

Tracking the dramatic changes in abandoned and unclaimed property



Dear clients and alumni,

As we find ourselves with Summer behind us and Fall underway, our attention turns to annual unclaimed property filings. As you are reviewing your potential areas of exposure and dormant properties, don't overlook the relationships you have with third party administrators and the escheatment implications that may result from those relationships. This edition's featured article focuses on key considerations that companies should evaluate related to third party administrators. In addition, we have included summaries of legislation that has been enacted or that we are tracking.

We hope you enjoy reading this edition of our newsletter, and look forward to hearing from you. Your continued feedback is invaluable to us.

Regards,

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National Leader - Abandoned and Unclaimed Property

Unclaimed Property Compliance and the Third Party Administrator

In brief

As states grapple with budget shortfalls, unclaimed property has become an increasingly scrutinized area of compliance, with many states conducting costly examinations lasting many years. Included in the review, states and third party audit firms now examine any third party administrator (TPA) relationships a company might have in assessing compliance with state unclaimed property laws. A holder of unclaimed property that utilizes TPA services should be aware of aspects of the process that may be analyzed by state authorities.

In detail

To focus on core business operations, companies often utilize the services of third parties to perform or administer services on their behalf such as payroll, benefits, and securities, as well as a myriad of other programs. When managing their unclaimed property compliance and reporting responsibilities, companies must consider many issues, including the following:

- Does the company have any TPA relationships?
- What types of property does the TPA administer?
- What are the TPA's unclaimed property reporting obligations for the company?
- What can the company do to mitigate unclaimed property exposure arising from these TPA relationships?

An analysis of any TPA exposure in unclaimed property examinations must begin with a review of property types. A company should perform the review when assessing their overall potential unclaimed property exposure or when preparing for an examination to determine whether the property types applicable to the company's business could lead to an unclaimed property liability.

Of the 100+ property types identified by the National Association of Unclaimed Property Administrators (NAUPA), the most common property types are vendor payments, payroll checks, and accounts receivable credit transactions.

However, companies should not overlook property types that may not be immediately apparent, but are often administered by TPA, such as the following:

- employee benefits, including workers' compensation and 401k plans
- rebates
- gift cards/certificates
- security-related property, including uncashed dividends or untendered shares.

Companies often overlook property types handled by TPAs, under the false assumption that the TPA is responsible for the escheatment of outstanding payments. However, during an examination, the burden of proof will be on the holder of property, rather than the TPA, to prove whether there is an underlying obligation, regardless of who (the holder or the TPA) is issuing the checks. The holder is responsible to determine who has the obligation to report those payments made by the TPA on behalf of the holder.

Along with examining property types, companies must determine the true holder of property. The Uniform Unclaimed Property Act of 1995 defines the true holder of unclaimed property as "a person, wherever organized or domiciled, who is in possession of property belonging to another". Although the definition seems straightforward, the distinction of who the true holder is becomes increasingly complex with TPAs making payments on behalf of companies.

To determine the true holder, a company must review the contract addressing the TPA's services. Is the TPA responsible for escheating outstanding items or are they

refunded to the holder who is then ultimately responsible for escheating those transactions? Is escheatment even addressed in the contract or is there an informal agreement between the parties to address escheatment?

If escheatment is not addressed in the contract, the company can analyze how transactions actually occur to determine who has the reporting obligation. For example, does the TPA or company own the bank account from which payments to owners are drawn? If owned by the TPA, are amounts refunded to the company when payments are outstanding after a certain period of time? If refunded to the company, what does the company then do with those payments?

TPA case law

An analysis of case law helps pinpoint where exposures may lie. Rebates and the TPA relationship were examined in *Fitzgerald v. Young America Corporation*, Iowa District Court for Polk County, No. CV6030 (1/5/2009). Young America, the rebate fulfillment TPA for prominent retailers such as Sprint, Walgreens, and T-Mobile, was the subject of multi-state litigation regarding uncashed rebate checks. Ultimately, the court held that the underlying obligation to pay the rebates remained with the retailers, not Young America. Thus, the retailers were responsible for any uncashed rebates.

Years later, Sprint, a defendant in the Young America case, in an effort to move forward and avoid further bad publicity, settled with 36 states, including Iowa, for \$22 million in outstanding rebates. However, Sprint still denied the obligation to report the outstanding rebates at issue. Sprint maintained the obligation was Young America's to escheat.

Additional case law adds confusion concerning the true holder determination. In an on-going case, Costco Wholesale Corporation (Costco) filed suit against the State of Washington over the state's demand for approximately \$3.3M in uncashed rebate checks (*Costco Wholesale Corporation v. Washington State Dept. of Revenue et al.*, Washington State Superior Court for King County, No. 11-2-08830-8 SEA (3/4/2011)).

Costco used a TPA, Continental Promotions Group (CPG), to manage a rebates fulfillment program. When the Washington State Department of Revenue tried to determine the holder of the uncashed rebate checks, the state discovered that CPG declared bankruptcy in 2008. The state then demanded payment from Costco, asserting Costco was the true holder of the uncashed rebate checks because it was Costco's obligation to the customers to pay out the rebates. Costco paid the requested amount under protest and filed suit against the state. The outcome has not yet been decided by the courts.

Cases like this indicate both the aggressive positions states are taking with regard to TPAs as well as the importance of clearly defining where reporting responsibilities lie (i.e. who the true holder is) in the contract between the company and the TPA.

Holder instructions

With such uncertainty concerning who has the reporting obligation, what should the holder do? To mitigate the exposure for transactions in which the holder does not own the process, it is imperative to first understand where areas of potential exposure may lie. To gain understanding, a holder must look beyond processes it may currently have in place and get assistance from various parts of the business to determine where TPA relationships may exist.

For example, the following departments should be interviewed to gain a better understanding of potential TPA relationships:

- customer relations and marketing/promotions
- human resources and payroll
- investor relations.

As detailed below, an analysis of responses from each department should assist in discovering possible TPA exposures throughout the company.

Customer relations and marketing/promotions

The customer relations and marketing/promotions departments should identify any TPA relationships for consumer rebates, loyalty or reward programs, or refund programs and obtain copies of the most recent TPA contracts. The contracts should be reviewed to determine unclaimed property reporting obligations. Additionally, the contracts should be reviewed to identify how 'slippage' (i.e. uncashed checks) is handled and who ultimately retains those funds.

Human resources and payroll

The human resources and payroll departments should identify any TPA relationships for payroll and benefits programs and obtain copies of the most recent TPA contracts. The contracts should be reviewed to determine unclaimed property reporting obligations.

Additionally, the contracts should be reviewed to identify how uncashed checks are handled. Are the funds returned to the company? Are they reported? Is any follow-up conducted on outstanding items?

The company should also review any benefit plans covered under ERISA for possible federal pre-emption of unclaimed property laws.

Investor relations

The investor relations department should identify any TPA or transfer agent relationships for securities/equity-related property and obtain copies of the most recent contracts. The contracts should be reviewed to determine unclaimed property reporting obligations and the administration of shareholder accounts in cases of abandonment.

Since unclaimed securities are often subject to additional regulation, the company, its legal team, and the TPA should routinely assess whether state or federal law has been amended for compliance purposes. Any accounts ultimately requiring escheat should be documented with a listing of corresponding information including name, address, account number, holdings, and balances. The department should designate one contact person within the company to ensure unclaimed property reporting obligations relating to each TPA and transfer agent relationship are ultimately met.

Input from management, internal legal counsel, and the individual business units should be incorporated, regardless of the business function performed by a TPA. Effective policies and procedures related to TPA should address the following:

- a detailed listing of all TPA relationships including copies of the active contracts as well as any relevant contact information
- copies of unclaimed property filings, if the TPA is reporting on behalf of the holder
- periodic reviews for completeness of the information provided by the TPA

The takeaway

Companies are becoming more savvy regarding the various states' unclaimed property laws and are making great strides to become compliant. However, state and third party auditors are now pursuing areas that were often dismissed or overlooked during examinations in the past. Rather than merely looking at the usual property types handled in-house, companies must look beyond their own organization to determine if they may have a reporting obligation for property over which they have little control or visibility. Proactively determining where these hidden liabilities may lie and documenting the process to address these liabilities can save a holder further grief when an unclaimed property examination is initiated.

Multistate developments

While not fully inclusive of all developments in state AUP, the following provides highlights of some notable items.

California

[2013 CA 212, signed by Governor September 26, 2013](#)

This bill requires, beginning July 1, 2014, that a person holding escheated property include in his or her report to the Controller the name and last known address of the apparent owner of any escheated property, except travelers checks and money orders, worth at least \$25. The bill allows the holder to report information regarding escheated items worth less than \$25 in aggregate. The bill authorizes a banking or financial institution to impose a service charge for notice if the deposit, account, shares, or other interest has a value greater than \$2.

[Unclaimed Property Program Newsletter, California State Controller's Office, July 2013, revised August 22, 2013](#)

This newsletter was reissued to amend an article regarding the escheatment of custodial accounts. The article clarifies that if the holder is the named custodian on the account for the benefit of the owner, then property escheats three years from the date the account is payable or distributable to the beneficiary. Further, a financial organization may escheat funds only if the funds are held in a fiduciary capacity for the benefit of the owner.

[Controller Reaches Settlements with Transamerica, New York Life and 9 Others, June 7, 2013](#)

On June 7, 2013, State Controller John Chiang announced major, multi-state settlements with 11 life insurance companies over unpaid life insurance benefits. Under the settlements, the companies have agreed to make each of their policy beneficiaries whole, pay 3% compounded interest, and adopt business procedures to ensure full compliance with the Unclaimed Property laws in order to protect policyholders and their families. These multi-state settlements are worth up to \$763 million nationwide, with up to \$86.7 million going to California beneficiaries.

The agreements require the companies to do the following:

- restore the full value of all impacted accounts dating back to 1995
- fully comply with California's unclaimed property laws and cooperate with the Controller's efforts to reunite these death benefits, annuity contracts and retained asset accounts with their owners or, in many cases, the owners' heirs
- pay the policy beneficiaries 3% compounded interest on the value of the held amounts from 1995, or from the date of the owner's death, whichever is later.

Florida

[2013 FL S 492, signed by Governor June 14, 2013](#)

This bill provides that all intangible property and any income or increment thereon held in a fiduciary capacity for the benefit of another person under a trust instrument is presumed unclaimed unless the owner has, within 2 years after it has become payable or distributable, increased or decreased the principal, accepted payment of principal or income, communicated concerning the property, or otherwise indicated an interest as evidenced by a memorandum or other record on file with the fiduciary.

Illinois

[2013 IL S 1988, signed by Governor August 16, 2013](#)

Holder reports require certain identifying information for each person appearing in holder records to be the owner of presumed abandoned property. The value for such abandoned property that requires the reporting information is decreased from \$25 to \$5.

Louisiana

[2013 LA H 348, signed by Governor June 12, 2013](#)

This bill limits the time to bring an action against a federally insured financial institution holder of unclaimed property from ten to six years. According to current law: (1) holders are required to maintain records containing the information required to be included in the abandoned property report until the holder files the report and for 10 years after the date of filing, unless a shorter time is provided; and (2) a business association that provides traveler's checks, money orders, or similar written instruments other than third-party bank checks is required to maintain a record of the instruments while they remain outstanding, indicating the state and date of issue, for three years after the date the property becomes reportable. The bill requires a federally insured financial institution holder to maintain unclaimed property reports and maintain supporting records containing the information required to be included in the report for six years after the date the report is filed.

Massachusetts

[Feingold v. John Hancock Life Insurance Co., US District Court of Massachusetts, No. 13-10185 \(August 19, 2013\)](#)

John Hancock's practice of holding life insurance policy proceeds until receiving proof of the insured's death was challenged in a class action lawsuit. The plaintiff claimed violations of consumer protection statutes, unjust enrichment, conversion, a breach of fiduciary duty, and sought declaratory relief. The US District Court of Massachusetts dismissed all claims and dismissed the lawsuit.

Nevada

[2013 NV A 226, signed by Governor June 10, 2013](#)

This bill sets forth new provisions concerning establishing the identity and death of an insured or beneficiary and the payment of death benefits under a policy of life insurance, annuity, benefit contract or retained asset account.

North Carolina

[2013 NC H 257, signed by Governor July 18, 2013](#)

Currently, the Treasurer is required to gather certain information from holders prior to escheatment. This bill simplifies those requirements by merely stating that the Treasurer must maintain holder records with reported unclaimed property. The bill also limits the information that may be subject to public inspection. Additionally, the definition of property is amended to include money along with tangible personal property.

Vermont

[2013 VT H 95, signed by Governor May 21, 2013](#)

This bill creates a new Act that relates to unclaimed property life insurance contracts and provides that an insurance company must perform a comparison of its insureds' in-force life insurance policies, contracts and retained asset accounts against a Death Master File, on at least a semiannual basis, to identify potential matches.

Wisconsin

[Wisconsin Department of Revenue Tax Bulletin Number 181, August 2013](#)

Wisconsin announced that effective July 2, 2013, the administration of the Unclaimed Property Program has been transferred from the Office of the State Treasurer to the Department of Revenue.

Let's talk

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