate awareness of the RPO status, and urge them to update their account.

To the client’s surprise, the volume of escheatable property was reduced by more than 64% in six months. Most significantly, this success allowed them to protect client relationships and retain tens of millions of dollars in assets that would have otherwise been lost. Since far fewer accounts now enter the escheatment process, the client also realizes savings from reduced volumes of due diligence mailings and other annual unclaimed property reporting costs.
Compliance: The Operational Impact & Benefits

The SEC understands that broker/dealers will have to spend more time and money in order to comply with the Rule. Specifically, they believe the annual recordkeeping function would require approximately one hour for every 500 missing or lost securityholder accounts. Based on Keane’s 15 years of experience helping companies comply with SEC Rule 17Ad-17, these estimates are extremely conservative and do not properly reflect the legal effort, systems analysis and development, adjustments to mailing and returned mail handling processing, retention of vendors to assist with database searches, and development of compliance procedures. There is certainly a significant level of effort required. That is why many transfer agencies have chosen over the years to outsource the operational aspects to search and compliance specialists like Keane, allowing them to contain costs and focus instead on their core business.

With 15+ years of experience helping companies comply with SEC Rule 17Ad-17, Keane’s search and compliance expertise has allowed transfer agents to contain costs and focus on their core business.

What Exactly Does the Rule Require?

SEC Rule 17Ad-17 requires transfer agents to conduct two electronic database searches for owners whose accounts are coded as “lost.” This typically happens when mail sent to the address of record is returned as undeliverable. These mandatory searches aim to reduce the vast population of disconnected investors — which is typically one to two and a half percent of the nation’s outstanding account base, but can be much higher depending on the nature of the company and its data management practices.

A transfer agent may confirm that the address is truly inaccurate by resending the returned item within 30 days. If this approach is taken, the account will not be considered officially lost until the second mailing is also returned as undeliverable. (Resending the item is a good best practice as it mitigates the risk of a postal error causing the account to be incorrectly coded as lost.)

Once the mailed item is returned a second time the account should be classified as “returned from post office” or RPO. Once an account has been coded RPO, the Rule requires the transfer agent to conduct an electronic database search for a correct address. This search must occur within 3 to 12 months from the date the account is coded RPO. An industry-accepted best practice is to send a notification letter to newly located addresses asking the owner to update their information. If the first search and mailing fails to produce a confirmed address change, a second search is required between 6 and 12 months from the date of the first search.

The compliance requirement helps companies and transfer agents reduce their populations of missing securityholders.

The Benefits of Compliance

Keane has conducted millions of SEC Rule 17Ad-17 searches for more than 60 transfer agents and corporations. We observe three primary business benefits for those that embrace the Rule’s requirements:

1. The first and most obvious benefit is that the compliance requirement helps companies and transfer agents reduce their populations of missing securityholders. We expect it will have a similar impact on the broker/dealer population. While it’s not uncommon for brokers and financial advisors to conduct some degree of location efforts to reconnect with lost owner accounts, taking a more comprehensive, standardized, and centralized approach, which includes mailing notices to the owner, will quantifiably improve the results. Specifically, in our experience, proactive searches like those required by the Rule can reduce the missing securityholder population by 40 to 60 percent.

2. The second benefit is that client data quality is improved. The reason that results can vary so dramatically is that there are many determining factors such as the completeness of the company’s records, the age of the data, and even the age of the investors themselves. Conducting the search and communication programs required by SEC Rule 17Ad-17 can correct and update many inaccuracies that have existed for a long time and have perhaps impeded effective communication. For example, brokers will be able to
better ensure that owners receive critical account communications in a timely fashion. Improving the data accuracy will prevent many inappropriate communications. Examples of this include situations where account information is being sent to seemingly “active accounts” where in fact the owners have not been the recipients or even situations where the owners have been deceased for many years. The Rule helps to eliminate some of these privacy red flags.

For broker/dealers, compliance with the Rule will contribute to protecting many of their client relationships that today are unnecessarily terminated.

Conducting searches and mailings to new addresses early in the dormancy period (i.e. as soon as the original address is learned to be inaccurate) helps increase the likelihood of owner response. So the required searches are more effective at resolving the problem than if the company waits one or more years to research the account. Further, many companies don’t do any searches, but instead rely upon the state-required “due diligence” mailing requirement which occurs 3 to 4 months before accounts are escheated to the states. In that sense, compliance with Rule 17Ad-17 has proven to be a great way for companies and transfer agents to get ahead of the game and protect dormant securityholder accounts.

Keane has conducted millions of SEC Rule 17Ad-17 searches for more than 60 transfer agents and corporations.
Best Practices for Minimizing Escheatment

However, just because the requirements of the Rule have been fulfilled does not mean that a company has maximized escheat prevention. Obviously, given the success range mentioned previously, there is also an “unsuccessful” range of 40 to 60 percent. These are the lost accounts that remain unresolved and at risk of escheating when the dormancy period expires.

There are several factors which contribute to this high unresolved rate:

1. **Data Quality** – As previously mentioned, data quality and the age of the information is a significant variable that can limit the effectiveness of electronic searches. There are many data issues and owner location challenges that simply can’t be resolved without an additional level of manual review and research.

2. **Exempt Account Volume** – Certain accounts are exempt from SEC Rule 17Ad-17. For example, deceased-owner accounts, which can constitute 10% or more of the lost account population, are excluded. Since there is no requirement to locate heirs, beneficiaries, or estate representatives, these accounts typically remain unresolved. Conducting specialized programs to proactively research and provide attention to these accounts to locate the correct legal claimants can significantly reduce escheatment in these situations. Conducting this type of advanced outreach also creates new opportunities for brokers to establish relationships with the deceased’s relatives.

3. **Foreign Address Accounts** – Accounts with foreign addresses are not exempt from SEC Rule 17Ad-17, but the Rule’s required searches are very ineffective at resolving them. The primary reason is that many foreign investors do not have a U.S. Social Security Number (SSN), yet the Rule focuses on the SSN as the basis for the searches and prescribes database parameters specific to the domestic population. Consequently, new addresses are not found for most foreign account owners.

4. **Limitations of the Search and Communication Frequency** – The Rule is absolutely an important first step in reconnecting with account owners, however it has many limitations. In term of providing a comprehensive approach to locating owners, using electronic database searches in the prescribed manner is only one component. There are many additional research tools, processes, and manual techniques that can be used to increase the hit rate for accurate new addresses. Further, the research effort is only the first step in connecting with the owner. The second step of actually causing the owner to take action is often as, if not more, difficult. As such, the notices that are typically sent following each of the two required searches are often insufficient at “getting through” to lost investors and convincing them that action is necessary.

5. **Escheatable Accounts That Are Not Lost** – There is a new intensity in terms of state enforcement of “account inactivity” provisions and the penalties for not complying. Under these provisions accounts become classified as dormant when there has been no “owner-generated” activity on the account for a specified period of time. Irrespective of whether or not the account has generated any returned mail, if the account owner does not take action to remove the dormant status, the account must be escheated once the dormancy expires. Since inactive accounts are not part of the SEC Rule 17Ad-17 requirement, they represent an entirely separate population of accounts that can escheat, but there are no requirements that any searches or communication efforts occur. Without a solution to address inactive accounts as well, transfer agents and brokers alike will experience an increase in the number of accounts that must be reported.

Keane’s experience is that companies which address the challenges mentioned above can dramatically improve escheat mitigation results – in many cases pushing results into the 80 to 90 percent range. This has been especially valuable to mutual funds – and will likely be valuable to brokerage firms – because of the importance placed on preventing customer accounts from unnecessarily escheating. Below are some specific best practices and considerations that transfer agents and broker/dealers can apply to maximize account resolution and retention.

**Follow the Best Practice of Sending Notification/Confirmation Mailings**

Electronic search programs apply search methodologies that leverage a combination of databases, including those from multiple credit bureaus, real estate records, phone records and the National Change of Address system. Using these methodologies on searches indexed by SSN, there should be a 90 percent “hit rate.” Addresses
returned at this stage however, should not be used to update client accounts – they need to be verified by owner response to a mailing. If accounts are updated at this stage, without owner verification, broker/dealers and transfer agents may run the risk of mailing personal or confidential information to individuals other than the rightful owners. SEC Rule 17Ad-17 recommends that a confirmation mailing be sent to each newly identified address. To maximize response, this mail piece should be very limited in scope, describing only that the owner’s account is classified as “missing” and that all shares are at risk of escheat unless the owner takes action. To minimize opportunities for fraud, additional cross-checks should be performed before the mailing to ensure that the name of the lost owner on the original list is a match with the name on the newly found address. This practice will help minimize the 8% error factor that Keane observes when searches use SSNs alone. This error rate is a simple reality associated with using public electronic data and credit information.

Proactively Search for Beneficiaries and Heirs

As mentioned previously, the accounts of deceased owners are not solved by the Rule. For every 100 lost accounts that are searched in the SEC process, there may be up to 30 additional accounts excluded from the searches because the owner is deceased. Depending on the demographics of the file, efforts to find these individuals can require extensive research time and legal documentation to confirm rightful ownership. Proactive location and communication programs for heirs, beneficiaries, and estate representatives closes this service gap. This affords brokers the opportunity to establish new relationships and potentially retain the assets under management.

Prioritize Additional Search Efforts Based on Dormancy Periods

As with any due diligence type effort, it is important to prioritize the order in which location efforts proceed. This will provide the most opportunity for customer location and outreach efforts to succeed. For stock, mutual fund shares, and brokerage accounts this means starting with accounts that would escheat to states that have a three-year dormancy period first, followed by five-year states.

Expand Searches Beyond Electronic Databases

Post-SEC securityholder location should include additional searching beyond mere electronic resources. Maximizing success can require intense manual investigation and research. This is especially true in cases with older owners who never used credit and in situations where there are multiple heirs that must be identified in order to resolve an estate. Unfortunately, most automatically searchable data sources date back less than 20 years. Further, electronic searches can produce erroneous data and “false positives” which can result in sensitive information being sent to the wrong person. Exhaustive manual efforts produce more reliable results and lost securityholder location rates of up to 90 percent.

Conduct Response-Driving Communication Programs

It is very common that non-responsive owners simply don’t know that they have an account that is at risk of escheatment. So, even after a customer has been located, a larger task still remains: helping the individual understand and resolve the situation. It is important to employ a variety of communication techniques to maximize the overall number of responses. The most effective means of explaining the customer’s situation and expediting their response is by one-on-one telephone conversations. Direct mail programs can complement telephone outreach by reinforcing the information shared in phone conversations or left on voice mail messages. It is best to customize each communication to address the unique situation of each securityholder/beneficiary whenever possible.

Since the objective in conducting outreach is to reconcile the account and repair a potentially broken relationship, personal interaction is often critical. As discussed, communications with individuals should be considered an opportunity to demonstrate corporate values and the firm’s interest in serving the needs of clients.

Exhaustive manual research efforts produce more reliable results and can increase lost securityholder location rates to 90 percent.
Incorporate Solutions for Inactive Accounts

It is important to develop a formal and persistent knowledge of the inactive population so you can plan communication efforts to contact dormant account owners accordingly. Ideally, you should conduct analysis long before the state-mandated due diligence process kicks in. For instance, it’s best to monitor which accounts have been inactive for 6 months, 12 months, 18 months, etc. and note the relationship with that client. Once this is done, you can filter the results based on the dormancy period in each owner’s state so that you can see how much time remains before escheatment. Obviously, armed with this data, you can prioritize outreach efforts in states with three-year dormancy periods, followed by accounts in states with five-year dormancy periods. Allowing the appropriate time will improve your success at retaining these owners as client. As important, is evaluating the potential impact of proactive searches for new addresses. Although the inactive accounts may appear to have a valid address because mail has not been returned, searches for new address can be successful on 50% or more of the population.

Build a Compliance Plan

Given the current fiscal crises in many states, the risk to accounts from unclaimed property compliance is here to stay, and is only getting more challenging. The trend of states shortening dormancy periods and stepping-up enforcement of inactivity provisions are clear examples that the window of time to protect accounts is narrowing. If brokers focus only on meeting the compliance requirements of SEC Rule 17Ad-17, there will be many valuable account relationships that slip through the cracks. That’s why brokers must take the compliance process seriously and consider it as a small part of the over escheatment landscape. Beyond simply “being compliant” it’s important to embrace the spirit of the SEC Rule 17Ad-17, which is to protect at-risk account owners, and to choose the goal of optimizing service levels for them. As with any new compliance requirement, there will of course be additional internal effort, and potentially significant costs that should not be underestimated. However, the companies that consider the full spectrum of unclaimed property risk and put the proper controls and solutions in place can ultimately protect and improve their bottom line. Keane is equipped with the specialized skills and experience that will empower brokers to minimize the cost of the compliance process and maximize its value.

It’s important to embrace the spirit of SEC Rule 17Ad-17, which is to protect at-risk account owners, and to choose the goal of optimizing service levels for them.

Lean on Keane

Keane is the leading provider of unclaimed property communications, compliance, and consulting services to the financial services industry. We deliver customized solutions for each bank’s unique circumstances to proactively protect as many dormant accounts as possible. We will help you preserve your customers, your reputation, and your bottom line.