
Unclaimed property: Considerations for corporate treasury and finance personnel

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Abstract This paper focuses on the importance of unclaimed property to corporate treasury personnel, with an emphasis on regulatory developments in the USA. A number of countries have laws regulating the reporting and remitting of unclaimed property to the respective jurisdictions. This paper provides an overview of what typically constitutes 'unclaimed property', discusses why corporate treasury and finance personnel should keep abreast of current developments in this area, and also discusses how the Sarbanes-Oxley Act 2002 interfaces with state laws regarding unclaimed property. The paper also provides an overview of the state audit process, and concludes by discussing how non-compliant businesses can 'jump-start' their own unclaimed property compliance programme. Companies that should be particularly concerned with unclaimed property include, but are not limited to: companies disbursing a lot of cheques, companies with many employees, banks/financial/insurance organisations, oil and gas companies, healthcare organisations, retailers and entities that issue gift cards, and companies doing business in multiple jurisdictions and/or that have been in business for more than five years. In summary, companies with outstanding obligations to their employees, customers, vendors or owners (ie shareholders, if publicly traded) should be particularly concerned about states' unclaimed property laws.

KEYWORDS: unclaimed property, financial statements, policies and procedures, managing state audits

INTRODUCTION

Many countries have laws regulating the reporting and remitting of unclaimed property

to the respective jurisdictions, and the number of countries with such laws continues to expand. Corporate treasury personnel can play

a key role in all phases of the unclaimed property compliance process (eg assisting their companies or organisations in identifying, tracking, reporting and remitting unclaimed property to the states). In addition, treasury personnel should play key roles in assisting their companies with implementing policies and procedures to identify and track unclaimed property and in the financial statement reporting of unclaimed property.

Although a number of different countries have enacted unclaimed property laws, this paper will focus on unclaimed property laws as they relate to the USA. At the 2009 Annual Conference of the Unclaimed Property Professionals Organization (UPPO), two analysts spoke on the topic of 'foreign unclaimed property reporting'. They noted, for example, that Australia, Belgium, Canada, France, Germany, Hong Kong, Italy, Kenya, New Zealand, the UK, and certain US territories also have unclaimed property or escheat laws.³ Furthermore, analysts who presented on this topic at the 2007 UPPO Annual Conference reported that the Canadian 'equivalent' of the US Uniform Laws Commissioners had been considering a proposed law for Canadian provinces and territories, known as the Unclaimed Intangible Property Act, which, according to the analysts would provide for a priority rule to consider 'last known address and nexus'.⁴ Thus, while the law of each appropriate jurisdiction should be carefully considered to see how it addresses disposition of property that has not been claimed by the rightful owner, the present paper will focus on unclaimed property laws within the USA.

States have been actively pursuing unclaimed property for decades. According to a *Wall Street Journal* article, 'The 50 states collectively held roughly \$35 billion in unclaimed property as of June 2006'.⁵ Experience suggests that it is not uncommon for companies to have large amounts of unclaimed property. However, until notice of an audit assessment is received, many companies typically do not realise that they have unclaimed property compliance

obligations. By developing a general understanding of unclaimed property, as well as the attendant reporting requirements, corporate treasury personnel will be better equipped to assist their companies in both understanding and working their way through the unclaimed property compliance process.

OVERVIEW

Unclaimed property generally has four basic characteristics:

- it is intangible personal property (eg uncashed cheques, outstanding customer credit balances and unclaimed stock certificates), subject to certain narrow exceptions, such as the contents of safe deposit boxes;
- the whereabouts of the apparent owner is not known;
- the property must remain unclaimed by the owner for a period of time prescribed in the statutes as the 'dormancy' or 'abandonment period'; and
- there must be a 'fixed and certain obligation' owed by the holder to the owner.

Common examples of unclaimed property include, but are not limited to, the following: unredeemed gift cards, uncashed payroll and account payable cheques, account receivable credit balances, and mineral proceeds. Once a determination has been made that an entity or organisation is in fact holding unclaimed property, the next question becomes: which jurisdiction is entitled to receive the unclaimed funds? Under the rules of jurisdiction or 'priority rules' promulgated by the US Supreme Court in the seminal case of *Texas v New Jersey*,⁶ the state with the first right to claim the property is the state of the owner's last known address, as shown on the holder's books and records (note: 'holder' is defined in the Uniform Unclaimed Property Act 1995 to mean '... a person obligated to hold for the account of, or pay or deliver to the owner, property that is subject to this Act'⁷). If the holder of the funds does not have the last

known address of the owner which would be sufficient for the delivery of mail, then the state with the secondary right to claim the property is the state of the holder's 'domicile', which is the state of the holder's incorporation for corporations, and state of formation or organisation for holders other than corporations. However, definitions of domicile may vary among those jurisdictions that have adopted a formal definition. Thus, the holder should review the unclaimed property statutes of the appropriate jurisdictions before reporting and remitting any unclaimed property.

Corporate treasury personnel should also be aware of the impact of the Sarbanes-Oxley Act 2002 on unclaimed property compliance. Under s. 404 of the Sarbanes-Oxley Act, a company must document its management's assessment of the effectiveness of the company's internal control structure. For example, although s. 404 does not specifically cite or address unclaimed property, as part of the company's internal control structure it is crucial to have controls in place to ensure that unclaimed property is periodically identified, tracked and reported to the appropriate state(s). Corporate treasury personnel also need to help ensure that the record retention requirements of the various state laws are observed. One key factor that separates unclaimed property compliance from other compliance obligations (eg tax compliance) is that generally, there is no statute of limitations for reportable unclaimed property which has not been reported to the state. Therefore, unlike a tax audit, state unclaimed property audits routinely reach back over 20 years. As a result, amounts that may not be deemed material in any given year can become material, given the cumulative effect of the unclaimed property audit exposure over a 5, 15, or even 20-year period (ie the sum of the past due unclaimed property plus any interest and/or penalties that could be assessed). (Although the financial reporting aspects of unclaimed property compliance are largely beyond the scope of this paper, the subject is explored further by Andreoli and Osibodu, 2004.⁸)

RELEVANCY TO CORPORATE TREASURY PERSONNEL

Corporate treasury personnel should play key roles in a number of phases involving unclaimed property compliance. First, corporate treasury personnel can assist with implementing policies and procedures to identify and track unclaimed property. For example, two accounting analysts have stated that companies should consider adopting policies that:

- '(i) Control all unclaimed property through separate accounts that are subject to a high level of internal control, (ii) require that all transactions in and out of the accounts have supervisor review and approval, (iii) capture and retain sufficient data on the name, address and taxpayer identification number of the property owner to enable the company to properly report the unclaimed assets to the states, and (iv) follow up on outstanding cheques and credits after six months (not after two or three years when the trail is cold).'⁹

Secondly, in addition to policies to identify and track unclaimed property, corporate treasury personnel, in conjunction with legal counsel, can ensure that there are also appropriate policies and practices in place to report and remit unclaimed property to the appropriate states in a timely fashion. Thirdly, in some instances companies do not recognise and disclose their unclaimed property exposure on their financial statements, consistent with requirements of generally accepted accounting principles. Analysts note that this practice raises '...issues related to recognising and disclosing unclaimed property liability under FASB Statement no. 5, Accounting for Contingencies'.¹⁰ In fact, some companies have sought to reclassify unclaimed property obligations as miscellaneous income or to make other financial statement adjustments. Analysts further note that 'This accounting practice conflicts with state unclaimed property laws, which are designed to preserve the property rights of the "lost" owner and prevent unjust enrichment of the company or holders of the

unclaimed property'.¹¹ Corporate treasury personnel who understand the unclaimed property rules can better assist companies to ensure that their accounting entries and financial statements reflect compliance with the unclaimed property laws.

ROLE OF STATES

With several exceptions for areas where unclaimed property is held by the Federal Government, the regulation of unclaimed property largely resides with the various states.¹² In general terms, the state unclaimed property administrator has three different roles to play in the unclaimed property process. First, the administrator seeks to provide guidance to the 'holder community', so that holders will know the 'rules of the road' for reporting, deadlines for reporting, which forms to use, etc. Secondly, the state administrator interfaces with missing owners to assist them in finding and receiving their unclaimed property that has been reported and remitted to the states. Finally, the state seeks to verify through audit activity that holders are complying with the law.

Corporate treasury personnel need to be aware of their reporting and remittance responsibilities under the unclaimed property laws, which vary considerably from state to state. Most states require the holder to report and remit, on an annual basis, any unclaimed funds in its possession for which the prescribed dormancy period has expired. Once the property has been transferred to a state, the state administrator is required to engage in various acts of due diligence designed to locate the rightful owner and reunite them with their property.

After a company reports property to a state, the state seeks to reunite the missing owner with the property by advertising the property, normally in newspapers or via the internet, through booths at state fairs, and through periodic news releases. The states also provide reporting instructions or reporting manuals for a company to become familiar with the unclaimed property laws, and issue prescribed

forms for the holder community to utilise to report and remit the unclaimed funds to the states. From a company's perspective, the internet provides an excellent vehicle to become acquainted with state laws, state reporting forms and instructions, and special unclaimed property releases by the states. Many of these forms and instructions can be accessed via the website of the National Association of Unclaimed Property Administrators (see www.unclaimed.org), which provides links to each state's website. In the event the state is unsuccessful in locating the missing owner whose property has been reported to it, the states generally hold the unclaimed property in perpetuity as the custodian for the missing owner.

SURVIVING THE MULTI-STATE UNCLAIMED PROPERTY AUDIT

In recent years, perhaps due in part to state budget deficits and in part to the growth of contract audit firms, state audit activity has greatly proliferated. The unclaimed property audits have become more comprehensive in scope, more time-consuming, and more financially significant. Seven-figure assessments are not uncommon. State unclaimed property triggers include:

- recent merger and acquisition activity;
- increased publicity;
- company size;
- specific industry and/or specific property types generated by the company;
- filing reports without the requisite industry property types;
- filing of zero (ie negative) reports.

There are numerous examples of companies that have found out the hard way the consequences of failure to comply with state laws regarding unclaimed property. For example, according to the abovementioned *Wall Street Journal* article:

'Waste Management Inc. received an audit notice from Delaware in 2004. Don Carpenter, the

company's vice president of tax, and his aides reviewed three years' worth of records for items such as uncashed payroll cheques, then extrapolated the results over 20 years. Following what Mr Carpenter describes as "a bit of negotiation," Waste Management paid \$19 million in 2006 to settle its unclaimed property obligations'.¹³

Additionally, a wire story stated that Bank of America paid a total of some \$223m to the states of California and Alaska to settle allegations that it failed to turn over unclaimed monies emanating from municipal bond dividends.¹⁴ Moreover, a wire story stated that Bankers Trust Corp. paid some \$63.5m to federal and New York state authorities to settle allegations that '...it boosted its financial performance by unlawfully diverting millions of dollars from unclaimed customer accounts into its own coffers'.¹⁵

More importantly, many states have adopted an 'anti-limitation' provision in their unclaimed property laws which provide that a state is not limited in recovering abandoned property by statutes of limitations that might otherwise apply to parties to the original agreement from which the unclaimed property arose.¹⁶ Thus, it is not uncommon for unclaimed property audits to reach back for 15–20 years or, in some states, even longer, with attendant assessment of penalties and interest for each year. In prior years, some companies may have thought that unclaimed property might not have a 'material' impact on the financial statements. However, as the authors of a leading article have pointed out, when one compounds interest, and adds penalty assessments over a 20-year figure, a significant or material amount may result. Their example is as follows:

'Assume a company's annual unclaimed property audit liability is \$50,000. Based on the average reach-back (or look back) period of 15 years for holders that have never filed unclaimed property reports, the assessment increases to \$750,000. In addition, the state can levy a failure-to-file penalty of up to 25 per cent of the assessment,

which in our example is \$187,500. In most instances, the state also can impose compound interest, ranging from 10 per cent to 15 per cent of the assessment. Depending upon the number of years applicable to the audit, the initial unclaimed property liability could double after penalties and interest . . . Based on the hypothetical illustration above, the cost of not complying with state unclaimed property laws could be significant enough to have an adverse effect on the company's financial statements'.¹⁷

Although there are a number of different types of state audits, the litmus test in demonstrating a company's compliance with the various unclaimed property laws is the multi-state audit (MSA) conducted on behalf of multiple states, usually by a third-party contract audit firm. A notice of an MSA is usually sent to an officer of a company, and indicates that the state through its contract auditor is conducting a review of the affairs of the company to determine its compliance with the state's unclaimed property laws. The notice normally states that a representative of the states involved in the MSA desires to meet with the company for an initial, exploratory meeting, sometimes referred to as the 'opening conference'. The importance of the opening conference cannot be overstated. It is an excellent forum to discuss a number of key issues that will ultimately affect the course of the MSA. For example, the duration of the 'look-back period' is critical. In other words, how far back in time is the MSA proposed? Which particular legal entities are to be involved in the audit? What is the scope of the audit? What particular property types are under review? What types of documents are being sought? In addition to the issues of immediate concern, a company should also be thinking 'down the road' prior to the opening conference. For example, policies of the key states involved in the MSA with respect to issuance of a 'closing agreement' upon conclusion of the audit should be discussed, as well as their policies with respect to indemnification of the holder for amounts paid pursuant to the terms of the MSA. The issue of whether, and under what circumstances,

additional states may join the MSA at a subsequent date also should be discussed.

The critical aspect of audit defence for an MSA is that a coherent plan should be in place to manage the audit, preferably with input from an adviser that 'has been there before' and is experienced in interfacing with state agents. Certainly it behooves a company to cooperate with the auditors, and provide them with pertinent records in a timely manner.

Practical pointers to simplify the MSA include the following:

- *Select one point person to interface with the state:* This should be someone who has familiarity with the company records, preferably in the area or one of the key areas where there may be exposure.
- *Confirm representation of the state:* Prior to the fieldwork being commenced and prior to responding to any state information requests, written confirmation should be obtained from the states that the MSA representative does indeed have authority to represent the state.
- *Obtain a confidentiality agreement:* At the outset of the audit, the audit agent of the states should sign a confidentiality agreement.
- *Keep communication alive:* Periodic communications need to take place between the point person and the primary state audit agent.
- *Determine what records are available:* At the outset of the audit, a company needs to 'get a handle' on what records are available, and for what periods. In some cases, an officer of the company may be asked to sign a declaration that company records for specific areas are not available beyond a certain date. In addition, if records are not available, a state representative is likely to use 'estimation techniques' to calculate the liability for the period where records are not available.

Another key step in the MSA process is the closing conference. A company should request that they receive the proposed unclaimed property audit findings to be presented at the

closing conference several days in advance, to allow them time to evaluate the proposed findings. At the closing conference, the parties should discuss the administrative process that will lead up to an assessment, and what appeal procedures are in place. As administrative appeals are governed by the laws of each state, this can be a tricky process in an MSA.

GETTING INTO COMPLIANCE

How can treasury personnel reduce their risk and assist their company in complying with the applicable unclaimed property laws? Important elements of an effective unclaimed property programme typically include the following:

- *Identification of unclaimed property exposure:* Conducting a thorough review of a company's books and records to identify and subsequently report any outstanding unclaimed property exposure to the proper jurisdiction.
- *Understanding of state voluntary compliance initiatives:* Being familiar with state unclaimed property 'voluntary disclosure programmes' or 'amnesty initiatives'.
- *Setting the tone at the top:* Adopting a corporate culture and policy addressing compliance with state unclaimed property laws. The policy should be rolled out by an appropriate representative of management, such as the chief financial officer or controller, and should be disseminated throughout the organisation.
- *Development of unclaimed property policies or procedures:* Developing and implementing detailed written procedures for identifying, tracking, and reporting unclaimed property and the retention of related records in accordance with the provisions of applicable unclaimed property laws, educating personnel involved in unclaimed property, and conducting periodic audits to confirm the policy and procedures are effective.
- *Formation of an unclaimed property committee:* An unclaimed property committee or working group should be formed. There are a number of advantages to having such a

committee (eg spreading the tracking and reporting burden among several departments, providing for continuity and retention of information within the organisation, and creating a formal process to ensure compliance with state laws regarding unclaimed property). While each company is structured differently, a representative of the controller's or treasurer's group is critical to a successful committee. Persons from areas with the largest exposure for the company also are likely candidates for the committee. For example, with retailers, someone from the gift card area would be helpful. With oil and gas companies, someone from the land department or revenue accounting area would be helpful. With healthcare organisations, it would be desirable for someone from the accounts receivable credit balance area to sit on the committee. With all organisations, a representative of the legal department would be helpful to serve as an adviser to the committee.

- **Reporting technology:** Companies should consider purchasing a software system to assist them in complying with a myriad of varying state reporting requirements. Chesapeake System Solutions, Inc., which offers the Unclaimed Property Compliance System software, and TRACKER are each reputable companies with a long track record of providing services in this area. Some companies prefer to outsource the reporting function. A discussion of the pros and cons of the different technology solutions to assist in this area is largely beyond the scope of this paper.
- **Regulatory guidance:** Due to the complexities associated with dealing with a myriad of jurisdictions with different reporting dates, different abandonment periods, etc, it behooves a company to utilise a reputable treatise in this area. The recently updated 'Unclaimed Property Portfolio' published by the Bureau of National Affairs (Corporate Practice Series) is an excellent source of information.¹⁸ In addition, CCH offers a

publication entitled 'Unclaimed Property Laws, Compliance and Enforcement', which is also helpful, particularly for newcomers to the area.¹⁹

CONCLUSION

Unclaimed property is a key revenue source for states, and enforcement efforts continue to increase as discussed in the *Wall Street Journal* article described previously. As a result, awareness and involvement in this issue by treasury personnel is important to a company's successful compliance efforts in this area and to ensure that proper procedures are in place to identify and track unclaimed property.

In addition, treasury personnel need to be aware of the rules and holder obligations related to unclaimed property in order to assist their companies in evaluating the difficult questions that arise when a company seeks to determine whether certain unclaimed property may properly be reclassified as an income item, and, in a larger sense, whether a company's financial statements accurately reflect its unclaimed property exposure.

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- 5 Uniform Unclaimed Property Act 1995, s. 1(6). Note: The Uniform Acts are 'normative' in nature, and do not represent the law in any particular jurisdiction unless and until enacted by the legislature of a particular state. However, they provide helpful 'background information' to an understanding of this area. The 1995 Act can be reviewed and downloaded by accessing the website for the National Conference of Commissioners on Uniform State Laws (www.nccusl.org).
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- 7 For example, 29 USC s. 4050, provides that funds being terminated which are attributable to missing participants in pension plans subject to the jurisdiction of the Pension Benefit Guaranty Corporation are required either to be paid to the Pension Benefit Guaranty Corporation, or transferred to an insurance company in connection with the purchase of a group annuity contract. By way of further example, funds emanating from unredeemed US Savings Bonds and uncashed federal tax refund cheques are held by the US Department of the Treasury, although there is currently litigation involving several states and the Federal Government pertinent to the issue of unredeemed US Savings Bonds.
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- 16 A representative example of such a provision may be found in the Uniform Unclaimed Property Act 1995, s. 19(a), which states that 'The expiration, before or after the effective date of this Act, of a period of limitation on the owner's right to receive or recover property, whether specified by contract, statute, or court order, does not preclude the property from being presumed abandoned or affect a duty to file a report or to pay or deliver or transfer property to the administrator as required by this Act'.
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