

Servicing and Protecting Shareholders Affected by Disaster

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Introduction

In 2017, a significant number of natural disasters, including major hurricanes and wildfires, affected many areas of the United States. Mutual fund shareholders were among the millions of people harmed by these disasters. Though such events often create challenges for shareholders in managing and accessing their accounts, they also create opportunities for scam artists and other criminals looking to take advantage of those in a vulnerable state. The issue of fraud is so common in times of disaster that the Justice Department established the National Center for Disaster Fraud (NCDF) in 2005 following Hurricane Katrina. According to the NCDF, federal prosecutors charged more than 1,300 disaster fraud cases in 49 different districts in connection with Hurricane Katrina.¹

The catastrophic events of 2017 led fund complexes to reevaluate their processes and procedures for servicing and protecting shareholders in a time of disaster. An Investment Company Institute (ICI) industry working group developed this paper to outline high-level considerations and common protocols related to servicing and protecting shareholders affected by a disaster.²

A fund or transfer agent may want to include the considerations outlined within this paper in their existing fraud prevention, suspicious activity, or red flag programs. Additionally, the scenarios summarized within the white paper may be helpful to include in a transfer agent's considerations related to disaster recovery.

This document is not intended to provide any legal advice and should not be relied on for that purpose. It is intended only to serve as a tool to assist fund operations and transfer agent management in their independent evaluation of their service plans as they consider how best to assist and protect shareholders affected by a disaster.

Service Considerations

Shareholders contacting their fund complex following a disaster are likely to be experiencing extreme levels of stress and may expect and need expedited resolutions to their requests. Therefore, it is critical to train call center and other personnel to display compassion and understanding while also being highly attuned to potential red flags and fraud attempts. When a widespread disaster occurs, funds may consider providing customer-facing personnel with refresher training regarding fraud prevention, including identification of red flags, potentially suspicious activity, and escalation protocols and procedures.

¹ The mission of the National Center for Disaster Fraud is to improve and further the detection, prevention, investigation, and prosecution of fraud related to natural and man-made disasters, and to advocate for the victims of such fraud.

² For the purposes of this paper, *disaster* is defined as a large-scale emergency event (e.g., hurricane, wildfire, tornado, significant flooding) affecting a sizable population. However, the concepts outlined in this paper may also apply on a smaller scale or to one-off events.

Additionally, funds may consider developing processes and procedures addressing the following so that they are prepared in the event a disaster takes place:

- » Supporting shareholders who no longer have a permanent address or are temporarily displaced, including identifying what mechanisms are in place to systematically store temporary addresses and identifying processes to validate address change requests received from affected areas of the country.³
- » Supporting shareholders who may require expedited transaction processing (e.g., redemption requests to pay for housing or other bills), including establishing appropriate escalation processes for exception requests and approvals.
- » Establishing protocols for approving general exceptions (as appropriate), including processes for reviewing and approving waivers or alternatives related to Medallion Signature Guarantees (MSGs)⁴ and other requirements.
- » Monitoring US Postal Service resources to determine area(s) where mail service has been suspended or discontinued in response to a disaster. Funds may consider establishing a process to hold mail, including certain regulatory documents, for shareholders residing in specific ZIP codes within the affected area(s).⁵

Displaced Individuals: Abandoned Property/Escheatment Considerations

Significant disasters such as Hurricanes Harvey, Irma, and Maria, as well as the California wildfires often lead to displaced individuals and disruptions to communications and transportation in the affected regions. This in turn can lead to an increase in shareholder accounts deemed abandoned, inactive, or lost as account owners concentrate on rebuilding their homes, businesses, and neighborhoods rather than maintaining contact with their financial institutions. To mitigate the potentially high number of accounts that may become abandoned, inactive, or lost, funds may consider the following:

- » Accelerate the normal process and timing of efforts to reestablish contact with inactive shareholders in affected areas, including initiating the process to reestablish contact with inactive shareholders earlier than customary and increasing the frequency of contact attempts.⁶

³ Mail delivery often continues to unoccupied houses, apartments, etc., until the residents ask for mail services to be discontinued, held, or delivered to a new address. Consequently, criminals searching mailboxes in the affected area may be able to access the residents' personal information. In some cases, fraudsters may change a shareholder's address before the shareholder has a chance to do so to gain access to financial and personal information.

⁴ For more information regarding MSG alternatives, see ICI's *Medallion Signature Guarantee Considerations and Alternatives* white paper: www.ici.org/pdf/ppr_17_msg_considerations.pdf.

⁵ In response to significant disasters, the Securities and Exchange Commission may issue an order that exempts registered investment companies from the requirements to furnish certain regulatory documents when mail delivery is not possible and certain conditions are met. For example, see Release No. 81760 / September 28, 2017, and Release No. 32842 / September 28, 2017: www.sec.gov/rules/other/2017/34-81760.pdf.

⁶ For more information regarding reestablishing contact with inactive shareholders, see ICI's *Suggested Process for Outreach Efforts to Reestablish Contact with Inactive Shareholders* white paper: www.ici.org/pdf/ppr_16_outreach_efforts.pdf.

- » Consider using the “designated representative to receive notice” (applicable for shareholders residing in Texas)⁷ or “trusted contact” (collected under Financial Industry Regulatory Authority [FINRA] Rule 4512⁸) listed on an account to locate “lost” or inactive shareholders in the affected disaster areas. The additional contact information on file may be helpful in locating an inactive shareholder or identifying a new address. Funds should be mindful, however, that designated representatives or trusted contacts often reside near the shareholder and also may have been affected by the disaster.
- » Contact the intermediary of record on an inactive account as another avenue for locating the shareholder or obtaining a new address.
- » Monitor mail returned by the post office (RPO) to the fund or transfer agent. Funds or their transfer agent may consider undertaking additional attempts to locate shareholders residing in specified disaster areas beyond standard protocols.
- » Encourage shareholders to register for e-delivery to reduce the volume of paper documents delivered by regular mail and the quantity of RPO mail.

State government offices also may be affected by a disaster, which could affect scheduled escheatment or other regulatory filings. Funds and their transfer agents should confirm that the relevant state offices are open and accepting filings before submission.

Fraud Prevention Considerations

As noted above, fraud generally follows disasters. Unscrupulous contractors and phony insurance scams abound, but identity theft is far and away the most common crime. Identity thieves often claim to be from the Federal Emergency Management Agency (FEMA), a state government office, or a volunteer group. They will ask for an applicant’s Social Security number (SSN), bank account number, or other sensitive information to achieve their goal of stealing personal identities and money. They will even search through storm debris or unattended mailboxes for financial statements or papers. To protect shareholders while being responsive to their needs, funds should consider:

- » Emphasizing with call center and other customer-facing personnel the need for heightened awareness regarding the increased exposure and opportunity for fraud following a major disaster. It is important that funds and their transfer agents balance compassion for the shareholder’s experience with hypervigilance against fraud.
- » Having knowledge of common and evolving fraud schemes. Funds can keep abreast of fraud trends and monitor for fraud alerts from various federal and state agencies, including FEMA, the Financial Crimes Enforcement Network (FinCEN), the Federal Bureau of Investigation (FBI), and the Department of Justice (DOJ).

⁷ See Texas House Bill 1454 for more details: www.legis.state.tx.us/tlodocs/84R/billtext/html/HB01454F.HTM

⁸ See www.finra.org/sites/default/files/Regulatory-Notice-17-11.pdf.

- » Coordinating with internal data security groups. Often internal data security groups or cybersecurity teams within a fund complex have relationships with various law enforcement agencies and are alerted to various scams and current trends related to criminal activity.
- » Monitoring postal delivery routes to determine when to hold mail to affected areas. Often the post office continues delivering mail to uninhabitable areas or neighborhoods, which increases opportunities for mail to be stolen. Identity thieves often will identify uninhabitable neighborhoods and impersonate homeowners to change a mailing address.

In advance of a disaster, funds and their transfer agents should contemplate instituting the following practices (if not already in place) to mitigate instances of fraud:

- » Implementing additional layers of authentication (e.g., additional challenge questions for shareholders in specified areas or ZIP codes)
- » Reviewing existing control environment for key controls that rely on customer contact via hard copy mail and consider alternative or compensating controls for shareholders whose address of record falls within an area affected by disaster
- » Working with the broker-dealer of record to authenticate the shareholder or a specific transaction request
- » Implementing heightened monitoring of transactions for shareholders residing in specified areas or ZIP codes
- » Instituting a process to revalidate requests for address changes or one time or temporary changes to an account
- » Employing technological solutions (e.g., voiceprint, biometrics, tokens) to assist with shareholder authentication
- » Employing vendor solutions that enable verification that a bank account registration added to a shareholder account matches the account registration
- » Prohibiting redemptions to a newly added bank account for a specified period
- » Employing real-time alerts of transaction activity via text or email to a designated phone or email address

Shareholder Education Considerations

Another important defense against fraud is shareholder education. Providing shareholders with information on how to protect their personal information and accounts can significantly reduce instances of fraud. Similarly, educating shareholders on steps they can take in advance of a disaster can assist in limiting instances of fraud while providing account owners with easier access to their accounts in a time of need.

Funds should consider establishing an educational resource page related to fraud prevention and disaster preparedness on their website and developing educational material, such as a brochure, that could be included with shareholder quarterly or annual statements. Funds might include the following topics in any educational resource developed:

- » The importance of protecting nonpublic personal information (e.g., SSN), passwords, and financial records and steps to take to do so
- » Ways to keep financial data secure
- » Options for storing copies of financial records in an electronic-secure manner that can be easily recovered following a disaster (e.g., online, cloud storage)
- » A list and description of common fraud schemes
- » Links to fraud prevention resources (e.g., Financial Fraud Enforcement Taskforce, FINRA, AARP)
- » How to set up fraud alerts and place a credit freeze with the three major credit bureaus
- » Disaster contingency planning fundamentals such as:
 - » How to establish online access
 - » The value of online access in the time of a disaster, including ease of access and decreased reliance on paper records
 - » How to register for e-delivery (eliminating the need for paper delivery of documents)
 - » How to preestablish banking information to allow for quick and convenient access to money versus waiting for the receipt of a check
 - » The importance of providing your financial institution with alternative contact information such as an email address and cell phone number
 - » Having the post office hold mail delivery until it is appropriate and safe for delivery to resume

Summary

Advanced planning, training of frontline personnel, and vigilance by funds and their transfer agents, coupled with a strong shareholder education program, can significantly reduce incidents of fraud following a disaster.

Additional Resources

Funds and their transfer agents should take advantage of the fraud prevention and related resources provided by the federal government and others. Examples of helpful resources are provided below.

Regulatory Resources

Regulators often issue guidance and exemptive orders following a major disaster. Funds and their transfer agents should monitor the SEC, Internal Revenue Service (IRS), and Department of Labor (DOL) closely for any relief or guidance issued. Examples of guidance and relief issued:

SEC

- » www.sec.gov/news/press-release/2017-181

FinCEN

- » www.fincen.gov/sites/default/files/advisory/2017-10-31/FinCEN%20Advisory%20FIN-2017-A007-508%20Compliant.pdf

IRS

- » www.irs.gov/pub/irs-drop/a-17-13.pdf
- » www.irs.gov/pub/irs-drop/a-17-11.pdf www.dol.gov/newsroom/releases/ebsa/ebsa20170830

DOL

- » www.dol.gov/newsroom/releases/ebsa/ebsa20170915
- » www.dol.gov/sites/default/files/ebsa/about-ebsa/our-activities/resource-center/faqs/for-participants-and-beneficiaries-following-hurricanes-harvey-and-irma.pdf

Government Resources

FEMA

- » www.fema.gov/disasters
- » www.fema.gov/news-release/2016/05/11/be-alert-disaster-related-fraud-and-scams

DOJ/NCDF

- » www.justice.gov/disaster-fraud

ICI Resources

- » Business Continuity Resource Center
www.ici.org/continuity
- » *Emergency Pricing Procedures Under the Investment Company Act*
www.ici.org/pdf/13_emergency_pricing.pdf
- » *Mutual Fund Operations Planning Guide for an Unexpected Market Close*
www.ici.org/pdf/14_ops_manual_marketclose.pdf
- » *Medallion Signature Guarantee Considerations and Alternatives*
www.ici.org/pdf/ppr_17_msg_considerations.pdf



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