

## **Don't Miss the Mail: Delaware Issues Unclaimed Property Letters**

by Joseph Carr and Anne Rachko

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In this installment of A View From the Windy City, the authors examine Delaware's voluntary disclosure agreement program.

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Delaware continues to send unclaimed property letters to entities nationwide that are incorporated in Delaware. The last set of letters went out around August 21, which state that recipients have 60 days to act upon the notice or face an audit by Delaware through its contract audit firm. With so many competing priorities businesses face today, most notably dealing with operational issues associated with the COVID-19 pandemic (for example, remote working, systems and people issues, and so forth), it is likely that an unclaimed property notice would not be a priority. However, failure to respond could result in a costly audit that can drag on for years. Thus,

we argue for participating in the Delaware voluntary disclosure agreement program (VDA) program when appropriate.

To start, and generally speaking, Delaware's VDA program in comparison to its audit program is best summarized below:

CATEGORY	VDA	Audit
Penalty & interest	Waived	Interest – 0.5% per month, max of 50% of unreported property; up to 50% may be abated; various penalties
Audit waiver	Audit waived unless misrepresentation or fraud	N/A
Lookback	10 report years (from date of enrollment)	10 report years (from date of audit letter)
Void waiver	90 days	30 days
Who conducts review	Self-review	Third-party audit firm (hourly/contingent fee)
Venue	Delaware secretary of state	Delaware Department of Finance
Timeline	2 years + extension	3-7 years
Estimation	Gross method	Gross method
Protest remedies	Withdraw from VDA or exclude property type from settlement – may be referred to audit – all remedies available upon demand issued	Informal settlement/litigation

While the above summary on Delaware escheatment programs is helpful to holders, many that have not received letters still ponder what to do should they receive one. To answer this question, it is important to understand:

- common escheat compliance misconceptions;
- companies with high-risk factors that should strongly consider the VDA program as a mitigating compliance option; and
- state of litigation.

### Common Escheat Compliance Misconceptions

The following are some of the more common misconceptions regarding Delaware unclaimed property compliance and risk:

- *I have low income tax apportionment in Delaware; thus, I do not have any Delaware unclaimed property* — false, the second priority rule operates as a throwback to state of incorporation,<sup>1</sup> extrapolation for periods without records;
- *I have little to no operations in Delaware; thus, I do not have any Delaware unclaimed property* — false, the second priority rule operates as a throwback to state of incorporation, extrapolation for periods without records;
- *The statute of limitations is like income tax, and therefore my risk is limited to three to four years* — false, Delaware's and many other states' lookback periods extend 10 to 15 years;
- *I have addresses for all years under our seven-year record retention policy and none of them are to Delaware, so I should owe nothing* — false, as Delaware extrapolates for years for which no records are available back to its full 15-year lookback period; and
- *I am in a net operating loss position, so I don't owe unclaimed property* — unclaimed property is not a tax; it is a financial obligation (expense) above the line.

<sup>1</sup> See generally *Texas v. New Jersey*, 380 U.S. 518 (1965) (holding in part unclaimed property is sourced first to the state of last known name and address on the holder book and records and then if none, to the state of incorporation or commercial domicile (for unincorporated entities) as a rule of administrative convenience).

### High-Risk Businesses

There are many factors that increase a business's escheatment risk profile, including:

- incorporated in the state of Delaware;
- located in other states with significant operations in Delaware that have not addressed or have underreported their unclaimed property with the state;
- never filed escheat returns in Delaware;
- filed little or \$0 escheat amount to Delaware;
- recently started filing escheat returns to Delaware — including past due property;
- never been audited by Delaware before;
- filed previous Delaware VDA or been audited but have additional entities or property to report for legacy or current periods; or
- acquired Delaware entities.

### Current Litigation

The following are some (not an exhaustive list) of the current cases in some phase of litigation that either in whole or in part challenge the constitutionality of the Delaware escheat program and more particularly the estimation calculation method:

- *State of Delaware v. AT&T Inc.*, DE Court of Chancery, Trans ID 64508991, Case 2019-0985 (Dec. 10, 2019). AT&T challenges Delaware's subpoena of records request through litigation and also raises argument made in prior Temple Inland case (due process violation, commerce clause violation, takings violation, and so forth); on July 10 the Delaware Court of Chancery issued an opinion in which the state's subpoena to enforce the production of records by AT&T was quashed.
- *Fruit of the Loom Inc. v. Geisenberger*, Case 1:19-cv-02273-UNA (Dec. 13, 2019). Fruit of the Loom quickly followed in filing suit after also being terminated from Delaware's expedited audit program and similarly alleges specific provisions of Delaware's unclaimed property law are in violation of numerous federal laws similar to Temple Inland case (case pending a hearing date at time of this writing).
- *Siemens USA Holdings v. Geisenberger*, Case 1:99-mm-09999-UNA (Dec. 17, 2019).

Siemens USA Holdings has also followed in filing suit after being terminated from Delaware's expedited audit program and similarly alleges that provisions of Delaware's unclaimed property law are in violation of numerous federal laws similar to Temple Inland case (case pending a hearing date at time of this writing).

- ***Eton Corp. v. Geisenberger, Case 1:19-cv-02269-UNA (Dec. 12, 2019)***. Eton, a Delaware incorporated public pharmaceutical company filed suit against Delaware after being terminated from Delaware's expedited audit program alleging that provisions of Delaware's unclaimed property law are in violation of numerous federal laws similar to Temple Inland case (case pending a hearing date as of time of this writing).
- ***Univar Inc. v. Geisenberger (Federal District Court) and State of Delaware Department of Finance v. Univar (Delaware Court of Chancery)***. Univar brought a procedural due process claim in federal court because Delaware is requiring Univar to submit to an audit by a private firm, Kelmar Associates LLC, with a financial stake in the outcome of the audit — it receives compensation based on the property calculated and escheated. At the same time, Delaware filed suit in state chancery court seeking to enforce an administrative subpoena requiring Univar to produce books and records as part of the audit. Although the district court did not dismiss Univar's constitutional challenges, the court exercised its discretion to stay the case until the Delaware Court of Chancery ruled on whether the state's subpoena of Univar's records is enforceable. On May 21 the chancery court denied Univar's challenge to dismiss Delaware's suit to enforce the subpoena to produce books and records. The court held that Delaware's suit was "ripe," but it still needs to address the merits of the subpoena. The chancery court also did not address any of Univar's constitutional arguments and instead will leave it up to the federal district court to address them.

## Conclusion

In conclusion, businesses that receive a Delaware unclaimed property letter should act promptly and seek advice from a competent consulting outfit. If you do not have high-risk factors or believe a letter was sent in error, you should contact the state to discuss being removed from the VDA program or negotiate a quick self-review to comply with the program guidelines. This has happened on occasion, and the issue can be resolved rather quickly in most circumstances (for example, no Delaware incorporated entities, only Delaware incorporated entity is a holding company, entity in question was sold, have de minimis revenue in reviewable entities, business filed bankruptcy, and so forth). This letter should not be ignored as it will result in an audit by the third-party audit firm that will likely include additional states, since the contracted audit firm has contracts with multiple states ("piggyback audits").

On the other hand, if you do meet high-risk factors or are unsure of your risk profile, you should seriously consider availing yourself of the VDA program for reasons outlined in the chart above. You can always exclude property types or entities from the program under regulatory guidance. To the extent those areas become subject to audit, all the work should have largely been performed, and all the remedies available under an audit should remain at the holder's election (including litigation like the cases noted above). So check your mail and take appropriate action steps to ensure your organization's escheat compliance mitigates its financial risk associated with any unclaimed property owed. ■