KAGE
STRATEGY

Principle 6 Customers' interests

A firm must pay due regard to the interests of its customers and treat them fairly.

Unclaimed assets

A compelling business case for action

Principle 7 Communications with clients

A firm must pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading.

Even without the threat [of legislation], the problem of dormant accounts . . . is not something a responsible management can ignore. Any financial organisation has a moral and fiduciary responsibility to do all it can to make sure that assets go to those who are entitled to them, and of course it is also a central plank of the FSA's principle of Treating Customers Fairly. But it is a resource-intensive process, and a heavy extra workload on a thinly-staffed organisation.

Anthony Hilton, 2009

Introduction | The need to address unclaimed assets

The purpose of this research report is to highlight an issue that is largely inconvenient or embarrassing for firms, for regulators, for the media and for individuals affected it: **unclaimed and dormant client assets**.

In the normal course of business, retail insurers and asset managers lose contact with a portion of their retail customer base; for example, new residents at addresses to which the firm sends mail may return that mail indicating the addressee is not at that address; he or she has "**gone away**" – the name given to clients with whom the firm knows it has lost contact. But this is just one method through which contact may be lost; and firms usually are not aware of all the clients with whom they have lost contact – they will have "unknown gone-aways" – which may also be material.

As a leading law firm quoted in this research report notes, the "responsibility" for loss of contact relating to these assets is typically the client him- or herself. Compounded by tortuous regulation which is peripheral to the real problem of firms failing to trace lost clients and repatriate their assets, unclear responsibilities have excused inaction by firms over time, leading to the build up of significant values of unclaimed assets originating from long-term products in insurers and asset managers.

What is the total value of such unclaimed assets? A key problem is that the interested parties – and there are several – do not know. The Financial Conduct Authority, the Bank of England, the government-appointed Dormant Assets Commission, are all guessing. There is no reliable estimate of value of unclaimed assets available. There should be; a matter we have attempted to address, as noted in this research report.

Among the parties, meanings of the terms used relating to unclaimed assets have not yet coalesced around accepted definitions; terminological confusion has added to the substantive confusion surrounding the issues. We start by attempting to clarify meanings and terms, at least as we use them in this research report.

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Overview

- **The FCA estimates the value of unclaimed assets in insurers and asset managements to be between £10 and £20 billion. It has stated it considers the levels of gone-away clients 'unacceptable'.**
- **The FCA has stated that firms with long-term products need to be more effective at maintaining contact with clients and at tracing those clients with whom they lose contact.**
- **The FCA considers that its treating customers fairly objective trumps narrow interpretations of customer terms and conditions.**
- **The Government's Dormant Assets Commission is likely to refer the issue of unclaimed assets back to the FCA for resolution in consultations with the asset management and insurance industry bodies.**
- **Firms with unaddressed pools of unclaimed assets face material and growing reputation risk as the issue gains increasing regulatory and media salience.**
- **The EU's new data protection regulation, GDPR will come in to effect in May 2018. After Brexit, GDPR will continue to apply to firms' EU business. Its subsequent applicability to UK customers will depend on the ultimate relationship to the Single Market.**
- **Fines for violating the accuracy provision are up to EUR 20 million or 4% of global revenues, a 20-fold increase over the current maximum penalty in UK law.**
- **GDPR requires that personal data be kept up to date and, where data are inaccurate firms must use "every reasonable step" to rectify inaccurate data "without delay."**
- **Gone-away clients and unclaimed assets may arise from inaccurate personal data. They expose firms to the full penalty provisions of GDPR.**
- **GDPR allows firms to process personal data in the 'vital interests' of the data subject, even where no explicit, pre-existing contractual permission exists.**
- **Under GDPR, firms face a new requirement to demonstrate how they rectify inaccurate personal data relating to owners of unclaimed assets; not only must they act, they must document and explain how they act.**
- **Increasing attention from the FCA to gone-away clients and unclaimed assets and the provisions and penalties of GDPR should encourage asset managers and insurers to review their decision calculus.**
- **To avoid unwanted supervisory attention and risk of penalties under GDPR, firms should act on their unclaimed assets and gone-away clients without delay.**
- **While addressing unclaimed assets is potentially expensive for firms, near-zero-cost options exist that have been shown to be effective, have been accepted by the FCA and protect firms from action on unclaimed assets under GDPR.**

Executive summary

Across the financial services industry, insurance and asset management firms have accumulated billions of pounds of unclaimed assets. There is no reliable data on the value of unclaimed assets; the FCA has recently **estimated the figure to be between £10 and £20 billion**. Firms are likely significantly to underestimate their unclaimed assets as they may have a pool of gone-away clients of whom they are unaware; in some legacy books, these 'unknown gone-aways' have been shown to be at levels as high as **20% of clients**.

In March 2016, the Financial Conduct Authority (FCA) published the results of a thematic review of closed books in the life insurance sector. Their findings were unequivocal: firms across the financial services sectors with long-term products need to be more effective at maintaining contact with clients and at **tracing those clients with whom they lose contact**. The FCA considers the level of gone-away clients unacceptable. They advocate more active tracing including use of external tracing agents. Importantly, they consider that their principle of **treating customers fairly** trumps narrow interpretations of customer terms and conditions that have contributed to inertia by firms on dealing with the unclaimed asset problem. They appear **likely to increase supervisory attention** to client assets and treatment of gone-away clients.

During 2016, the Dormant Assets Commission (DAC) has looked at the possibilities of transferring long-dormant unclaimed assets to the charities sector under government direction; the DAC has considered many of the issues involved in tracing gone-away clients and repatriating unclaimed assets. They will report to the Government in December 2016. They have indicated that they are likely to recommend a regime for client money that streamlines transfers to charity; for unclaimed client assets, they are likely to refer the matter back to FCA for further consultation with industry. There is a clear logic in addressing transfers of dormant, unclaimed assets to charity at an industry level. But, in the absence of a market failure, a government-imposed and directed solution is unjustified. Both insurance and asset management sectors should organise **industry-level solutions to transferring dormant assets to charity** independently of Government that address issues in which their original owners have a clear interest: savers, saving and household-level risk transfer.

Whatever the DAC's recommendations, the Government's subsequent consultation process around their proposed changes will raise the profile of the unclaimed assets issue. Firms that have failed to act risk unwanted media and public attention and **reputational damage**.

In May 2016, the EU's approved its **General Data Protection Regulation** (GDPR), which will come in to effect from 25 May 2018. **GDPR is a game-changer.** Among its other provisions, GDPR requires that personal data be kept up to date and, where data are inaccurate – as may be the case with gone-away clients – **firms must use "every reasonable step" to rectify inaccurate data "without delay."** Fines for violating this provision are up to an eye-watering **EUR 20 million or 4% of global revenues**, a 20-fold increase over the current maximum penalty in UK law. After Brexit, this provision will continue to apply to firms' EU business. Its subsequent applicability to UK customers will depend on the ultimate relationship to the SIngle Market. Firms choosing to limit UK customers' rights following Brexit risk the opprobrium of supervisors, the media and customers alike.

In its work on dormant assets, leading law firm Eversheds has raised issues about the legality of and potential liabilities attendant to firms investing a client's funds in assets after the client's death. Their view is that legal precedent establishes that such actions are not authorised. This raises the stakes on returning clients' assets post-mortem.

For firms, in addition to the balance sheet and incentive impacts of repatriating unclaimed assets, acting on unclaimed assets and tracing gone-away clients can be expensive. Tracing services provider **Assets Recovered** has a business model that is **near-zero-cost** to firms. It provides new address data on live clients with success rates that set new performance benchmarks for tracing – achieving results of **over 90% on an asset manager's gone-away file** – without charge to the firm. For returning balances to the estates of deceased clients, Assets Recovered levies an **opt-in charge of 10% of principal value** (plus VAT) for balances above a de minimus level. The FCA is **aware of and has stated it is comfortable with the business model**. This represents a low-cost opportunity for firms to resolve their unclaimed asset balances.

There is a pressing need for better data on unclaimed assets. Kage Strategy is collaborating with EY, Eversheds, the Investment Association, the Wealth Management Association and Assets Recovered to **undertake research on both the scale and scope of the unclaimed assets problem**.

The unclaimed assets problem has grown to a scale where it can no longer be ignored by regulators, supervisors or government. Nor, as a consequence, can firms abrogate any longer responsibility for resolving it. Firms must take action before they attract media attention and material adverse publicity. Under new EU data protection regulation, fines for failing to address unclaimed assets are signficant enough to force insurers and asset managers to reconsider their decision calculus. The risks of inaction are real, pressing and growing. The business case for firms to deal directly with their gone-away client and unclaimed assets problems is compelling.

Definitions of unclaimed assets

Within the topic of **unclaimed assets**, there are two definitional issues:

- what are different categories of unclaimed asset (the **classification** issue)? and
- when does an asset become unclaimed (the **trigger** issue)?

We address each of these in turn. Note that in these definitions, assets includes money balances.

The classification issue

Not all unclaimed assets are the same. The differences have caused considerable confusion among both regulators and practitioners. In the following table, we set out the relevant classifications.

These terms are largely common sense. Better differentiation between these classes of unclaimed assets would enable practitioners and regulators to understand more clearly the scope and scale of the unclaimed assets problem and the expected or reported efficacy of solutions.

Trigger events

Triggers for the respective definitions will be based either on events or passage of time. Time-based triggers are self-explanatory. **Event** triggers may be **positive** – an event occurs; or **negative** – a required or expected event fails to occur. Examples of these are mail is returned saying "not at this address" (positive) or customers fail to respond to a request to contact the firm or to cash a cheque (negative).

Table 1 Useful terms for classification of 'unclaimed assets'

Term	Definition	Time trigger	Event trigger	Re: tracing
Unclaimed	Assets where the status or whereabouts of the ultimate owner are not known by the firm	potentially	potentially	before or after
Inactive	No activity on the account by the customer over a specified period of time	specified period		na
Gone away	Client has failed to respond to requests for information or mail is returned		mail returned	pre-trace
Orphaned	Assets where firm the ultimate owner has died		death	post-trace
Untraceable	Client records where there is insufficient client data to identify a client uniquely			trace not possible
Dormant	Orphaned or untraceable assets that have been inactive for a specified period	specified period	inactivity	post-trace
Unallocable client money	Money in firms' client money accounts that cannot be allocated to specific clients		funds applied by firm	no originating client

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Unclaimed assets

A compelling business case for action

SECTION 1

The regulator's view

Of late, the Financial Conduct Authority has underscored its commitment to dealing assertively with issues of handling of client assets. Since 2013, the FCA has levied significant fines on firms it has found to have violated the key provisions of its client assets regulatory sourcebook, referred to as CASS.

While none of these fines deals specifically with either the quantum of or firms' treatment of unclaimed assets, the fines demonstrate a pattern of increasing attention by FCA supervisors to client asset issues. Recent FCA work backs up the trend.

In March 2016, the FCA published the results of a thematic review titled *Fair treatment of long-standing customers in the life insurance sector*. The emphasis of the review was **treating customers fairly** (TCF). Among the key outcomes of the thematic review, the FCA focused on firms' handling of gone-away clients. Although the review focused on the life insurance sector, the FCA made it clear its findings applied more widely, especially to "other sectors which sell retail investment products."[1]

Generally, the FCA was unimpressed, describing "poor customer outcomes being delivered through ineffective 'gone-away' processes . . ."[2] The FCA noted that over half of the firms reviewed demonstrated weaknesses in their management of gone-away customers that "had resulted in, or were very likely to result in, poor customer outcomes."[3] Such firms, the FCA noted pointedly, "have a higher risk of not treating [such] customers fairly."[4]

The scale of the problem is unclear; the FCA, itself, is uncertain:

> The scale of the total amount left unclaimed by customers is large. Estimates vary between £10 and £20 billion across the financial services industry. The Unclaimed Assets Register suggests there is approximately £4 billion in life assurance and pension schemes.[5]

Firms can lose contact with customers for a wide variety of reasons; the most common causes are likely to be failure to notify the firm of change of address following a house move and death respectively. Analysis by Kage Strategy and tracing provider Assets Recovered shows how readily these gone-away balances can arise through *lost contact associated with house moves*. Based on ONS workforce participation and mortality data for age cohorts over 30 years old (*i.e.* savers) and making a very conservative assumption

Table 2 FCA CASS-related corporate fines since 2013

Firm	Date	Amount	Reason stated by FCA
Xcap Securities	May 2013	120,900	For [a range of] client asset failings.
Aberdeen Asset Managers	Sep 2013	7,193,500	For failing to identify, and therefore properly protect, client money placed in Money Market Deposits with third party banks.
SEI Investments	Nov 2013	900,200	For failing to arrange adequate protection for client money for which it was responsible.
Barclays Bank	Sep 2014	37,745,000	For failing to properly protect clients' safe custody assets.
BNY Mellon London Branch and International	Apr 2015	126,000,000	For breaching Principle 10 and for breaching a number of rules in Chapter 6 of the Client Assets Sourcebook
Towergate Underwriting Group	July 2016	2,632,000	For breaches of PRIN 3, PRIN 10 and CASS related to client money/assets in the general insurance and protection sector.
Aviva Pension Trustees UK & Aviva Wrap UK	Oct 2016	8,246,800	For [multiple] breaches . . . related to client money/assets and culture/governance in the life insurance sector.

1 Financial Conduct Authority, *Fair treatment of long-standing customers in the life insurance sector,* March 2016, para. 1.16

2 *Fair treatment*, para. 3.81

3 *Fair Treatment.*, para. 3.127

4 *ibid.*, para. 3.125

5 *ibid.*, para 3.124

The regulator's view, cont.

about house movement (mobility) among savers[6] of 1.75% *per annum*, we have shown that over 30 years – a realistic life for a long-term savings product – loss of contact will be significant:

Table 3 Kage Strategy / Assets Recovered analysis of the 'loss of contact' problem

Assumed % contact loss per move	5%	10%	15%	20%	25%
% customers lost over 30 years	3.8%	7.5%	11.3%	15.1%	18.9%

This analysis[7] shows that if 25% of status/address changes result in lost contact from failure to notify to the company as deceased or 'gone-away', over 30 years **the firm would be unaware that it has lost contact with around 19% of its long-term customers**.

The FCA thematic review is clear about the obligations of firms both to pursue actively gone-away customers and to ensure the primacy of the FCA's principles relating to treating customers ahead of contractual limitations on contact and follow-up with customers. In its thematic review, the FCA states:

> Firms that did not have the customer at the heart of their businesses generally relied on strict compliance with contractual T&Cs which they felt would automatically result in fair outcomes for their customers, without taking any other action to ensure fair outcomes. [8]

The FCA notes that contractual terms and conditions are not the last word in *treating customers fairly*; they note, further:

> Firms' obligations under our Principles for Businesses and rules are wide and require them, amongst other things, to consider customer outcomes . . . [D]elivering against contractual T&Cs is an important part of treating customers fairly. However, strict compliance with delivering what is required by T&Cs only, without considering wider outcomes, might not necessarily ensure a fair outcome for customers. [9]

The implication is clear: the FCA expects firms to apply their judgment to interpreting contractual terms and conditions to ensure that firms treat customers fairly, including in relation to contacting gone-away customers; firms should not interpret their original contractual terms and conditions narrowly to limit actions to identify and trace gone-away customers.

The FCA thematic review was clear that firms should use all means at their disposal to increase the effectiveness of their gone-away client processes, including, specifically, use of external tracing agents where these providers could demonstrate superior performance.[10]

Not only has the FCA been clear that its findings and guidance in its thematic review apply across sectors dealing with long-term products, it is clearly increasing supervisory attention to CASS issues and has stressed that dealing with existing customers who have become inactive is one of its priorities in 2016/17.[11] This suggests that firms that fail to deal effectively with gone-away customers will face increasing supervisory pressure; fines may ensue.

The FCA estimates the scale of the total amount left unclaimed by customers is £10 and £20 billion across the financial services industry

The conclusion is inevitable that the **FCA is increasing supervisory attention to firms' treatment of gone-away customers across all sectors that deal with long-term products; both insurers and asset managers will be targeted**. Furthermore, in relation to gone-away, orphaned and dormant assets, regulatory and supervisory pressures are not all these firms will need to contend with.

6 versus a crude mean from ONS mobility data of 4.33%; assumption reflects relatively higher stability among over 30s and savers

7 This analysis is available directly from Kage Strategy

8 *Fair treatment*, para. 1.19

9 *ibid.*, para. 1.20

10 *Fair treatment*, Draft guidance in relation to treating customers fairly, p.49

11 FCA *Business Plan 2016/17*, p. 36

SECTION 2

The Dormant Assets Commission

Announced in December 2015, the Dormant Assets Commission is a creation of the Cabinet Office, established to identify:

> . . . new pools of dormant assets and work with industry to encourage their contribution of these assets to good causes.[12]

The Dormant Assets Commission is tasked with reporting to the Prime Minister and Cabinet Office by the end of 2016.

After a sustained struggle with the definition of dormant assets in each of the sectors, the Dormant Assets Commission sought evidence from firms as to the quantity of dormant assets and issues in their release. It appears from consultation briefings with industry[13] the Commission did not receive the data it expected from firms and has struggled to quantify values for assets across the classifications offered above.

The principal focus of the Dormant Assets Commission is those assets that could be transferred to charity following a suitable period of dormancy. Existing CASS rules permit such transfers after 6 years for client money and 12 years for client assets; this is shorter than the comparable period of dormancy for assets in the banking sector, set at 15 years under the legislation establishing the dormant assets regime in the banking sector.[14] The CASS rules provide for an onerous and somewhat contradictory process for release of money and assets to charity and require firms to retain full liability for any subsequent claims by customers for funds transferred.

From discussions with industry forums, the key issues facing the Dormant Assets Commission appear to have been:

(i) the paucity of data on unclaimed and dormant assets within firms and available from firms – the same problem identified by the FCA's thematic review

(ii) the industry-wide problem of *unknown 'gone-away' clients*: the inability to quantify total gone-away clients and systematic under-reporting of unclaimed assets

(iii) the comparability of treatment of client money and client assets and across asset classes

(iv) potential liabilities associated with variability of asset values subsequent to conversion of non-cash assets to cash and the liability in perpetuity for transfers to charity

(v) legal prerogatives for conversion of assets without client instruction – especially the problem of circumventing trust law

(vi) mandatory versus voluntary elements of any resulting dormant assets regime for insurance and asset management sectors

Views emerging from industry are contradictory. Many have a preference for retaining voluntary adherence to any standards for conversion of client assets to cash and transfer to charities, whether within the existing CASS rules or under a newly-established regime to channel funds to causes selected by Government. However, some firms and representative groups have expressed a preference to make elements of the regime mandatory. This would allow firms to justify their actions under the mandate of the new rules (whether statutory or regulatory) and give clear legislative cover for apparent breaches of trust law or original contractual terms and conditions.

The lack of reliable data on unclaimed assets and dormancy has hampered the Dormant Assets Commission's ability to form robust conclusions.

It is clear that the Commission has been surprised by the looseness of the rules around maintaining contact with customers and the informality of the regime for handling loss of contact and subsequent

12 Dormant Assets Commission, Terms of reference, 10 March 2016

13 The Dormant Assets Commission established working groups in, among other areas, asset management and insurance. The working groups' deliberations have been conducted under 'Chatham House rules', with permission given to discuss the status of consultation. We have participated in the asset management working group.

14 Established under the *Dormant Bank and Building Society Accounts Act* 2008

The Dormant Assets Commission, cont.

tracing obligations. However, the lack of reliable data on unclaimed assets and dormancy in asset management and insurance sectors has hampered the DAC's ability to form robust conclusions. From their most recent feedback, given the complexity of the issues they have confronted, their preferred solution appears to be to refer issues back to the FCA for clarification, consultation with industry, rule-making and subsequent enforcement. Usefully, they have divided the problems in to (i) dealing with legacy issues and old books and (ii) on-going management of 'gone-aways'.

Any regime associated with limitation of liability for transfers to charity would only be feasible at far higher levels of tracing performance than are currently common. For example,

Performance at tracing gone-away clients

working with the 'gone-away' element of an aged book of an asset manager, Assets Recovered managed to trace over 90% of clients identified as gone-away for which in-house tracing had already been attempted and identified current addresses for almost 85% of those clients

Addressing 'unknown gone-away' clients

from a 'live-client' file, Assets Recovered identified over 20% as 'unknown gone-aways' that had either moved to a new address or died.

From these results, just as the FCA indicated in its thematic review, it is clear that the insurance and asset management sectors' management of gone-away customers is insufficiently effective. Given the observed levels of both untraced gone-away clients and unknown gone-aways, significantly increased transfers to charity under existing CASS rules would leave firms with unmanageable liabilities in perpetuity for balances transferred. It appears likely the Dormant Assets Commission will identify as areas for additional rule-making:

(i) improved mandatory reporting requirements for gone-away client money and assets and asset dormancy

(ii) increased and on-going know-your-customer obligations and frequency of customer 'touches' throughout the life-cycle of long-term products

(iii) increased sensitivity of triggers for customer tracing and enhanced tracing protocols where firms have lost touch with customers

SECTION 3

Unclaimed assets as a reputational risk

Either way, it seems likely that the Dormant Assets Commission will not see business-as-usual as an acceptable outcome of its deliberations and will motivate greater attention to unclaimed assets and dormancy at the FCA.

The Dormant Assets Commission will report to the PM and Cabinet Office in December 2016. Those offices, in search of positive news stories, will, entirely conceivably, seek to move rapidly on their findings and recommendations. In consultative meetings, the Dormant Assets Commission has suggested their work will emerge publicly as a 'Green Paper' – a government consultation document. Once that is published, the issues of unclaimed and dormant assets will be very clearly in the public domain.

If the FCA is correct and the figure of unclaimed assets is between £10 and £20 billion – and that is the only official figure in the public arena, the failure of financial services firms to seek actively to repatriate those assets to their rightful owners is likely to create a significant media and public reaction. If firms holding unclaimed assets continue to delay action on repatriating those assets, they risk incurring material reputational damage, especially once data on successful repatriation of unclaimed assets begins to emerge.

Assuming the Green Paper appears in mid-2017, firms have a window for action that they would be wise to utilise. Those firms that move deliberately and vigorously to address their unclaimed assets can position themselves to benefit positively from the emerging publicity of the issues.

Firms face a relatively stark choice on unclaimed assets: act now or risk subsequent reputational damage

When it comes to unclaimed and dormant assets, insurers and asset managers with significant gone-away clients face a relatively stark choice: act now or risk reputational damage as the progress of the Government's dormant assets initiative increases media and public attention and, inevitably, opprobrium on firms that have relied on customer and regulatory inertia.

SECTION 4

GDPR: a game-changer

The following is our opinion based on reviewing GDPR and related documentation. We have prepared this statement for information purposes only; it is not intended as and should not be relied upon as legal advice. We accept no liability for firms relying on our opinion. Firms wishing to understand their obligations under GDPR should seek their own legal advice.

After four years of consultation and negotiation, in May 2016 the EU issued the General Data Protection Regulation or GDPR. Because the EU has issued it as a regulation, GDPR applies automatically; it does not require transposition in to domestic law and will apply uniformly across the EU from 25 May 2018. At the earliest, Britain will exit the EU from March 2019 meaning all UK firms will be subject to its provisions for a minimum of 10 months. Depending on the form of relationship to the EU adopted in exit negotiations, from the point of exit, UK firms may no longer be subject to the provisions of GDPR in relation to their UK business; however, GDPR will apply to the EU business of all firms that offer goods or services to EU citizens.[15]

While it may be defensible legally, applying one privacy rule to EU customers and another to UK customers is a domestic public relations disaster waiting to happen. Similarly, reducing recently-introduced withdrawing GDPR protections for UK customers as a result of leaving the EU would place firms in an invidious position: having to justify publicly or to regulators or supervisors or both the firm's decision to take advantage of customers' reduced legal protections resulting from EU exit. In either case, firms would need to take or could reasonably be inferred to have taken a conscious management decision to disadvantage customers by withdrawing protections bestowed under GDPR.

The attention-grabbing element of GDPR is the level of fines for infringements: GDPR provides for "administrative fines up to 20 000 000 EUR, or in the case of an undertaking, up to 4 % of the total worldwide annual turnover of the preceding financial year, whichever is higher."[16] For UK firms, this represents a colossal increase in potential penalties. To date, the highest fine levied by the UK Information Commissioner's Office has been £400,000 against TalkTalk Telecom Group in October 2016[17], 80% of the statutory maximum under the Data Protection Act 1998 of £500,000. For UK firms, GDPR will represent a 20-fold increase in the prescribed maximum penalty for breaches of applicable privacy legislation and regulation (except for firms with revenues in excess of €500 million – where 4% of global revenues will be higher). Importantly, the scope of exposure has also altered.

While there are material changes from earlier EU and UK legislation to the scope of rules UK firms face, in relation to unclaimed assets of asset managers or insurers three key provisions apply:

- Accuracy of personal data
- Accountability provisions, and
- Lawfulness of processing personal data

Every reasonable step

In relation to unclaimed assets, the most significant provision in GDPR is the requirement under Article 5(1) that . . .

> "personal data shall be . . . (d) accurate and, where necessary, kept up to date; every reasonable step must be taken to ensure that personal data that are inaccurate, having regard to the purposes for which they are processed, are erased or rectified without delay ('accuracy')."

This accuracy provision clearly applies to the personal data about ultimate owners of assets, whether claimed or unclaimed. In the case of unclaimed assets and gone-away clients, firms must take "every reasonable step" to ensure customers' contact data are rectified; sitting still on a pile of 'gone-aways' or unclaimed assets is no longer an option; efforts cannot be cursory or limited. This obligation requires asset managers and insurers to deal with their unclaimed asset problem "without delay," or face potential fines of up to €20 million. While firms may gamble on their period of exposure and reversion to *ex ante* UK legal provisions or the efficacy of enforcement, when combined with the increasing salience of unclaimed assets publicly and for regulators and growing supervisory attention, firms doing so will be taking an enormous risk.

15 under Article 3(2)a)

16 under Article 83

17 ICO's TalkTalk Telecom Group PLC's monetary penalty notice at https://ico.org.uk/media/action-weve-taken/mpns/1625131/mpn-talk-talk-group-plc.pdf

GDPR: A game-changer, cont.

Not only must firms rectify inaccurate data, under Article 5(2) they must also demonstrate compliance (referred to as "accountability" under the Article). Guidance on GDPR prepared by the Information Commissioner's Office states:

> The GDPR includes provisions that promote accountability and governance . . . While the principles of accountability and transparency have previously been implicit requirements of [UK] data protection law, the GDPR's emphasis elevates their significance.
>
> You are expected to put into place comprehensive but proportionate governance measures. Good practice tools that the ICO has championed for a long time such as privacy impact assessments and privacy by design are now legally required in certain circumstances.[18]

That is, GDPR requires that asset management and insurance firms demonstrate how they rectify personal data relating to owners of unclaimed assets. This places the onus for action and demonstration of compliance squarely on asset managers and insurers; not only must they act, they must document and explain how they act and how they satisfy the requirements to take 'every reasonable step' to rectify unclaimed assets 'without delay'.

Previously, some firms have been unwilling to act on unclaimed assets because they have not had explicit contractual authority to do so or to engage external tracing agents to do so; GDPR provides a solution. Under Article 6,

> 1. Processing shall be lawful only if and to the extent that at least one of the following applies:
>
> (b) processing is necessary for the performance of a contract to which the data subject is party or in order to take steps at the request of the data subject prior to entering into a contract;
>
> (d) processing is necessary in order to protect the vital interests of the data subject or of another natural person;
>
> (f) processing is necessary for the purposes of the legitimate interests pursued by the controller or by a third party . . .

Together, these provisions clearly imply that, where the processing of data is in the interests of the 'data subject' – the customer, it is lawful regardless of the existence or not of prior contractual authority. Returning assets to their rightful owner is clearly an implied element of the "performance of a contract to which the data subject is party" and in the "vital interests of the data subject." Because there is a "link between the purposes for which the personal data have been collected and the purposes of the intended further processing" – a consideration for data controllers under Article 6(4) – these provisions indicate that, even where firms do not have explicit, prior contractual approval to use clients' data to trace unclaimed assets, to do so is lawful under GDPR. This is a very useful clarification of legal position.

Firms must take "every reasonable step" to ensure customers' contact data are rectified; asset managers and insurers must deal with their unclaimed asset problem "without delay," or face potential fines of up to €20 million.

The GDPR is here to stay for business conducted in the EU; its ongoing applicability within the UK will depend on the terms adopted for Brexit. However, regardless of those terms, it will apply for a minimum of 10 months to UK firms' domestic business. The scale of potential fines are such that firms cannot afford to risk actions under GDPR. To avoid exposure, asset managers and insurers must develop and implement plans that take every reasonable step to rectify clients' data and do so without delay. Even those firms that assume the risk of inaction and escape penalties under GDPR will have a hard job explaining to regulators and supervisors and to the media and, ultimately, to customers why they have chosen a path of inaction or limited action. The provisions of GDPR strengthen not only the hand of ICO; they also provide clear ammunition to the FCA. The financial benefits of inaction on unclaimed assets to firms no longer appear worth the risks it creates.

18 ICO, 2016, Overview of the General Data Protection Regulation (GDPR), 13 October, available online; at p.27

SECTION 4

Finding a cost-effective (and workable) solution

Tracing gone-away customers is a specialised task that is not core to the operations of insurers or asset managers. Many firms maintain 'gone-away' teams but, often, their performance is either not measured or, when it is measured, is unimpressive. Similarly, because of the age of many older books, use of matching routines from personal data providers is often ineffective at tracing clients from legacy systems whose records were generated before the industry adopted more comprehensive KYC routines at client take-on. With third-party administrator fees for tracing activity prohibitive (and their results no more impressive than those from using personal data from commercial providers), the options facing firms seeking cost-effective tracing are limited.

Tracing service Assets Recovered operates differently, both in terms of its tracing process, InTrace®, and its pricing model. By combining multiple data sources and human intervention, Assets Recovered achieves greatly improved efficacy in tracing for both known and unknown gone-away customers.

More about tracing performance

For an asset manager that operated on-going in-house tracing, Assets Recovered traced both 'gone-away' and 'live' clients in aged books. In the 'gone-away' file, Assets Recovered traced 91.0% of clients of which almost 7% were deceased; in the 'live' file, they identified over 20% of client records as 'unknown gone-aways' where the client had either moved or died.

Results such as these greatly exceed the effectiveness observed in the FCA thematic review of long-data products in the insurance sector.

However, it is the pricing model that makes this offering especially interesting to insurers and asset managers needing to address their unclaimed assets.

A near zero-cost charging model

Assets Recovered does not charge for confirming addresses or providing new addresses identified either for gone-away or existing clients (i.e. 'unknown gone-aways'). Instead, in collaboration with the firm (which is identified), Assets Recovered approaches the executors of estates of deceased clients and offers to manage the repatriation of funds owned by the estate from the insurer or asset manager for a fee of 10% of the principal amount (plus VAT) above a de minimus level. The executor can decline service fee and approach the firm directly.

In this way, Assets Recovered can offer a rate of clearance of unclaimed assets that considerably exceeds previous benchmarks at near zero cost to the insurer or asset manager. Both Assets Recovered and Kage Strategy have confirmed the acceptability of the charging model to the FCA[19]; the regulator has noted that such cost-recovery models are used extensively within the industry already.

In its 2016 thematic review, the FCA expressly underscored the primacy of the its Principles favouring tracing of gone-away clients and return of unclaimed assets. Even without express contractual permission in firms' terms and conditions to release client data to tracing firms (provided data security is protected) to repatriate unclaimed assets, the FCA has indicated it supports such tracing. On unclaimed assets, firms are running out of excuses.

19 Assets Recovered explained the pricing model to the FCA CASS regulatory and supervisory team in October 2015. Kage Strategy verified the acceptability of the pricing model in May 2016 as part of a research project in which it is collaborating with EY, law firm Eversheds, industry representative bodies and Assets Recovered to quantify the asset management industry's unclaimed asset problem; *see page 15 below*.

SECTION 5

A legal perspective on unclaimed assets

While considering the issues addressed by the Dormant Assets Commission's deliberations, a major London law firm, Eversheds, has confirmed the FCA's view that charging estates for return of client money and assets is permitted under current rule. In Eversheds' words, the current rules provide that:

> . . . the 'responsibility' for the assets becoming unclaimed lies with the client who forgot to claim them, rather than the firm looking after the assets as a result . . . [so] it would make sense that those firms which return client assets should not be out of pocket for doing so.

Eversheds notes that while current CASS rules on tracing relate to release of unclaimed money and assets to charity *rather than for returning these assets to clients*, use of tracing firms is explicitly condoned as legitimate by existing FCA regulations.[20] Indeed, it is a feature of existing CASS rules – on which the Dormant Assets Commission seems destined to comment and to formulate recommendations – that they do not specifically address any obligation to return unclaimed assets to their rightful owners. However, as the FCA notes in its 2016 thematic review, tracing obligations are well within the scope of FCA Principles 6 (relating to treatment of customers) and 7 (relating to communication with clients).

The most interesting aspect of Evershed's perspective on firms' legal duties in relation to unclaimed assets relates to asset managers' duties (as agent) in the case of a client's (*i.e.* principal's) death. Eversheds notes:

> . . . it is a principle of agency that, since agency is by nature a personal contract, the death of the principal automatically services to terminate the agency, regardless of the agent's knowledge of this death,

citing relevant precedent.[21] Further, Eversheds notes the implications for *post-mortem* action by the asset manager:

> If the investment manager invests into an asset after the death of the client, then this is an action which the investment manager does not have authority to undertake. As such, the estate may have grounds for suing the investment manager in the event that the assets depreciate, on the basis that the investment manager has invested in an asset without authority . . . [Firms] should ensure their clients are not deceased before taking any action on their behalf.

Such a view clearly reinforces the need for asset managers to establish processes to ensure they are aware of, and act upon, the death of clients.

The present regulatory position of unclaimed assets is both unresolved and unsatisfactory; greater clarity and direction from the FCA would be beneficial and appears likely to come from consultation in line with the expected recommendations of the Dormant Assets Commission. However, the FCA's view is unambiguous: firms need to act on tracing gone-away clients and, by implication, returning to them the assets they rightfully own. Certainly, the argument for proactive searches for deceased clients, tracing estates and repatriating to them unclaimed assets appears incontrovertible.

The argument for proactive searches for deceased clients, tracing estates and repatriating to them unclaimed assets appears incontrovertible

20 see CASS 6.2.12 for client assets and 7.11.53 for client money.

21 for example *Campanari v Woodburn* (1854) 15 CB 400 and, for a more general discussion, see Munday, Roderick, *Agency: Law and Principles*, (Oxford: OUP, 2010) at p. 331

SECTION 6

Finding a solution at firm level

Many insurers and asset managers operate gone-away processes using in-house teams and personal data providers. However, as the FCA has shown, their performance is mixed. In addition to providing enhanced tracing performance, use of a leading external provider offers the well-understood benefits of outsourcing non-core activities:

(i) elimination of relatively inefficient internal processes and the cost-saving associated with headcount reduction, and

(ii) improved performance of outsourced processes by focused and specialised providers

Of course, the benefits must be balanced against the costs of outsourcing. There is a reduction of management control or, more accurately, a shift to a contractually-determined process and level of management control and a change in processes of oversight and assurance. There is also a change to control over cost; where previously cost was managed using traditional managerial techniques, cost is now managed contractually and is subject to change in accordance with the terms of outsourcing agreement. As ever, the biggest risk associated with cost comes through unanticipated circumstances for which charges were not specified contractually.

Here, the near zero-cost tracing model Assets Recovered offers firms gives them a third option that has been *on which the FCA has been briefed and which they have accepted*.[22] However, firms still face impediments to action, namely:

- opposition from legal or compliance functions nervous about balancing the FCA's stated position on tracing of gone-away clients and return of deceased clients' assets to their estates against release of data to tracing agents not envisaged in original contractual terms and conditions
- nervousness about moving 'ahead of the pack' in return of unclaimed assets following death
- the loss of assets under management or values insured and related fees
- potential reductions in managerial bonuses relating to AUM or balance sheet or fees

All firms will need to address and resolve these issues for themselves. However, the increasing pressure from the FCA on gone-away clients, the impending publicity associated with Government action following the deliberations of the Dormant Assets Commission and the legal status of deceased clients funds (per the view of Eversheds, above) all suggest that the balance of risks from inaction has shifted.

In order to avoid supervisory attention and, probably, reputational damage, it will not be necessary to resolve all unclaimed balances and (known and unknown) gone-away clients immediately; acting upon these balances and clients is likely to be sufficient to avert supervisory sanction and defend against media attention and public opprobrium. But the window for addressing the issue before it is in the public arena is closing.

A near zero-cost tracing model offers firms an option that has been considered by and accepted by the FCA

22 see details at briefings to the FCA CASS teams at footnote 15, above.

SECTION 7

Options for industry solutions

As noted above, the FCA estimates the value of unclaimed assets across the financial sector as between £10 billion and £20 billion[23]; during its call for evidence, the Dormant Assets Commission did not receive enough data from industry to form a meaningful estimate. Without a clear perspective on the quantum of unclaimed assets in the insurance and asset management sectors, policy-makers and regulators are flying blind.

Kage Strategy, in collaboration with EY, Eversheds, the Investment Association, the Wealth Management Association and Assets Recovered, has commenced a project to sample asset managers' client records and to identify unclaimed assets and deceased clients. The project is seeking participants from the asset management industry to form an estimate of the quantity of unclaimed assets and to review key issues and impediments to action. Firms can find out more about the research at

www.kagestrategy.com/unclaimed-asset-research

The collaborating entities recognise the importance both to the sector as well as to clients of dealing with the unclaimed assets issue and of doing so from a position of information about the scale of the problem. The FCA has offered a statement encouraging firms to participate in research on the problem:

> The FCA welcomes initiatives aimed at increasing industry's understanding of the scope of policy, legal and operational issues in unclaimed and dormant assets and of the scale of the problem. The FCA also welcomes initiatives aimed at resolving and returning unclaimed or dormant assets to their owners and preventing further assets from becoming unclaimed or dormant.

The research will also address the spread of scope issues relating to gone-aways, orphaned and dormant assets and disposal of assets after establishing dormancy (as well as suitable tests for dormancy). At present, dormant assets and unclaimed money can be transferred to a registered charity once the FCA's conditions, detailed in its Handbook[24] have been satisfied. The Dormant Assets Commission presumably intends to recommend that such sums be paid to a Reclaim Fund or similar entity for subsequent allocation on a basis equivalent to that currently applied to funds transferred from banks' and building societies' dormant accounts. *The policy justification for this is highly questionable.* There is a logic to an industry-wide approach: eliminating the potential for accusation of transfers benefiting managers' preferred charitable causes at the expense of the original owners of the assets. But in the absence of a *clearly-articulated market failure*, we believe government stipulation of the destination of funds is unwarranted and invasive.

The insurance and asset management industries can and should organise independent clearing functions for transfers of dormant unclaimed assets to charity to be used in ways that are consistent with the original intent of the saving or risk transfer activity, such as improving financial literacy, as well as other causes selected by the industries' representatives acting consistent with their duties as charitable trustees.

Such a scheme would be consistent with the industries' responsibilities to their original clients, accountable and independent of government.

23 at footnote 5, above; see *Fair treatment*, para. 3.124

24 For client assets, see CASS 6.2.8–6.2.16; for client money, see CASS 7.11.48–7.11.58

About Kage Strategy

We are a strategy consulting firm – we work with clients to create strategy and to amplify and augment existing strategies. We also operateonstrategicissuesacrossse ctors,aswellashowsectors interact and inter-relate strategically.

Our work attends both to qualitative and quantitative analysis to enhance the clarity, reach and impact of strategy in markets and within firms and organisations. We enhance firms' strategic efficacy.

Services we offer include:

STRATEGY CONSULTING We assist firms to add analytic and narrative depth – what we call **DIMENSIONALITY** – to their strategy to enhance its utility, impact and resilience.

GOVERNANCE We assist clients to ensure that their governance structures and processes support their strategy-making and management of uncertainty & risk.

POLICY AND POLICY-MAKING Policy has to be robust to a range of settings or assumptions and relevant variables must be tested in a range of values. Few are; this must change and we can help.

SUPPORT FOR CHANGE When change is constant, the ability to change becomes a source of advantage. We help firms develop a capacity to change and to avoid the need for sudden, dislocating shifts.

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